Q2 2014 Earnings Call

Company Participants

- Jeremiah Alphonsus O'Callaghan
- Wesley Mendonça Batista

Other Participants

- Daniel Sensel
- Eriko L. Miyazaki-Ross
- Farha Aslam
- Jose J. Yordan
- Pedro Leduc

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, everyone, and welcome to JBS' Conference Call. During this call, we will present and analyze the results for the second quarter of 2014. As requested by JBS, this event is being recorded. The recording will be available to listeners this afternoon and can be accessed by following instructions posted on the company's website at www.jbs.com.br/ir.

Taking part on this call, we have Mr. Wesley Batista, Global CEO of JBS; Mr. André Nogueira, CEO of JBS USA; and Mr. Jerry O'Callaghan, Investor Relations Officer.

Now, I'll turn the conference over to Mr. Wesley Batista. Please go ahead, sir.

Wesley Mendonça Batista {BIO 15243148 <GO>}

Thank you and good morning to all. Thank you much for being in our earnings call, our second quarter earnings call. I will turn the call to Jerry to go through the presentation and the highlights for the second quarter. And before we turn to Q&A, Jerry – after Jerry finish the call, I will make some more comments about our performance in the second quarter and our view about the business overall.

So, I'll turn the call to Jerry. Jerry.

Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Okay. And, Wesley, thank you. Thank you, Wesley. Good morning, everybody, and thank you, all, for being on the line with us today. We've put our presentation on our webpage this morning, and I just wanted to mention that we will be making reference to this presentation during this call and I will mention page numbers for those of you who are accompanying us.

Well, starting on page 3, the highlights on a consolidated basis for JBS for the quarter. We had BRL 29 billion in sales, BRL 7 billion greater than the same period last year, 32% sales growth. Our gross margin was BRL 4.25 billion, that was up BRL 1.3 billion, or 44.5% (sic) [44.3%] (02:10) in relation to the same period last year. And our consolidated EBITDA for the period was BRL 2.4 billion and that was up almost 46% in relation to the same period last year with an EBITDA margin of 8.4%.

Interesting just to highlight there that our revenues were up, 32%, but our gross profit and our consolidated EBITDA was up 44%, 45% in the same period. So, obviously, there is an improvement in operation. There is a better performance this year in relation to the same period last year.

Net income for the period was BRL 254 million or BRL 0.09 per share. It was impacted by two factors which we mentioned in our press release last night. Firstly, we paid – we prepaid 16 bonds, a portion of our 16 bonds. That cost us BRL 90 million. And we continue to maintain our position, our dollar-exposed position in Brazil hedge, which is an expensive exercise, but we think it's a prudent exercise in this environment. We think it's better to have this expense but to have – to be protected against currency variation.

Our exports in the period were up quite substantially, as well, up 45% in relation to the same period last year, and at $4.3 billion in exports on a global basis from JBS. That's almost one-third of our total revenue coming from exports of this growth in the emerging markets, where production is not keeping up with demand. And on leverage on a consolidated basis, our leverage, we ended the quarter at 3.15 times against 3.26 times at the end of the first quarter. And if we go back to the third quarter of last year, we were about 4 times after we've announced the relevant acquisition. So a big decline in leverage through the last couple of quarters.

Looking at the business units individually and making reference to page 4 in our presentation, which is available to you. So mentioning the highlights – at least, one highlight from each of the business units. And starting with our JBS Foods in Brazil, which is basically our poultry and pork business and all our prepared and convenience foods business in Brazil, which is a relatively recent business unit. We had more than BRL 3 billion in revenues in the period, and BRL 440 million in EBITDA, with an EBITDA margin of 14.3%. You might recall that we had an EBITDA margin of just north of 13% in the first quarter. So we've seen revenue growth in EBITDA and improvement in the EBITDA margin.

Our JBS Mercosul business, which is basically our beef business, our hide business and other related businesses in South America, Brazil, Uruguay, Paraguay and in Argentina, BRL 6.3 billion and sales in the second quarter. It was up 15.8% in relation to the second quarter of last year. And EBITDA of BRL 634 million with an EBITDA margin of double digits, 10.1%.

Our U.S. beef business, $5.3 billion in sales, that was up almost 11% in relation to the same period last year, and BRL 108-plus million (sic) [$108 plus million] (05:52) in EBITDA with an EBITDA margin of 2%.

And our pork business had revenues of just over $1 billion, $1.028 billion, 18.4% up on the same period last year. EBITDA was almost $114 million with an EBITDA margin of 11.1%. And then, finally, regarding our business unit, our poultry business in the U.S., Pilgrim's Pride Corporation, which was already reported, the almost $2.2 billion in sales, which was stable in relation to the same quarter last year. $338.6 million in EBITDA with an EBITDA margin of 15.5%.

Continuing in our presentation and making reference to recent events, which were announcements made by the company since the end of the quarter, basically in the month of July. We announced two acquisitions during that period of time, and I will briefly describe those acquisitions here. We announced the acquisition of Tyson in Mexico and Tyson in Brazil. And we also announced the acquisition of a local poultry producer here in the state of São Paulo close to the big consumption centers in Brazil.

Regarding the Tyson Mexico acquisition, $400 million, three vertically integrated processing units and seven distribution centers. $400 million was what we paid for that. In Brazil, Tyson, also three integrated poultry units, six distribution centers. $175 million was what we paid for that. And then the company in São Paulo state, it's called Céu Azul, two integrated poultry plants, three hatcheries and feed mills. All of this is subject to antitrust approval. And so this was an announcement made in the last month and subject to antitrust approval.

Tyson Mexico acquisition done in the name of Pilgrim's Pride Corporation and the acquisitions made in Brazil, Tyson do Brasil and Céu Azul made in the name of JBS Foods.

Now turning to page 7 in our presentation, talking a little bit about our exports. We already mentioned 45% increase in exports. Those are broken out by destination on a consolidated basis on page 7. So we see an increase in our sales in the South American region and a substantial increase overall in the sales, 45% up. And obviously part of that is due to the increase in our production capacity and export of poultry and pork products out of Brazil.

Now talking a little bit about CapEx and our debt profile, looking at our presentation from page 9 onwards. So firstly, on CapEx, we had BRL 760 million in CapEx between the quarter. About 40% of that is related to acquisitions, expansion and facility modernization and the balance 60% to maintenance.

And also, in the period, we record – we finalize the acquisition of convenience, prepared foods business here in the state of São Paulo called Massa Leve. That involves the transfer of BRL 203 million worth of share, JBS SA shares, which we held in Treasury plus the payment of BRL 55 million in cash, and that can be seen our statement of cash flow in the line 'net effective working capital from acquired companies.'

Cash generation was BRL 147.3 million in the period. And basically, cash generation was limited because of increased exports which requires working capital and increased capacity and increased pricing across just about all our business.

Debt profile on page 10 of our presentation. We can see the evolution of our leverage from the third quarter of 2013 coming from just over 4 times to just over 3 times at the end of the quarter. Our debt by currency 77% is in U.S. dollars. The cost of that has declined now to 5.67% per annum, and the balance in real is 23%, 11.25% annual cost of that debt.

We issued bonds at JBS USA. in the quarter, $750 million. Part of the proceeds we used to pay down all 16 (10:55). And so, again, that is the measure which is allowing us to extend our maturity curve and to reduce the cost of debt in dollars.

On debt – continuing on the debt profile on page 11 of our presentation. We ended the quarter with BRL 10.3 billion in cash and with $1.27 billion in fully available facilities in our JBS USA business.

If we add our cash position plus these available lines in the U.S. that represents 133% of our short-term debt. And the percentage of our short term debt in the period reduced from 29% to 28% of the total debt.

And just on our debt maturity also on page 11, we see that a good portion of our debt matures now to 2020 and onwards.

Okay. And then just briefly on each business unit, I'll go through this very quickly from pages 14 onwards. Page 14 is regarding JBS Foods, where we are, basically, the brands we have, the breakdown between domestic and export markets, and a good balance of the export markets that we are working with. The Seara brand is highlighted also in our presentation.

We've been increasing our market share with the Seara brand in Brazil and doing quite a lot of promotion and advertising around the brand. The results of that business unit, specifically, are on page 15 of our presentation. And revenue is up from BRL 2.8 billion in the first quarter to BRL 3.1

billion. EBITDA was up to BRL 440 million with an EBITDA margin of 14.3%, as I mentioned earlier. And so we see a constant improvement in this business unit.

JBS Mercosul, which is basically our beef business in Brazil, in Uruguay, Paraguay, and in Argentina, our Hides business which is quite a substantial business, and also other related businesses like biodiesel and other byproducts that we produce. Again, this is 47% exports, 53% domestic. Quite a lot of exports to Asia and to neighboring South American countries. And again, we have a very strong brand in our beef sector in Brazil, which we've been supporting and which we've been increasing our participation in the market.

Revenues of BRL 6.3 billion for the period. It was up 16% in relation to the same period last year. If we look at exports, they were up 22%. EBITDA was at BRL 634 million with an EBITDA margin of 10.1%. We see a lot of consistency in the EBITDA of this business, double-digit margin, very constant margins over the last five quarters.

Going to our U.S. business and starting with our JBS USA Beef business. And again, on page 20 of our presentation, we show the location of those businesses JBS USA in the U.S., our operation in Canada - up in Alberta in Canada and also our operations in the east coast of Australia. 28% of this business is export. 72% is domestic.

Because of our Australian exports to Asia, there's a big concentration of the exports into Asia. But also, a lot of sales into our neighboring North American countries and some - and a very recognizable brands, very specific brands like Aspen Ridge, Cedar River and the Swift, various types of Swift brands that we've got.

Revenue was up 11% in relation to the same quarter last year of $5.3 billion. We saw price increases domestically and in the export market. EBITDA was just over $108 million, 2% EBITDA margin. Cattle prices were up, prices were up as well. And we saw quite strong exports to Asia as I mentioned.

Our pork business in the U.S. Again, we are located in the U.S., three production facilities. 85% is domestic U.S. 15% is export. Again, exports are concentrated item in the neighboring North American countries or into Asia. And again, very strong brands and some high-quality products like our Dry Rubbed ribs and other pork items inside the U.S. market.

Revenue went from just under $900 million to over $1 billion quarter-on-quarter, up almost 19% year-on-year. We saw substantial price increases in the pork category. Wesley will comment about that business a little bit later. EBITDA was very strong at just under $114 million with an EBITDA margin of 11.1%. EBITDA was up 124% in relation to the same period last year.

And then finally, on the business units, just briefly on our Chicken business in North America, Pilgrim's Pride Corporation, we report the numbers right at the end of last month. So most of you is familiar with that business. Just a little bit about 80% domestic, basically 11% is our Mexican operation, 9% of exports. Again, a lot of those exports are out of the U.S. in to Mexico, so a bigger participation than actually what we produce in Mexico, with also some exports to Asia. This business posted revenues of $2.2 billion, which is pretty stable in relation to the same period last year, but a big increase in EBITDA. EBITDA was up to $339 million, with an EBITDA margin north of 15%. So we saw - and besides reduction in feed price, we've seen efficiency improvement across this business which was responsible for that very strong EBITDA in this business unit.

So that finalizes our presentation today. And I'll pass you on now to operator then Mr. Batista to make some further comments before we open for Q&A. Thank you very much.

Wesley Mendonça Batista {BIO 15243148 <GO>}

Thank you, Jerry. I will go through some price (17:18) to summarize some key points here on this quarter. So, Jerry already mentioned these points, but very good top-line growth of 32%, this quarter compared to the same quarter last year. Very strong gross margin expansion. So, we expand 44% of our gross margin this quarter compared to the same quarter last year. EBITDA, the same thing, 45% expansion in EBITDA this quarter compared to last quarter. So, clear demonstration that gross margin and EBITDA is growing more than our revenue, so we did 32% growth in revenue, but the gross margin and EBITDA expand 44% and 45%.

So, good quarter in all these fronts. So, net income, so we lift net income based on two factors. So we did BRL 254 million in net income, affected by BRL 90 million. That is a one-time event, the premium that we pay on 2016 bond, so this impact our financial cost in $90 million. And also the cost to carry the hedge on our dollar exposure so, we are fully hedged, so this is costing us, but due to the political scenario in Brazil, we strongly believe that is the most secured thing to do now even though it's costing quite a lot.

Leverage, we'll keep deleveraging our balance sheet. So, since we are now in (19:26) acquisition, we have then mentioned to the market that we are going to finalize 2014 at around 3 times leverage and we are well positioned to even close this year below 3 times leverage.

Export, very strong growth, 45% growth you see this quarter compared to last quarter. So we have seen a very strong demand in a lot of different markets. China is a big, big demand especially for beef. A lot of emerging markets, very strong export demand.

Talking quickly here about each business units. So JBS Foods, that is our chicken-prepared food and pork business in Brazil. Last year, we announced BRL 1.2 billion in synergies that we are going to capture this year. We are ahead of this number. We already captured BRL 700 million in this first half of 2014. So in a run-rate base, we are looking for a BRL 1.5 billion instead to BRL 1.2 billion. So ahead of our initial guidance in terms of synergy for our JBS Foods business. So 14% margin EBITDA and extending the margin comparing to the first quarter. So we are very satisfied where we are going with this business.

So our Mercosul business, that is the beef, the hides in Brazil or Argentina or Uruguay and Paraguay is going well, Stable business. They're forming double-digit margin around 10%, and we keep satisfied where we are and where we are going in this business. And we have seen, again, very strong demand in export. You all know Russia open out the beef plants in Brazil, chicken and pork plants in Brazil. This is going to benefit our – and as well, China. This is going to benefit our beef business in Brazil.

So, the beef business in North America, moving to North America, the beef business in North America last year and in this first half of this year definitely was the most challenged business in our whole company. But we are seeing improvements in the beef business in North America. In the last 12 months or more. A year-and-a-half, we saw five plants that shut down in U.S. and that definitely is going to help to balance the supply and the industry capacity to be much balanced that we – we are fortunate that we are going to see good improvement on the beef business.

We are looking for a much stronger third quarter on this segment. We are already in the middle of the third quarter, and we are seeing very strong improvement on our beef business in North America, Canada, and Australia's performing really well.

So, our pork business, a stable business, we have been performing really well on this business. It's a benchmark in the industry in U.S. So we did over 11% margin EBITDA and again, we look very – we are very confident that this business will keep performing in a double-digit margin. The third quarter, we look for even a better number than the second quarter.

So finally, Pilgrim's Pride and we have already reported the number, did very well, 15% margin EBITDA in the second quarter. The business is performing extremely well. Pilgrim's today definitely is a really, really well managed company. When we are satisfied about the results but even more when we compare ourselves look in the agri stats number and the surveys that we can compare our profitability in this business compared to the industry, Pilgrim's is performing really well. It's inside of the best companies in terms of profitability in the U.S. So we are very satisfied.

We are looking for a very strong second half of 2014. Again, third quarter is going actually ahead of the second quarter comparing to the same period. So we, again, look forward for even stronger third quarter comparing to the second quarter. Grain price in U.S. declined and definitely, this will help margin. So we are very satisfied on where we are.

So overall, we are looking for, in a consolidated base, we are looking for stronger third quarter, stronger than the second quarter and we are satisfied with our structure. We are very pleased about our management team.

We have been working really, really hard on things that we control, being better in cost, being better in product mix, being better in all the pricing strat (25:47). And so we are very satisfied where we are going with JBS overall.

So with that, I will turn the call to the operator to open for Q&A. Thank you.

Q&A

Operator

Ladies and gentlemen, we will now begin the question-and-answer session. Our first question comes from Farha Aslam with Stephens, Incorporated.

Q - Farha Aslam {BIO 6151888 <GO>}

Hi, good morning.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Hi, Farha. Good morning.

A - Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Hi, Farha.

Q - Farha Aslam {BIO 6151888 <GO>}

I have a question on Hillshire and your decision. You've decided to pass on Hillshire due to valuation. But kind of going forward, could you share with us your interest in growing in the U.S. and, particularly, your interest in branded food businesses in the U.S.?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

So, Farha, yeah, exactly what you mentioned. So we participate on the Hillshire deal. So we went until we're – where we were seeing value creation for us and we kept disciplined. And so Bill Lovette, he mentioned already that we keep looking opportunities. We would like to expand our business in North America. Branded and packaged food products is an area that we are looking for. It's not the only area that we are looking for.

For example, we announced the acquisition in Mexico. It's a very strategic acquisition for Pilgrim's Pride, where we already have a strong presence. So overall, Farha, in Pilgrim's and in JBS, overall, we'll be looking opportunities in North America and South America in the chicken, pork and the prepared food business. So, if we see opportunity that correct value for our shareholders, we'll be analyzing.

Q - Farha Aslam {BIO 6151888 <GO>}

Thank you. And just as a follow-up, you had mentioned briefly Russian trade bans. How do you anticipate that impacting your business, and how do you anticipate global protein flows to change as a result of that?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

So far, a very few impact in Australia, so we don't export a lot of products from Australia to Russia and as well in North America. And overall, beef, chicken and pork, very, very small volume is going to China – to Russia, sorry. Some more leg quarters go into Russia compared to beef or pork. So very, very few impact in our business. And, actually, we don't see any impact – it's not very few. We don't see any impact in our business in North America or Australia. And it's very beneficial for Brazil, overall, but much more because the restriction on Europe than the restriction on North America, because Europe export much more volume especially in pork to Russia than North America. So overall, very positive for JBS overall.

Q - Farha Aslam {BIO 6151888 <GO>}

Great. Thank you very much.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Thank you.

A - Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Thank you, Farha.

Operator

Our next question comes from Daniel Sensel with JPMorgan.

Q - Daniel Sensel {BIO 16854713 <GO>}

Yeah, I've got – hi. Good morning.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Hi. Good morning.

A - Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Hi, Daniel.

Q - Daniel Sensel {BIO 16854713 <GO>}

How are you, guys? So quick question again about Hillshire and leverage, right. You mentioned that the company, it's on track to be below three times. However, if the Hillshire acquisition would have gone through, then leverage would have been much higher than 3 even close to 4. So are you guys still looking for a big acquisition or these acquisitions that you just mentioned that you're looking are much more?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Daniel, first of all, you are right. So when I mentioned that we are on track to be below 3 times leverage, this is without a big major acquisition. So we try Hillshire - we thought that Hillshire was quite a unique opportunity in the U.S., great company. And so we kept where we were seeing value and there was a very unique opportunity. So we were - if we have done Hillshire, yeah, you are right, our leverage was going to be 4 times again.

But without acquisition, a major acquisition, we'll be below 3 times. And when I mentioned that we are open to look opportunities, this doesn't mean that we are looking. So we are not involved or engaged in any large or big acquisition. We are not analyzing any major acquisition. So we don't see actually real risk, we don't see anything big coming as opportunity for us to look. So even if we do some acquisition in a smaller scale, like we did Tyson, in Mexico and Brazil, this will not impact our leverage overall, and we will be able to be 3 or below 3 times leverage by the end of the year.

Q - Daniel Sensel {BIO 16854713 <GO>}

Okay. Thank you.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Thank you.

A - Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Thank you, Daniel.

Operator

Our next question comes from Mauricio Martinez (32:08) with GBM.

Hello, everyone. Thank you for taking my question and congratulations on the report. I was wondering, if you can give us a more - I was wondering if you can give us more color on derivative losses, and if we should expect higher losses than current level or maybe such losses should normalize.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Actually, it's not that low. It's in fact, the result of course because this caused us to hedge our exposure. It's not a derivative loss, it's the cost to hedge our exposure in dollar. And it's our option, we can hedge or we cannot, so we have been hedging our exposure to the political scenario in Brazil, we feel that is the insurance that is costing us over BRL 300 million, but at this stage, we believe we prefer to know the cost of this insurance than to run a risk that we can see the real tomorrow (33:29). I'm not saying that we, I'm not saying that we - our view is that the real will jump back. We prefer to lower the cost than to wake up and you see the real at 3, at some point, that this can cost billions in our company in terms of exposure. So it's a decision that we are taking to pay this cost to not run a risk on the currency.

Q - Operator

Great. Very clearly. Thank you.

A - Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Thank you, Mauricio.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Thank you.

Operator

Our next question comes from Jose Yordan with Deutsche Bank.

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

Hi. Good morning, Wesley and Jerry.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Hi, Jose.

A - Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Hi.

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

I had a follow-up on this last question. Because of your – I mean, Brazil, your global exposure, you have a natural hedge and you can translate more of those dollars – dollar liabilities outside of Brazil and just have it be hedged naturally. Is there any effort right now to make that happen, to lower the dollar exposure in Brazil? If you can tell us what the actual dollar amount is would also help and then I have another question on the U.S.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Yeah. Our exposure is around $5 billion. This is the amount of exposure that we have. And yeah, we, the way to mitigate this is to reduce our dollar exposure in Brazil and we are going to look and we are looking. So, we would like to have the debt – dollar-denominated debt in U.S. and in Brazil, more real-denominated debt. So, we are looking to shift this to U.S. more dollar-denominated debt and more to Brazil more real-denominated debt. So, this is the best way to mitigate this.

When you say natural hedge, look, this is a very complex conversation because some people in Brazil are here, some companies are saying that they have natural hedge, and we have a hard time to believe that anyone has a natural hedge. Why? Because if the real tomorrow jump to a higher or becomes weak, it's hard to say that you'll have a natural hedge because you can run a risk that the sales price, internationally, and because the attractiveness of the export will decline. So, if this happens, you are not natural hedged.

So, overall, again, this is a quite difficult analysis. Each one has different view on current exposure. For us, at this point, we have election in Brazil in a couple of months. At this point, we prefer a big cost – we prefer to pay this big cost, but we prefer to know how much is the cost to not run any risk, instead, to be open on the currencies.

So, this can change. We can change all our minds. So our board thinks in that way as our executive team think in that way, and we are keeping this hedged. So of course, this is impacting our net income plus the BRL 90 million that we paid on the bond impacted our net income. But for this stage, we prefer to lower the cost.

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

Totally agree that conservative is better. And my second question is on the U.S. I mean, I see – I hear your comments about the plant closing, et cetera. But is it the only reason why the inflection point in margins in the third quarter or is there something else behind that? I'm talking about U.S. beef now, right? And I mean, how sustainable is it into 2015? I mean, what would be your – if this turn is really more sustainable, what kind of margins can you see in this business in 2015 and what's the status of herd rebuilding? I know we've seen early stages of herd rebuilding but it takes a while to do. I mean, are you more or less bullish on that prospect than you were in the last call?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Well, look, Jose, a couple of things that we are more optimistic about this business in the U.S. First of all is of course the industry adjusting capacity is a key factor. Five plants closed in the last year and a half. So this took almost 8,000 heads per day out of the market. So for sure, this is a key factor to help balance the industry to have a better margin and a better result.

But not only that, export is growing overall. So we are seeing a strong demand in China. So we believe we will see less meat – less beef available in the U.S. and this also helps sales price. So, overall, and also, our Canadian business, we are making good improvement there. Our regional and our feed (39:32) business in U.S. as well we are – we did some change and we are very opportunistic about where we are going with our beef business.

So, you said exactly right. So we are in the early stage in terms of the herd expansion. But in our view, the worst fears on the beef business is behind. I think the second half of this year will be better and I think 2015 will be better, and I think 2016 will be a very good year for the beef business in the U.S.

So if you ask what is the normalized margin that I think we can see in this business, look, we feel that this business is not reasonable running a beef business in U.S. and a competitive industry and not making at least 5% margin EBITDA. So we are well behind 5%. But like I mentioned in the beginning, the third quarter will be much stronger than the second quarter. We're already in the middle of this third quarter, so the third quarter we will be well, better than the second quarter.

So, overall, we are positive. I'm not saying that we believe this business will jump for 7%, 8% margin. I'm saying that I believe our second – the second half will be far stronger than the first half. And the coming years, 2015 and 2016, we will see improvement due to these factors, export and the plant closure in U.S. are just the capacity and the supplies.

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

Okay. Very clear. Thank you.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Okay. Thank you.

Operator

Our next question comes from Pedro Leduc of JPMorgan.

Q - Pedro Leduc {BIO 16665775 <GO>}

Hi, everyone. Thank you for taking a question.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Hi, Pedro.

Q - Pedro Leduc {BIO 16665775 <GO>}

Hi. A bit different one and regarding the Pilgrim's acquisition of Tyson's poultry assets in Mexico. Once approved by the antitrust, you'll probably become as large as the current leader there. But it's a little bit of a different market than you currently operate in. It's a net importer of poultry, net importer of grains, and it's a market that seems to value fresh protein a lot more than processed.

So could you guys help us elaborate a little bit on the rationale for this acquisition and the long-term potential you see there? And what should be the JBS strategy in this country from now on?

Thank you.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Okay. So, first of all, Tyson has a great business in Mexico. They have been operating this business, I think, over 20 years. And they have a strong operation there. They do very well in Mexico. So it's a well-run a business that we are going to acquire. So the huge amount of synergy we follow our business, Fabio, our CFO in Pilgrim's, mentioned in the earnings call with PPC the amount of synergy that we believe we can capture on this acquisition.

And, again, Mexico is a net importer in chicken and a net importer in grain, but it's a huge consumer market for us. And we believe being in Mexico, the market is growing in Mexico, in our view. Demand is a very, very strategic move for us and PPC already have a strong presence in Mexico. And combining the Tyson and the Pilgrim's Pride operation, we see a lot of synergy. We see synergy in costs. We see synergy in operation. We see synergy in division and sales. So in our view, it's a very strategic and great, great move for Pilgrim's and also buying a business that is a good business that Tyson built over these past many years and is well managed already, a well-managed business. And we see opportunities to even expand margins further and do the synergies that we believe we can capture.

Q - Pedro Leduc {BIO 16665775 <GO>}

Very Well. Thank you.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Okay. Thank you.

Operator

Next question, Mr. Eriko Miyazaki-Ross with Barclays.

Q - Eriko L. Miyazaki-Ross {BIO 15385970 <GO>}

Hi there. Congratulations on a great quarter, guys. A couple of questions, if I may.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

Thank you.

Q - Eriko L. Miyazaki-Ross {BIO 15385970 <GO>}

With regards to the JBS Mercosul and the U.S. pork divisions, and obviously, very strong margins this quarter. I'm just wondering if those levels are sustainable going forward, particularly within the pork division.

And then, with respect to the Russian sanctions, are you able to potentially quantify the impact that might have on your LatAm operations?

And then, finally, are you able to give us an update with regards to the potential opening of the U.S. to Brazilian beef and any potential impact that might have?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

So, let me start with your first question. So our pork business, again, I mentioned in the beginning, we have a very strong core corporation in U.S. for a long time. It's a well-managed business. We – it's already three quarters consecutive that we are around 10% margin EBITDA. So we did 9.5 and 9.2 and now 11, and what I can tell you that we believe this is sustainable and that actually, I think, we can see some improvement in the third quarter compared to the second quarter, in terms of margin percentage, in a percentage base.

So, I think it's sustainable. We have seen good demand for pork. So, we have seen much less beef available in U.S. so big decline in beef production. But it is very beneficial for chicken and pork in the U.S. So, we believe that these margins can sustain, going forward, for pork.

So, on the South America question about our view, when you ask if we're open to Brazilian beef, look, it's hard to say this is the beck and call (46:42) discussion. The USDA is analyzing and is going through a process. We believe, in some point, Brazil will be able to access U.S. and I think Brazil has quite good beef to serve U.S. in terms of trimming, we have lean meat in Brazil, and the lean meat in U.S. actually is going quite short in terms of supply, lean beef to the hamburger industry. So, we believe at some point U.S. will open to Brazil. To say when, it's hard. Look, I don't know. Maybe from here to the end of the year, to the beginning of 2015, I think is possible.

So, on the Russian, it's very beneficial for our business in Brazil. Russian opened out a pork less (47:44) chicken and beef, and this will be beneficial to our South American business. We do between $600 million to $800 million, actually, we believe we can increment by between $600 million and $800 million in sales in Russia to our South American operation.

Q - Eriko L. Miyazaki-Ross {BIO 15385970 <GO>}
That's incremental sales?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}
Yes.

Q - Eriko L. Miyazaki-Ross {BIO 15385970 <GO>}
Okay, I'm pretty sure that you're expecting margins to stay pretty stable in the kind of double-digit context?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}
Yeah, I believe so.

Q - Eriko L. Miyazaki-Ross {BIO 15385970 <GO>}
Okay. Great. And then last one, sorry to take up your time, JBS Foods, obviously, fantastic margins again this quarter. Are those sustainable levels? I mean, I think you'd initially guided that you'd hope to reach kind of low double-digit and, obviously, surpassing that somewhat and just wondering is that something that we can expect to continue?

A - Wesley Mendonça Batista {BIO 15243148 <GO>}
Yeah. You can expect that this will continue and, actually, we are not satisfied. We believe we have more things to do.

Q - Eriko L. Miyazaki-Ross {BIO 15385970 <GO>}
Fantastic. That's great. Thanks very much.

A - Wesley Mendonça Batista {BIO 15243148 <GO>}
Okay. Thank you.

A - Jeremiah Alphonsus O'Callaghan {BIO 19817115 <GO>}

Thank you, Eriko.

Operator

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

A - Wesley Mendonça Batista {BIO 15243148 <GO>}

So, I'd like to thank you all for being in our earnings call this morning and look forward to talk again with great numbers in the third quarter. So thank you very much. Have a good day.

Operator

This concludes JBS audio conference for today. Thank you very much for your participation, and have a good day.