Q2 2010 Earnings Call

Company Participants

- José Antonio do Prado Fay, Chief Executive Officer
- Leopoldo Viriato Saboya, Financial and Investor Relations Director

Other Participants

- Alan Alanis
- Analyst
- Gabriel Lima
- Jose Yordan
- Marcel Moraes

Presentation

Operator

Good morning and welcome to BRF Brasil Foods SA Second Quarter 2010 Conference Call.

This conference call and the presentation are simultaneously transmitted via webcast in our website, www.brasilfoods.com/ir. At this time all participants are in a listen-only mode and later, we will conduct a question-and-answer session. Instructions will be given at that time. We would appreciate if each participant made only one question. [Operator Instructions]

Forward-looking statements are related to the company's businesses, perspectives, projections, results and the company's growth potential are provision based on the expectations of the management as to the future of the company. These expectations are highly dependent on market change, economic conditions of the country and the sector and international markets, thus are subject to changes. As a reminder, this conference is being recorded.

At this conference are Mr. José Antonio Fay, Chief Executive Officer and Mr. Leopoldo Saboya, Chief Financial Officer and Investor Relations Officer. I would now like to turn the conference over to Mr. Fay. Please sir, go ahead.

José Antonio do Prado Fay

Good morning to you all. We will show -- we will talk about the second quarter results of Brasil Foods. The second quarter shows the trend of a consistent improve in results in

Brazil. We had a quarter with good sales volume and better margin performance driven by sales volume. The margin performance were driven by volume and cost reduction.

When we analyze internal and external markets. In the external market we can see the volume that improved 10%, but the volume, the dollar price and the FX rate, also we reached the same gross sales in cash. It was much better in margin due to cost and the higher volume and then we can go in details after.

For domestic market, we keep on seeing a consistent performance in volume and to add the competitive scenario keeps on strong in competitiveness. We had good volumes and we had better margins, but prices were little down during the period. We got into EBITDA margin, we reached the two digits 10.6, which is close to the historic one; we are reaching the historical levels of EBITDA margins. And we can consider that the quarter was good in cash generation.

We have a good operational cash generation decreased in the net debt and reaching the ratio of EBITDA net debt 2.5, which is keeping going down.

Now, Leopoldo can explain in detail what we are talking about.

Leopoldo Viriato Saboya {BIO 16137418 <GO>}

Thank you, Fay. So, good morning everyone. So, let's analyze in a little more detail, the highlights of our performance in this quarter and talk a little bit about our main perspectives for the year-end.

So on slide five, we can follow our results, so first of all, talking about the second quarter and then we make some highlights of the first half. So first of all, related to the top-line, the gross sales in five nation, we reached at R$6.3 billion in gross sales, 4% higher last quarter. And a very good performance into the domestic market in terms of sales. We also buy for us as denominated and other process goods that increased 6.7% in volumes with flat prices. And the remaining growth came from there basically.

Flat revenues for exports, because of the fact that five nation. But with a very good performance in terms of volumes and in terms of profitability as we will see ahead. And we reached a very good expansion on gross margins, coming from 23.4% of the net sales to 27.4% this quarter, so on an expense of 400 basis points.

In terms of operating expenses, the SG&A, we had also a 40 bps reduction coming from 20.7 of the net sales to 20.3% of the sales in this current quarter, which reached the EBIT at R$393 million 174% higher than last year and a net income of R$132 million that compares with a R$476 million last year bolstered by FX gains. In that time, Sadia had a very larger balance sheet exposure, which is now settled.

The EBITDA, we batted to the two digits, 10.6 compared to the 7.2 last quarter. And also to get this net income of R$132 million, we had financial expenses of R$170 million, I'll give more details further on this presentation. And other operating expenses of R$71 million and the majority of this amount is due to the idle capacity in the system of the pre-operational idle capacity basically.

The results of the first half, I would emphasize what we have achieved in terms of the profitability measured by EBITDA, so we were above R$1 billion. 9.8% margin with a 440 bps increase compared to last year.

So moving on our next slide, we can see the breakdown of our sales, in fact no big change of what we have last year and average of the full year '09, so nothing to comment on here, the export accounting for basically 42% of the sales and the net market, 58% of the sales, the very same figure of last year.

Now analyzing a little more to volume prices and trying to understand what is boosting our profitability in a quarter-over-quarter basis and also in quarter-to-quarter basis, let's move to the next page, slide seven. So first of all the domestic market analyze it the meat, poultry and the dairy. The domestic market as a whole, we increased the profitability, but the majority came for the meat division because dairy in comparison last year it was a poor results. In terms of volumes in the meat domestic markets 7.5 were higher volumes with a decrease in prices of 1.19% which lead to a 5.4 growth in terms of gross sales.

I would emphasize that in the category mainly processed marinated and order process compounding all the processed meat products, we have a flat prices, so meaning in line with that we faced the competitive environment that with a reducing cost scenario lead to these market behavior and at the same time we could boost our margins by a lot compared to last year.

And in dairy, we reached a very bold increase in terms of volumes 17%, but it was a mix effect that produced much lower average price than last year. So this 17% is concentrated on the growth at around 25% quarter-over-quarter. And the profitability measured by EBITDA margins and these are specific segments reduced quite a bit compared to last year not because this year is best for, but because last year was very, very high margin scenario in this specific quarter last year.

But in summary the domestic market as a whole boosted margins in a little more than 300 basis points compared to last quarter last year. In a quarter-to-quarter analysis, it is likely better than the first showing that the domestic market is reaching a very good performance although we keep on seeing opportunities in the future for margin expansion.

In terms of the export market, we have this almost 10% increase in volumes, which is quite good for the market as we are same and especially after the so many disruption than collateral effects because of the prices, international prices, but and we could reach a 4.5 increase in prices -- in U.S. dollar prices, but coupled with the real appreciation at around 14%, we had a pretty flat scenario for gross sales.

But this time that we could reach a 600 basis point of margin expansion quarter-over-quarter and in a quarter-to-quarter basis, we also reached some at around 400 basis point expansion, which explain in the majority the EBITDA margin expansion from the first quarter to the second quarter that we are seeing. So, this is in a nutshell what we can analyze about volume and prices.

Looking now next page, on page eight, because this is the expression of this better profit at around 400 basis points better this quarter, apparent of that is due to a conjunctional factors like corn and soybean much lower than last year in average in the 20% area, so corn is little bit lower than that, some 15% lower than last year and soybean milk it's around 25% lower in the quarter, domestic market compared to last year help us to reduce our costs and a part of that is of course resulted of a much better performance with normalizing volumes and normalizing demands. So, we are now have an operating expenses according our business plan.

Looking into a little more details to SG&A, we could save 30, 40 bps and also including in that account, the 30 bps expenses of -- pre-merger expenses that accounted for around R$22 million in the quarter, in the year-to-date we are in a R$35 million in that line, which has to do with IT consultant pre-merger expenses with other consultants and other work that we need to do before capturing and synergies.

On next page, page nine; we can see the evolution of EBITDA margin, so more of what we have been talking to you of gradual and consistent margin expansion forward our business is due to the margin.

Moving forward, on page 11, so a little more color on the main drivers of our segments. First of all, propane on top left, we can see that after our -- rules on top prices. In the last quarter, prices stabilized in these $2.5 per kilo areas, but in terms of an average, it was 9% higher than first quarter whereas the chicken is pretty much stable in the short term, but with the 12% higher prices compared to last year.

But why do they think -- is because of research on seed prices remain weak because of the big drop Russian corn and some other European Eastern countries, we are seeing in fact which prices are skyrocketing and which is resulting increases of corn and soybean prices as well and this is of course especially margins of the all the province segment in which we are seeing opportunities for as on prices right now.

As you can see here at the bottom of the grants -- so you have here the curves of soybean and corn. You can see that two quarters compared to last year, we have reduction both corn and soybean, but when we compare, short term is flat as I mentioned, but right now has a very sharp increase and just for you to have an idea comparing the ending of June to August until now we are having 59% higher with prices absolutely because of 25 million funds shortage of wheat basically in Russia, which is very supportive for all the grain, the wheat grains in the world.

Looking on the right part of the chart, you can see all this is still my fact, but look on the bottom on this box the comparison on prices paid to producers. You can see that with a

17% higher prices compared last year, but when you compare second quarter to the first quarter, we paid 22% higher prices due to a shortage of milk, because of climate conditions and other stuffs, which of course pressured our margins as we could not pay down the prices, especially of crude milk like UHT.

So the perspective is for these circumstances to stay at least improve at year-end. In terms of U.S. dollar, we are seeing at least seeing September, October last year a little stable scenario in a range of 175-185, which is pretty good for us. We used to say that we don't have a preferred dollar range, but though a stable dollar, which is very good to us and we are seeing our in respect of that.

In terms of market share, next page just to show you that this is the current picture of our market share year-to-date and it's pretty stable in both fields, in the mid-term when we look year-over-year compared to last year and also on the short-term field, which means month after month Nielsen figures; it's pretty stable in terms of volume.

Next page, just taking a look at export variation, so there is no big changes in the breakdown of sales internationally and now we will pick the advantage of these chart to give you some update of every region, every main region we are exploring right now.

In the summary, I'll say that international markets performing quite well nowadays. There is no big inventory, no big surplus or it starts the off products in the majority of the regions we deal with and remarks are Far East, basically Japan, we are looking at adequate inventory levels and good demand for Brazilian chicken and good margins year-to-date. Eurasia, it's Russia basically import very positive volumes for prices due to the skyrocketing -- scenario and traders tend to bid up inventories for the year end and because of the scenario of the cost is going up. For chicken, we profit from the shift of around 150,000 tonnes of chicken from U.S. to Brazilians.

Other countries is, I would remark Africa, in which we are seeing good demand for the next quarter and the cover of the good demand of next quarter in Russia, we are seeing a more supportive market for Africa in the second half. In Europe, after a big long period of lackluster margins and lackluster demand, we are now seeing a more stable market with good demand due to summer, so there is a positive similar effect for chicken, basically, and this pretty same story of Russia of higher cost of -- is right now boosting chicken breast -- fresh chicken breast at the market. So prices are going up and we plan to take advantage of that scenario going forward.

So moving to -- I forgot to mention about the Middle East, sorry. In the Middle East, we now see a really normalizing pipeline, no more over supply in the region. We tend to see better prices in the second half, also punctually, we are seeing good demands from Iran and good perspective for Egypt due to the new agreement, which takes lower tariff.

Now we move to the investments and investment profile, first half we reached a total investment of around R$402, splitted in R$241 million pure CapEx and R$161 million investment in breeding stock. And the guidance for the year is the very same of R$1 billion total investment.

Looking to the debt profile, we ended the quarter little below R$4 billion of net debt and the ratio to EBITDA 2.4 times coming down since last year and approaching quickly the two times area in which as we felt last quarter we believe to have that before year end, and the two times area is what we consider to be a good ratio for the company looking to the long term.

Also I would comment that the long term debt non-current accounts for 75% of our total debt, which is pretty good and with a very good maturity above two years.

Now we are going to see two slides that we brought at this time, in this quarter to explain some literally -- changes and important one to comment to you, which is related to our balance sheet FX exposure. In exposure in the past in a pro forma basis. Second quarter '09, it was almost $3 billion and after all the liability management with this after year, we stabilized this exposure according our internal risk management policy in the level of 1.1 billion.

It was the same story until last quarter. And this quarter we are publishing only $154 million of exposure and the change is reason being basically two ones; the first is on cash generation during the quarter and we use that cash to down pay U.S. Dollar debts. And the second is due to a new international conference thunders rule in this migration to IFRS, there is this so called Brazilian CPC-38, where there is a treatment for hedge accounting, so a special accountability for this type of instrument, which means that you can designate an export prepayment facility like we have placed in our balance sheet to designate as hedge accounting. So, we did that by 1st of June, designated little more than $0.5 billion of this type of facilities. So meaning that from now on all the FX effect of this amount with the MTM will be in our balance sheet in the network of the company, but not in the P&L, the monthly P&L or the quarterly P&L.

We are only going to see the effect of that when you have that portion of debt matured according the revenue we exported. So, the FX effect will be much more according to the cash flow and not the accounting movement quarter-over-quarter.

So that will help us to understand the next slide. This is just to say to you that from now on the U.S. dollar effect on our P&L based on the balance sheet exposure will be reduced. Now, we took advantage on this quarter of this conversation to explain or to give -- to bring here what we publish in our notes regarding the breakdown of financial expenses. So first of all, understand the first half breakdown of the R$326 million, total financial expenses that breaks down like this: 177 is interest, which is basically the result of average net debt of around 4.2, R$4.3 billion at 7.5 coupon average and some other banking costs and...

This FX effect of R$83 million is basically the result of our fixed sales real depreciation from quarter to second quarter, quarter last year as fourth quarter last year to second quarter this year. The $0.06 by $1.1 billion of exposure that you saw in the last slide and on top of that you must add some R$12 million of the -- amount of 511 million that will be designated as hedge account on 1st June at 183 -- benefit let's say from this job on FX until the end of the quarter.

So, by saying that, this was the U.S. dollar effect and this 61 million that we call as investment conversion is basically the effect, the euro effect during this period from first to second quarter of the international holding companies established in Europe, so this loss is reflect basically the euro depreciation over the capital invested through all the time. As you know, from first to second quarter, we had pretty stable FX scenario, real to dollar but up to -- phase appreciation of real compared to euro. So when it happens, we have these kind of the losses, but right now as euro is appreciating again this effect this is back.

As we can see the majority of these results of the Europe is concentrated on this second quarter. So, having said that, let's move to the end of the presentation just showing to the shareholders composition, wheat has no change, but the -- appears here as higher than 5% that we need to disclose and the other participants very much keep on the same participation.

Most administrative volume, next slide 94% higher than last year in terms of -- analysis in a year-to-date analysis it's much higher growth because we reached a $53 million per day.

Now, from launches of the company, Batavito, which is a brand name from Batavo is a line of products fermented milk, this is a launched for teenagers, youngsters and here the -- the cheese, the kind of a cheese queen is very popular here for winter times, the new product from Batavo. On the bottom right, I want to highlight that because the name in Brazil, but it's a very popular dish here in Brazil, very good one. And Brasato; it's a high end...

So having said that, I leave here as a final message the combination of the market in terms of some awards we got in this period and I would highlight the first one and we were considered among 500 companies in Brazil, the best company from IstoÉ Dinheiro Magazine.

With that said -- having said that, I will turn to the operator for Q&A session. Thank you.

Questions And Answers

Operator

Thank you. Excuse me, ladies and gentlemen, we will now begin the question-and-answer session. [Operator Instructions]

Our first question comes from Mr. Marcel Moraes from Credit Suisse.

Q - Marcel Moraes {BIO 6696122 <GO>}

Good morning, everyone.

My first question regards profitability at the and at the business, the way they are today. We know that we are much -- little bit chance of seeing grain prices going up, because of the weak price. And but you have also mentioned that profitability has gone up over the last 12 months. So, would you like to just comment on not considering -- if you expect profitability to keep on going up over the next few quarters and where should it come from, if it's in domestic market or if it's in the export markets? This is -- are my questions.

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

Marcel, thank you for the question. In overall, we don't think that with margins will keep on this -- like trend from now on except for the effect, off the seasonal effect of the last quarter. So this is our base consumption for the second half, but of course we need to take into consideration right now the other effect related to some cost pressures, but as I said we are seeing the margin, the supply demand situation now favorable for this -- prices.

A - José Antonio do Prado Fay

Yeah. I would compliment what Leopoldo said that this week from the situation in Russia, Eurasia will have to prepare the winter time in a work scenario for production cost approaching. It's hard to say the total effect of that, but I would say that we expect to have more volatile scenario for commodity for next time, I think that commodities will have bigger prices, not as big as it was in 2008-2009, but bigger than it used to be during 2010. So, we can expect from price volatility and price point changing, mostly in export goods.

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

Marcel, just a specific information for you, during this period that I mentioned during the presentation from the ending of June when this scenario triggered until today with international wheat prices increased by 59% at around 42% for this -- in Europe in average and the corn prices -- in the same time increased only 12% and domestically, not only because of this movement, but also because of the support from the government, the domestic corn prices increased by 12%. So, just for you to balance the impact of the international players, especially the ones in Europe to our impact.

Q - Marcel Moraes {BIO 6696122 <GO>}

Okay. Thank you, thank you very much.

Operator

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

Q - Alan Alanis {BIO 15998010 <GO>}

Thank you so much and congratulations for the quarter. You just mentioned that you expected more volatile and higher commodity prices going forward. Should we infer from that comment that you are activity hedging or you could remind us what your hedging policy would be for these commodities, please?

A - José Antonio do Prado Fay

We had our risk management; the point that we have some protection that we can be long or short depending on position that we took that we have a comfortable moment to safety, but anyway, I believe that we are facing a turning point regarding the international price of protein. We expect that this price goes up in the short.

Q - Alan Alanis {BIO 15998010 <GO>}

And also regarding I mean that thin line of -- looking for exports. Have you seen any change or what are the kind of changes that you're seeing now that Russia announced that it will importing or it should be importing some poultry again from the United States. And what are your expectations of -- let me ask a very general question, in terms of increased capacity throughout the world now that demand will continue to pick up?

A - José Antonio do Prado Fay

Let's say so in worse scenario everybody tends to be more flexible regarding to import the importations that -- and Europe now released some GMO corn to import, so this is normal when the scenario pick ups this trend that it happens since Russia announced the situation on the wheat crop, so I expect more flexibility from the markets, which may include American, but it's not yet -- I don't see any modification on that part. And the other question was?

Q - Alan Alanis {BIO 15998010 <GO>}

Regarding the effective?

A - José Antonio do Prado Fay

I think that the production cost will increase all around the world more than in Brazil. We see that an opportunity to give more at the competitiveness of Brazil could improve now due to this commodity change mostly in Europe and Eurasia. I don't believe that we can have a lot of capacity increase due to this scenario, yeah.

Q - Alan Alanis {BIO 15998010 <GO>}

I hear you. So, basically you're saying that even if this commodity prices were to go up that and I'm assuming that FX for the -- remains at this level that Brazil will regain some of its global competitiveness so you have a positive outlook for next year?

A - José Antonio do Prado Fay

Yes, it's a guess. It's our guess.

Q - Alan Alanis {BIO 15998010 <GO>}

Okay. Thank you so much for that.

Operator

[Operator Instructions]

Our next question comes from Jose Yordan from Deutsche Bank Securities.

Q - Jose Yordan {BIO 1496398 <GO>}

Hi. Good morning. The question for you Leopoldo: you mentioned your migration towards IFRS et cetera. If you can remind us, when the official date that you will switch over is and I guess what is your expected impact on your EBITDA calculation because the one thing that you don't include in your EBITDA calculation at the other operating items, which will likely be which are new from part of the EBIT calculation under IFRS. So, just two sides of the same question, when will it happen and I guess what's your normalized other operating income and expense going forward?

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

Okay. Regarding the IFRS above, it's going to reflect the results, the full year results. So by year end, it will reflect towards that IFRS, of course we are right now is -- all the gaps for us to address aggressively. Regarding to these specific point of CPC 38, we took up advantage of a policy that already mentioned and triggered that point to use this type of understand your or ruling to adopt this type of accounting, but in terms of the type of the impact that we should expect in our EBITDA margins, although we are still analyzing very important to emphasize that we don't expect to see a big impact, according to our first impressions or calculations.

Q - Alan Alanis {BIO 15998010 <GO>}

Okay. Thank you very much.

Operator

Excuse me. Our next question comes from Mr. Gabriel Lima from Santander Bank.

Q - Gabriel Lima {BIO 16224058 <GO>}

I have just a quick question, just want to better understand the strategy regarding our dairy segment as milk has increased much more than the dairy segment. So what is the strategy here? Are you being less exposed to produce processed milk and more exposed to commodity milk or that's not a case? Thanks.

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

Yeah, the general strategy is to keep improving our processed milk business, which means yoghurts and to have less fluid milk. Not less milk than we have now, but more possessed milk than we are having. So, we are putting more efforts on Batavo brand and going to put more structure on refrigerated dairy business in order to decrease the dependence on the commodity.

Q - Gabriel Lima {BIO 16224058 <GO>}

Yeah. But when I see your release here that milk segment increased 14% in volumes in the first half compared to your goal and the dairy products decreased 6%. Is that the case? I mean is that reflecting less exposure to commodity milk?

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

The point that we are having a very poor performance on -- during the first quarter then we recover some new carriers and then this is the left page so a mix between the new perfection milk area you're farming the milk farming areas and the product strategy, the product strategy is much based on percentage but at this very moment the first half of the first quarter, we have a very poor performer -- and now we are keeping and maintaining our performance as it was before. That's why there is this difference, but it's more static than the strategic.

Q - Gabriel Lima {BIO 16224058 <GO>}

Okay, got it. Thanks.

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

Okay.

Operator

Excuse me. Our next question comes from Tim Thiagio from Fator Capital Markets.

Q - Analyst

Good morning. I guess my question is around the domestic process, food market and you obviously saw a benefit from the World Cup in the second quarter. How should we look at as far as volume growth? What percentage the World Cup and the potential boost from that had on food consumption Brazil?

A - José Antonio do Prado Fay

As a matter of fact the World Cup helped a lot, the beer manufactures, for us it's not strong impact regarding to that. We expect as usual to have the second half of the year positive seasonality mostly due to the end of year product, the seasonal Christmas product that used to be a good moment for us, but the World Cup, probably we do not see any important assumption increase.

Q - Analyst

Okay, thank you.

A - José Antonio do Prado Fay

You're welcome.

Operator

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

Q - Jose Yordan {BIO 1496398 <GO>}

I have a quick follow. Just on the consultant fees that you mentioned in your press release et cetera. I guess any color you can give us on how long the McKenzie mandate last for and so I mean for how long and what kind of amount per quarter should we expect the consultant fees and I wonder if it will disappear altogether?

A - José Antonio do Prado Fay

This is pretty much not only McKenzie, but there is IBM, SAP -- this kind of consultants term that the need to prepare the synergies to we are changing the system we put the same SAP on Sadia and basis in the BRF basis for next year, so we have a lot of job to do in the preparation and we need some consultants firm to help us mostly during this year, and partially next year, this year the main.

Q - Jose Yordan {BIO 1496398 <GO>}

We should expect the similar kind of trials as we saw in the second quarter, let's say until middle of next year or something like that?

A - José Antonio do Prado Fay

Yeah, maybe what we are talking is some in the area of at a maximum R$100 million of expenses to be seen this year or partially this year and part of next year. But this would be the total amount of expenses to prepare the merger -- prepare the merger of until personnel or processes and everything.

Q - Jose Yordan {BIO 1496398 <GO>}

And so far it's been about 25 or whatever the amount...

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

It's been 35, year-to-date; it was 22, I think in the quarter and 35 year-to-date.

Q - Jose Yordan {BIO 1496398 <GO>}

Okay. Great. Very clear.

Operator

Excuse me. Our next question comes from Mr. Effiem Javez from Arthur Capital.

Q - Analyst

Hi. Thank you for taking my question. One, I was hoping you could provide me with an update on your discussions with -- and what if anything you can tell us about when this final decision to be made.

A - José Antonio do Prado Fay

Okay. During this quarter -- which is the part of Government Financial Minister puts its report on -- which is the Board of -- and they approved, they said that our operations could be approved with some refraction.

We do not agree on that, we believe that our operations according to Brazilian regulations could be integrally approved without any restrictions, but this was the opinion of the Government, Financial Minister. And then we are now waiting for -- to call us to argue regarding to this two points. We leave that we have strong data, strong positions to argue with them. That's the competitiveness, the rivalry, the market concentration and the efficiency. Under this four points, our operations could be approved.

So this will be a discussion that is difficult predict how long it will take. We keep on wanting this as quick as it's possible, but it's hard to say when we will have this final and decision from the Board.

Q - Analyst

Can you just remind me, what those restrictions were specifically?

A - José Antonio do Prado Fay

They consider that we can have market control from the entry price brands. So it's not -- they suggest, let's say so, that we sell this entry price brands, which they put some options. They talk about the -- the margarine brands, the -- which is a brand -- some other. It was the price in margins the -- in the margarine business.

And for the meat they ask us to analyze the selling of -- or Batavo, which we do not understood except because Batavo, 75% of the Batavo is there, which is not analyzed at this moment; it's out of the analysis of the case, because there is no concentration in dairy. So -- but, let's say in general they are saying this that we have to sell our enterprise brands. They put another option that it was completely difficult to understand that was to hire -- go -- outside brands for someone else, which is absolutely inefficient regarding to the consumers in an competitive environment. We really do not agree on that, but this is under my point of view only negotiation position and not really something that can be sustained on data, on basis -- on an economic basis.

Q - Analyst

Okay, thank you very much. If I may ask just one more point of clarification in terms of the charge related to idle capacity. If I understand correctly, I think it was Jose Yordan, who asked about if IFRS, you will have to treat those differently than you're probably treating them, which I think that the right now you are basically excluding that from your EBITDA calculation. And in that IFRS, you would have to include those, which will depress your margin. Is that correct? Is that what the change will be in IFRS?

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

No, it should not change. In fact we changed the calculation of this either capacity and also the way we calculate the depreciation the new ruling. So you should not expect an impact related to that.

Q - Analyst

Thank you.

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

Welcome.

Operator

Excuse me. Our next question comes from Juan Respito from Metlife.

Q - Analyst

Good morning, how are you? My question is linked to CapEx and basically the base of CapEx year-to-date, which seems to be slow compared to your full year guidance of 1 billion. Are you just linking this to the approval of the merger or you have more projects coming for the second half of the year and in which areas will they be? Thank you.

A - José Antonio do Prado Fay

Let's say there is a lot of things to consider. We have idle capacity in Sadia system. We do not know exactly how much it is, but we know that there is a idle capacity in this system. We are investing in line with we said that during the follow on time that we think that this year 1 billion could be good guess for investments we as Leopoldo said before we keep on having this guidance. And of course to improve the investment level in CapEx if we will need to have the complete clearance from to make the right choices anyway.

Q - Analyst

Okay. Which kind of investments will you prioritize for the second half of the year?

A - José Antonio do Prado Fay

We'll keep on this productivity and enhancement, this is the prioritization of our investment has been so, it won't change. We gathered this currency from...

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

We keep on completing the operation that is starting up. We keep on putting money in projective and as Leopoldo said.

A - José Antonio do Prado Fay

It's important to emphasize that this situation it's not jeopardizing our capacity to grow and to produce. It's very important to say it's not that we are ready.

A - Leopoldo Viriato Saboya {BIO 16137418 <GO>}

We are not postponing any investment that can jeopardize our business in the future due to cardio or something else.

Q - Analyst

Okay, very clear. Thank you.

Operator

Excuse me. This concludes today's question-and-answer session. I would like to pass the floor to Mr. Fay for his final consideration. Please sir, go ahead.

A - José Antonio do Prado Fay

I just want to thank you all to stay with us and I see you in the next quarter. See you bye.

Operator

That does conclude our BRF Brasil Foods SA's conference call. Thank you very much for your participation. Have a good day.