Q1 2013 Earnings Call

Company Participants

- Abilio dos Santos Diniz, Chairman
- Jose Antonio do Prado Fay, CEO
- Leopoldo Saboya, CFO, IRO
- Unidentified Speaker, Unknown

Other Participants

- Alexander Robarts, Analyst
- Fernando Ferreira, Analyst
- Isabella Simonato, Analyst
- Morty Locafeature, Analyst
- Thiago Duarte, Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good morning. Welcome to the BRF SA First Quarter Year 2013 Conference Call. This conference call and the presentation are simultaneously transmitted via webcast in our website, www.brf-br.com/ir. You can also have a full version of the slides to be downloaded. At this time, all participants are in listen-only mode. And later, we will conduct a question-and-answer session. Instructions will be given at that time. We would appreciate it if each participant made only one question. (Operator Instructions)

Forward-looking statements related to the Company's business perspectives, projections, results. And the Company's growth potential are forecasts based on the expectations of the management as to the future of the Company. These expectations are highly dependent on market changes, economic conditions of the country and the sector and international markets. And thus are subject to changes.

As a reminder, this conference is being recorded. At this conference are Mr. Abilio dos Santos Diniz, Chairman of the Board of Directors, Mr. Jose Antonio do Prado Fay, Chief Executive Officer and Mr. Leopoldo Saboya, Chief Financial, Administration and Investor Relations Officer. I would like to turn the call over to the Company's management. You may proceed.

Unidentified Speaker

Good morning, everyone. I think everybody woke up now with the noise in the room. To begin our earnings presentation, I would like to give the floor to Abilio to take and state the opening remarks. Thank you.

Abilio dos Santos Diniz {BIO 1781457 <GO>}

Good morning, everyone. This is the first time I'm participating in the earnings presentation of BRF. Actually, it is the first time I do it outside my original home, which is GPA. And I hope I can stay here for many and many presentations. I'm feeling very happy here, very pleased and very welcome. And also very grateful for the investors for all their confidence. My intention -- my humble intention is to contribute to make this Company even bigger and greater than what it already is. I welcome you all and I can see some people here. I don't think you covered GPA. I don't see so many familiar faces. But anyway, I hope to manage to have a good relation with you as well.

I always gave a lot of attention to the market. Back in GPA, I always had a huge identification with the market. Since 2005, two-thirds of my participation in GPA related to the market. So I want you in BRF to count on me for full transparency. I know this Company is very transparent already to you. So let's move on now to the earnings presentation. And after that, I will be happy to take any questions you may have or any comments. And please bear in mind that I am only a three-week veteran at this Company. So tomorrow I'll be celebrating three weeks as of my new position here. So I'll be here at your service. Fay?

Jose Antonio do Prado Fay {BIO 15337837 <GO>}

Let us get started now, moving now to the earnings presentation per se. We will begin addressing the new cycle at the Company. And it's impossible to address a new cycle at the Company without thanking first the safe and competent leadership by Nildemar in our leadership. We've had several years of Nildemar as Perdigao leader. But that's not the point. He was also a BRF leader. He also played a leading role. And the Company's management is very grateful to him.

And now, we are under a new leadership, a new vision, looking to the future. And, to some extent, uncovering and releasing our capacity for growth under the leadership of Abilio as of now. It is the First Quarter that we have Abilio with us. And he already started on the right track. We have a good quarter to present to the market and expect it to keep doing so. We know that we have volatility. But luck is also important in life.

So to address very briefly the cycle, over the last three years the Company -- well, almost four years, on May 19, more precisely, we signed the protocol or the Memorandum of Understanding merging our companies. So over this timeframe we had several activities oriented to execution, with huge concern of not having any rupture. We manage a very long chain. And loss of this chain control was something very severe in our business and also very challenging to recover. We had this concern of taking all these actions that were not simple at all.

We started the merger first with the treasury onwards. Our first action was to merge the treasury and then we started with administration, followed by systems. And then we started working lastly to join our front-end, which is the commercial area. And we are bound to complete it. We are not done yet. We expect to have it completed, delivered in June when it comes to administration. In other words, it means all of our warehouses may be working with multi-product and multi-brand.

Yesterday -- well, a couple of things are very emblatic [ph]. Yesterday, for instance, we had the first unload of Perdigao brand in one of the craters, the Sadia system in JuneDIE [ph]. So as of now JuneDIE is also working with multi-brands. And by doing so, we'll be completing our merger that took a lot of effort and also allowed us in-house vision by the Company. And that's what really drive us to a new cycle. So that's how we can speak of a new cycle to some extent. And through July this year, we'll be completing in Brazil our integration.

Please bear in mind that we still have strong focus in the foreign markets. We're doing absolutely the same in Argentina with the same SAP, our single platform. So we continue with a series of tasks. But in Brazil, by mid-year, we expect to complete this phase. The Company is very much oriented in-house, very much oriented in not losing its chain or its pace or revenue or results and meeting all the resolutions we are expected to achieve.

Over this timeframe, we had a top-line growth of 30%. We grew. And we grew a lot. And our ADR grew 288%. So the Company was really oriented in-house. But we managed to deliver. And this was one of our assumptions during this timeframe. And as of now, we turn the page and, to some extent, we also get the Company ready for this new growth. In other words, like I said in previous circumstances, we have to revisit our Company. We already had a project to work on the organization again. And we thought about the post-merger phase. And just as any organization, a company, it takes some time and it has to be pegged to our strategy.

Our strategy over the last four to five years was to grow. But basically taking care in order not to have ruptures of loss of control in our categories. So it has to do with people. We have to change our organization chart. And it will be changed in the following months. And we also have product launching. We had to work on several product launches in order to reorganize our product portfolio.

In 14 categories, key categories, we have some kind of CADE rule and that took a whole change in our portfolio. So as of now, we'll be changing the portfolio. But this time more oriented to renovation and pretty more focused on consumers rather than we did up to then where we had very good performance. We launched over 400 products in this reorg. And that took a lot of our research and development people. And we are about to have a new TD in JuneDIE. It's really state-of-the-art, really high end. We invested BRL60 million. In other words, the Company is putting all the assumptions of the acceleration growth process.

Next, we also have our consumers and retailers, our brands, basically. We have all sustainability indexes. We are GRI level A, ISE for quite a long time. So the Company has a lot of responsibility and deep concern with citizenship. And we'll represent investors. And we want you all to keep on betting on us. And by the way, I would like to thank you, investors, for your trust in the previous cycle. The Company was always supported by investors ever since the follow-on we had to capture our Sadia payment, BRL2.5 billion that we got from the market in 2009, three or six months after Lehman Brothers. So it does show investors' trust in the Company.

So now let us start addressing our results. I'll give you some highlights -- and next, Leopoldo is going to give you more details. We had a good quarter. We consider the quarter to be a good one. This quarter was very intense when it comes to the Company's actions.

So if I were to summarize this quarter, what would I say? In the domestic markets, the price that we had by the end of the year, because by year-end we had a vision. And we even discussed it in our previous call. Grain should go down during the First Quarter. But that didn't happen -- actually didn't happen. There was a slight effect in Chicago. But not in Brazil. That's not exactly what happened. Later, we can go deeper into that. But that maintained the pressure we saw in December, that we will keep on having cost pressure over the First Quarter. Then, we made huge efforts for prices, promotions in the point of sale in the domestic markets so we could overcome that barrier.

We have a good scenario right now and we are keeping an eye open on volumes. We are concerned because the market is being challenged to absorb volumes. As to the foreign markets, quarter-on-quarter, First Quarter of last year and First Quarter of this year, there is a price increase that is very significant. We made huge efforts again in terms of price increase.

And foreign exchange is also beneficial. If you'll recall the First Quarter of last year, foreign exchange was way lower compared to what it is today. So we have these two drivers that help the market. And later on we can break it down by region.

Food services saves a lot of expenses. Expenses are very much controlled, food services. And they can have a bottom line very much protected. There is a significant price rise as well to offset these costs. And also, in the First Quarter of last year, we had excess inventory. Food service, therefore, had to go to some settlement in sale with tempered results in the First Quarter.

For dairy products, we've been working since September last year to work on the composition of dairy products again. It's a slow process. We're still beginning to reap the fruit of this work. Basically, we need a right-sizing of UHT category, which is very significant to maintain our relevance in the milk producing region.

But from the moment we work on the cheese category, we have possibilities to do that. Without cheese, we would have a significant cheese category. But it would be difficult to do what we are doing right now without losing relevance in the milk producing regions, which is very important to a leading Company or has a leading role. It is very important to be relevant in our milk producing region. So dairy products have this action to structure what is currently being done. And on top of that, we still have a long way to go.

But I'm very happy for our results for dairy. But we know that we still -- we are on the right track. We are doing fine, consistently improving our dairy results. But we still have a way to go in order to turn dairy categories into a big driver of value of the Company as a whole.

So as opening remarks, that's all I had to say. Now I'll turn it over to Leopoldo to get into details and then we can talk again later. And also, we have the Q&A.

Leopoldo Saboya {BIO 16137418 <GO>}

Good morning, everyone. So let's resume our presentation after introductions about the current scenario in our earnings to get into more details now. Now, moving straight to our performance of adjusted EBITDA, for all effects, our EBITDA was very good, especially when we consider it is the First Quarter of the Company.

And historically speaking, it tends to be the weakest quarter for many reasons -- seasonality, consumption, vacation, holidays. But our quarter was strong, though, considering our recovery cycle that had been designed ever since late last year and was very much in line with our expectations despite all the difficulties and some weaknesses identified in the market -- the consumer market in the world and also in Brazil.

So when we look at the marginal contribution for these results, with no exception whatsoever, all of the Company's businesses had a positive impact to this performance, this positive performance between the First Quarter of last year and this quarter. We can see this contribution of BRL89 million from foreign market and BRL175 million as contribution from our businesses in Brazil, basically known as domestic service or food service, domestic market. And dairy products.

Another highlight is the performance of our revenue. The Company, especially last year, we spoke a lot to you last year about our focus, strong focus to recover our critical mass or our size after TCD. That was done. And now we compare a quarter where we have total impact from the brands sold and also temporarily suspended brands vis-a-vis a quarter in which the Company was still in the previous stage. We can see the growth of almost 14% has to be really highlighted.

And in summary, we have 5% less in volume and almost 25% more in price. I remind you that the 5% drop in volume, if we didn't do anything, the effect of TCD to the organization would be 13% in volume. So if subtract TCD in both forms, both sale and behavioral, that would mean 13% less volume in the margin. And we are showing only a drop of 5% in volume. And in the top line, virtually we don't view at all considering what the Company has done up to now.

As the breakdown of our business, we had some changes. However, when we look now on a comparative basis, it is very small. You might recall that what we sold from BRF was basically process products, not only capacity. But also brands and categories that in the vast majority were processed. And it never brought lack of balance in the organization when we look at the current mix. This mix is enriched within categories. It has become richer and richer, be it through brands or our average portfolio with launches in order to make our categories stronger.

In other words, our results also stands from the strategy outlined in order to go through this new balance to our top line. So when we look at the organization today, it is not so different compared to what it was. But we did have to do -- or to work on huge efforts to be where we are today.

Now, this is our income statement in a graphic representation. All figures are absolutely positive vis-a-vis last year. I would highlight first the expansion of our gross margin of 2.3percentage points, which is very necessary. Our gross margin was very much compressed. And on top of this gain in gross margin, we also had additional gain in convergence to EBIT and EBITDA of over 1percentage point stemming from very consistent effort in savings in SG&A, in other words, our commercial and administrative expenses.

When it comes to net sales, they had a drop of 1.1percentage point vis-a-vis last year. And we are below the barrier of 16%. Until very recently, it was something we had never done before. In other words, we closed the quarter with adjusted EBITDA margin of 11.8, or 3.4 points above the previous year. And also, stronger net income compared to last year, BRL359 million vis-a-vis BRL153 million announced in 2012.

Moving forward, think about cost of goods sold. And we think it's important to talk about that for a couple of minutes. It helps to understand the current cycle of the Company and what we'll face in the future. I don't know if you recall it, those of you who saw our Fourth Quarter earnings presentation, we talked about the 16% increase in our costs and they happened, to some extent, over the second half of the year. Visually speaking, it's easy to notice because it was relatively flat over the first half of 2012 and then there was a big rise over the second half of the year, which coincided with the moment when we first started to increase our prices to transfer the inflation effect that we had been feeling.

And we also mentioned a phenomena that did really happen, which is the carryover effect of our costs from last year to this year. When you look at the price, the cost is slightly higher compared to last year with no mix effect. Notice that the mix in the Fourth Quarter is richer. It is already a COGS per kilogram that is naturally higher if you were to deduct the mix effect. Trying to have COGS under the same basis between the Fourth Quarter and the First Quarter, price -- or cost increase would be even higher.

And this explains, to a large extent, why we have such a margin compression, particularly in the foreign market comparing the Fourth Quarter to the first one. The First Quarter year-on-year, like I said, everything is better -- all business units, all markets are rising. When I look to the Fourth Quarter and then the First Quarter, what is different is only the foreign markets. But, above all, related to costs.

We had a cost crunch already expected. We also said that about a month ago. And precisely, it came from corn prices. There was an effect in-between crops. And because we had been carrying over short stocks or short inventories, we affected staple categories that are basically what we export. And I'm beginning to explain the foreign market and also the cycle to the future.

The next chart, for instance, it shows historical corn rotations. It's important to understand when we are in the cycle, where we are in the cycle. The first historical message shows what we've been speaking of for quite some time now. After 2007, there is a change not only in broad movement. But also in the frequency in movements. Corn, for instance, it has very high historical levels.

In Chicago, these are international quotations, by the way -- well, it was attenuated started late last year. But this international relief did not come to a domestic relief. Actually, it was the opposite because Brazil was only the only corn supplier to the world, there was additional demand. They wanted Brazilian corn. And quotations in Brazil increased before the end of the year. And actually, this relief started around February. So ever since February, we can see a decreasing cost curve. And that might be an impact in the Second Quarter.

In other words, just to highlight, our COGS in the First Quarter was mainly due to cost of acquisition from late last year and also the beginning of this year, January and February, having an impact on costs and also having a stronger impact. But most significantly, the foreign market than the domestic market, that could handle the circumstance due to higher value-added portfolio and also additional market moves.

Moving ahead, we show meal with a very similar story. The drop was slightly stronger. Just to explain that drop in the curve, this is not our projections, these are future quotations, forward-looking contracts of the positions that the market sees today. So new world crop, particularly the new crop from South America. But substantially from the US, we expect a cheaper new crop, according to these quotations, due to the good harvest and also due to consumption, tied consumption. And also some uncertainty when it comes to a drop in consumption for feed in the world.

And despite this drop, from now onwards -- well, apparently it is significant. But the mass of expenses or the average cost we expect to see with soybean meal and corn in 2013 will be not different from 2012. We went up and now we are going downward. But on average expense or average acquisition and consumption cost will not vary so much compared to what we had in the previous year.

Now I also highlight our expense ratios. We are being very tight about BRL1.1 billion expenses on a quarterly basis, or 15.3% of our revenue. And this is where we also find part of our synergy visibly seen. We have the merger and the synergy in COGS which also happens. But it's not visible today due to a very intense change in the levels of costs. So there was a gross margin compression that we are beginning to decompress and COGS synergy will also come back and have an impact on gross margin. But in SG&A, we already begin to see gains stemming from the merger and we are absolutely on track with our synergy capture plan that we constantly mention to you.

Now, what about CapEx? I also have to mention very briefly these figures. They are important to understand how they talk to our guidance and also how we think about the future. Actually, consider the figures, as we disclose, CapEx is the summation of investment in fixed capital plus biological assets of BRL516 million. And to add to this, acquisitions of interest. So basically, Federal Foods, dating in the First Quarter, around BRL75 million out of the BRL107 million.

But I have to explain that out of the BRL516 million, for comparative purposes with a pure CapEx investing by the Company in organic growth and -- are the projects, we have to take part or 88 for logistics and also another parting support, which is our Creditiba [ph] facilities. Though this is mercantile lease, it is not cash leaving the organization. But it has to be posted as CapEx. And the reason offset a counterparty that cancels the capital effect, which is long-term accounts payable, which are billed to suit. So to all these facts, if I deduce 127 of these and 121 of biological assets, pure CapEx this quarter would have been, or was, approximately BRL270 million. So these are the figures.

When I speak of BRL1.5 billion investment in CapEx for the year, it is comparable to this BRL2.8 billion for the quarter. So that's important to make that reference so you know that we are below our pace, our investment rhythm. So we can get to BRL1.5 billion that was mentioned as the Company's goal for the fiscal year.

Now, also talking about our financial position. We are in a very sound position, as we have been all over the year. And despite the low cash that we had last year, we had a debt of around BRL7.2 billion. It is a very well extended net debt in its terms and the origins are below trade finance, as you can see here, that they are all very well balanced. We can already see a drop in the First Quarter, going to BRL2.38 million, our leverage. And the trend is to have deleveraging of that figure. And this is good.

It is important for the Company because it is preparing it for new leaps, new growth in an inorganic, selective and intelligent and well thought way. And that's how the Company has been working lately and we are paying attention to all details. And right now, we are opening up the new potentials which are very important, analyzing our perspectives and cash generation for the next year.

In terms of product launches, we are still working with added value products and convenience products. These are a few samples that we have been doing in the last half of the year. I will not go into details. But you can see that they are many.

And now we'll go into specific areas of the market. Starting by the domestic market. And Fay already mentioned a few words about it, we had a very good quarter in terms of results. And despite of being the First Quarter, it was a very sound First Quarter. If we compared that equation of volume and price for the top line, the domestic market, if it is compared to -- was past year, it's good.

But if I did a base adjustment of the same three be of revenue and I adjusted the base of last year to reflect the effects that we had in the next half of the year, that is, the sold categories and the suspended categories, we had the growth of the same pace of 38% in revenue and 23% in volume. That is very significant. It's a large growth, considering the organization size and also our portfolio. And we also did that with a very good profitability.

Again, analyzing that equation among -- between price and volume, they are below the revenue -- the revenue is above. And in fact, price and mix is what I was explaining in the beginning. In the interim mix, if we analyze the frozen or other processed products, the mix is better due to launchings that we had. And also, the portfolio was brands that we still have in the Company. So all of that brings a positive effect of prices going beyond our cost impact, of course. Then, we have an expansion of almost 400 points in net profit and net income for this quarter.

And I would like to take this opportunity and mention that from now on when we analyze this cost against the margin -- and let's remind ourselves that in the domestic market it is not as the sun going up and it's not going to be as the sun going down, it has this added component. But we are sure it is a moment to better focus on the cash margin so that it can be more fluid in terms of volumes so that we do not accumulate volumes in a moment in which the consumer market is showing weaker signs.

You probably are following other results from non-durable products. And you can see that changes are coming. We are following that trend. We do not have very evident signals. But there is a trend, we see that. Therefore, we have the opportunity and the capacity and strategy of analyzing our profitability and think about cash margin not only in the percentage margin and the revenue. And that's what is our idea now for the next half of the year.

About the foreign market, we have a performance that probably has already been explained. Revenue is increasing because we had integration of Quickfood, especially in the last quarter. Of this percentage that the price has increased, part of that is due to the exchange rate that benefited us. But also there was an increase in the orders from one year to another. Our margin has improved vis-a-vis last year. But, as I have explained, it drops vis-a-vis the Fourth Quarter due to cost. And we have not lost in price. But now when we go into more details, region by region, you will see that we did not have and do not have room for higher price in dollars due to the perspective of dropping prices.

And basically, that is the summary of our scenario. Just to give you an idea, when I talk about CPV 16% of increase, 22% was domestic market and 10% was the whole domestic market. Then, I'm adding retail, food services, dairy, everything domestic market, 10%. And foreign market, 22%. That's how we account for the average 16% in the Company. So we have a major cost impact that has happened in the foreign market.

Now, the main market, the Middle East, was very good in the quarter. We want really to work on the profitability that we have reached there. Of course, when that happens, everyone turns their eyes into the region. In Europe, no one is safe to the price. And when we work with food and with chicken, the protein in a down-trading, it is benefited. But even then, we did have a very challenging scenario in Europe.

Food inflation in the world is very important. And even more important in countries in Europe that have a serious economic problems with high rates of unemployment. For instance, turkey meat, which is a more noble meat compared to chicken, it just takes a hit and right now we are working with a profitabilization and we have next -- good quarter and we expect to recover price and profitability.

Eurasia, you can see that their participation has been decreased year-by-year. And increasing volume here is because we have reopened some plants to export to Russia. And when this market is open, the results are good. In the Far East, in summary here, we are talking about Japan. Yes. We do have more adequate inventory levels here. And not very high ones. But there is an important fact, which is the devaluation of the Yen, that added to the high cost of food, froze a little bit, the market. And we had a problem increasing the prices in dollar.

And with the perspective that we see all over the world in the lowering prices of raw materials, corn and meal, that's when it is difficult to raise prices. But we will benefit from that movement without having to increase prices, just like I said. So the challenge is really to hold the prices in dollars, prices which we have already reached.

Now, talking about LatAm, I already mentioned Quickfood. And with all the problems that we had in Argentina, we understand that we are at a good pace and we are able to have advances, integration improvements, go-to-market. We have a specific and a strategic product -- project, even with not that many pricing leverage that the market does not allow us.

Africa is also a strategic market for us. We are growing. We have dedicated portfolio, data are very good. But also, we are adjusting our portfolio there in Africa for eventual sale. But in the long-term, we are having good results.

So now, our last two businesses, food service and dairy. I believe Fay has already talked a little bit about food. We had that volume compression when I talked to you last year. And I would like to remind you that last year we were in another module where we were also using food service as a channel to drain products. We are not doing that this year -- we are being able to keep the portfolio more intact in terms of strategy. That's why we have this price performance as well as the profitability, bringing food back to a platform, a stage where we had before. That's what we wanted. We had said that in the past. We want food operating in our historical levels since merging.

And finally, dairy. Probably here you can see where our strategic really comes up. And I had told you in the past before wait a little bit because this is going to be good. I believe we have to focus on good results because we are in a ramp-up of leverages to bring the business into a sound result and then consistent result. But in the First Quarter, we can see it, this drop in volume had to do with UHT that we compressed. And therefore, we can bring better prices to our portfolio.

In the category, we also see a better improvement in the dry division and in the chilled products division. And with that, our EBITDA margin goes to 4.4% and EBITDA is around 6%, 6% something. And for dairy, this is an interesting margin. And we now have the intercrop [ph] for milk. We've seen that the sourcing of prices for milk have increased, which is good when we have the right market. But on the way back it's a challenge to keep profitability.

But anyway, we are very happy with these figures as they really express our strategy and our ability to implement our plans. So I hope I stick to my time and I have just here one last slide. But now I'll turn the floor to Fay.

Jose Antonio do Prado Fay {BIO 15337837 <GO>}

I believe we should now talk -- start the Q&A. Just talking about the last slide, the Company -- it shows how the Company has performed. We did have a good performance. It has -- as I already have the trust of our shareholders, because they see the future of the business that was and is being built since May 19, 2009. And now, we are ready to get into this new cycle.

So let's start our Q&A session and then we'll deliver our final remarks. So let's start the Q&A.

Questions And Answers

Operator

Excuse me, ladies and gentlemen. We will now begin the question-and-answer session.

Q - Unidentified Participant

Good morning. Congratulations on the results improvement. So I have just one question for now. What is your perspective from now on for prices for processed foods? We understand that on the one side there is not the best demand. And not only for you. But also other categories of basic foods. And we see the industry with some -- with little idle capacity. And so my first question is about processed foods. Would that be able to keep in the current levels and despite of dropping grains?

In Natura products as well, you have shown that there is a better mix, better channel. So the prices then for wholesale are also better. Is that going to change also? And dairy products and food service products, what is the trend, in your final view, in terms of prices? Will those be kept?

A - Jose Antonio do Prado Fay {BIO 15337837 <GO>}

Well I'll make general remarks about prices and those should address your questions. Leopoldo said, as you might remember, that last year we recovered our margin. That's what we were looking for. We wanted to recover our rates. So right now we are looking for cash margin. We have to analyze the fact, volume and price.

The long food inflation. And if you have lived inflation in the past, you know it takes time and it corrodes the prices. So that is taking time and it's being -- the prices are going up -- food prices are going up for a long time and we had an increase of prices of meat. And then they have stabilized at a high price. And then vegetables and all basic foods also come up. And consumer is feeling that. So right now, the consumer is very sensitive to price. Because the food inflation hits everyone. It is a very important matter for a family's budget.

So our price strategy is to be horizontal. And that's when we are concerned with volume. That is what we are focusing on. And several of our categories are showing lower volumes. Sometimes we have the same variadeten [ph] amount, which is not bad. But the volume is a little bit shrinking. So the way we are working with prices is something very sensitive. We have to be very careful dealing with it. And we have abilities of choosing channel categories, regions. And that is a very important job so that we are able to keep up with our position.

Food services is not a difference -- as different. As consumers become more selective, they go out to eat less. You see that jobs are not being generated as much anymore in restaurants. So the main focus of the Company right now is volume and prices. Costs are being pressed. We see a drop in grain prices. And that comes -- and those prices come from a high price. So it's not a very high drop and our short-term costs are not relieved by it.

Maybe in the long-term we will have a better effect. But this mechanism of price, I believe that today to increase price and the process of price increasing is not our first choice as it has been in the past. And actually, it was not a choice, it was something that needed to do. We were not able to support our costs if we had an increased prices. But right now, our modus operandi is to use the leverage and tools that the Company has to hold on to our current results.

Operator

Isabella from Merrill Lynch.

Q - Isabella Simonato {BIO 16693071 <GO>}

In terms of the export market, as Leopoldo has shown, we see an improvement in costs. But also a more complicated demand in the main market. What is the scenario for demand improvement in those markets? What is the impact of the Asian flu in China that could have in your products in general? So at the end of the day, how can we expect the margins to go back to normal in this category?

A - Jose Antonio do Prado Fay {BIO 15337837 <GO>}

In the foreign market, we have some specific points of attention. Europe had not a good performance -- it was a bad performance. And now, it has a seasonal trend of improving performance because we will have the barbeque season and we will be able to have a better performance here in terms of rates and margins. But in terms of volumes, we are not very excited about more volume in Europe.

In the Middle East, we need to keep the performance going. The performance has been good. Argentina is shown some signs there, although our business there is facing difficulties due to the Argentinean scenario. But our great organization efforts have been reducing costs and I believe things are going on a good pace. It might take some time. But they are just moving and costs should start dropping.

So how do we sell in the foreign market? Grill are in some processed food. And they are more sensitive to prices of food stuff. So those results should be slow but consistent. And that might be our recovery MO. I don't think it has much to do with price.

So the United States right now is in a not well defined market. We have to wait to see where it is going to go. We do see some concerning signs. China has decreased consumption. So I believe the world is in a stress point. What we see is that we have the possibility of costs dropping in the short and medium-term.

Operator

Morty Locafeature [ph] from Goldman Sachs.

Q - Morty Locafeature

My question has to do with your comment on volume pressure in the domestic market. This growth of 23% ex TCD, it suggests actually that growth was still good. So I'd just like to have a better understanding, when you make this comment, what exactly are you referring to?

A - Jose Antonio do Prado Fay {BIO 15337837 <GO>}

Actually, I think you would have to highlight the great Company performance when it comes to TCD. In the past, you used to say that there was a big issue. A big point was to go through execution or performance because at least we had four key categories and two very important and we had a strong CADE ruling which is ham with the Perdigao brand, away from the Perdigao market. And cured sausage.

Perdigao was a leader with almost 34% of the market. And there was also an exit. So we had to rearrange our sales forces in those products in order to offset Sadia and Perdigao portfolios. And we lost all the entry brands. The Company did not have any entry consumption brand. So this action was very well done.

If you exclude TCD and consider the same basis, the Company's growth is really big and volume recovery is significant. So this was very well planned and very well done. And this is the reading when you see, just as you read, if you work on the same basis, you will see the Company's growth was significant, very relevant.

The domestic market, as I said before, I am concerned with consumers. In other words, I am concerned how we can make this -- how can we handle this high inflation rate and consumers have to pay automobile and services. And when we support well-being and the categories that consumers have started to buy. We were discussing that just yesterday.

Not even class A, B or C lower the number of categories they buy, for instance. Class A used to buy 54 categories of the Nielsen basket. And they stick to 54. But they buy less. And to some extent, we also see it happening in our customer portfolio. There is a smaller drop size. We don't lose customers, we don't lose consumers -- however, there is a reduction in consumption or a repositioning or another arrangement in consumption.

Then, we have to see how long this process will last. But we can see all consumer companies showing this slowdown in consumption of non-durable goods.

Operator

Fedrico from Pesem.

Q - Unidentified Participant

I would just like to have a clarification related to volume in domestic markets. When you say you're concerned with volume growth in the domestic market, are you consider your older base or other brands as well? Aren't you only looking to the 23% growth or base adjustment and only concerned with a 7.5 drop? Is that the reading over the year?

A - Jose Antonio do Prado Fay {BIO 15337837 <GO>}

Absolutely. One of the pressure points of the Company is scale. And one or the things we strongly highlight to ourselves is that although we are losing almost one-third of our volume in the domestic market due to the ruling we follow, we should get ourselves strongly organized in order to recover it. The scale certainly is one of the Company's pillars. And your reading is right.

Q - Unidentified Participant

Perfect. I just wanted to understand if you had a very strong slowdown down the road. Another question, Leopoldo. If we put together EBIT, just as you do revenue, adjusted basis for the domestic market, do you have a reading for EBIT growth under adjusted basis as well? Could you share that with us, please?

A - Leopoldo Saboya {BIO 16137418 <GO>}

We don't have information on conciliation of EBIT under the same basis. However, I can assure you that growth is equivalent or maybe even greater. At that moment, we also had a general effect of results. Remember, the average result, if I'm not mistaken, was 9.4 of EBIT margin, which was not a bad one, far from being bad, EBIT around 13. So when I work on the base adjustment, you don't see a change of the delta effect between the adjusted First Quarter year-on-year.

Operator

Thiago Duarte, BTG.

Q - Thiago Duarte {BIO 16541921 <GO>}

Two questions. First, I missed a figure, which is the number of synergies. I missed the figure in the First Quarter. And first, I would like to congratulate Abilio's presence here and would like to know from him what upfronts are being worked on? And when he talks about the growth of the Company, what he foresees? And I would like to know from him a little bit more details around that vision.

A - Abilio dos Santos Diniz {BIO 1781457 <GO>}

Well I've been with the Company for three weeks. But Fay has been teaching me a lot with private lessons. And I've been able to understand the Company and really -- I'm really proud to be here and it's proud to all of the Brazilians to have a Company like BRF. And I would like to take this opportunity to highlight the work that has been done so far since the merging and especially to follow CADE determinations. And that all has been done with a lot of competence and with a lot of professionalism.

I'm just coming in. And when I look back and see all the work that has been done by Fay and the whole team, we really have to congratulate them. Probably it was not easy. It was not simple to follow all the guidances and rules. But the Company now is ready -- is ready to be whatever it wants to be. The Company is ready to be what we can make happen.

The opportunities in the domestic market are huge, although our share is already very relevant. But we still have room to grow. Not with acquisitions. But we can grow organically. And especially improving processes, improving other things that can be done best. We have room, we have the launching of new products, a lot of things to do in the domestic market.

But a Company that is in such a position in its original country in Brazil and being Brazil, a country that can be considered the barn of the world, we believe that our mission is really to supply the world. We supply Brazil and the world. It's inevitable. And this is good for the Company and important as well.

If you study the history of companies, you will be able to see that the ones that became international -- internationally well succeeded are also well succeeded in their country of origin. That company then takes on new challenges, new habits, it goes to new people, new countries. And the domestic markets of that company is also benefited. You can check all the well successful companies in the world have gone through that path.

Obviously, what we want in the international market is to still sell commodities, of course. We are not going to be decreasing that. But we also want to sell brands. And I'm amazed to see, because right now at this stage where we are, I talked to representatives of investment funds from Saudi Arabia and I was really impacted to see what they thought about our brand, Sadia. We are very strong in their world without going into countries such as Indonesia, which corresponds to the poorest population in the world. Also, Malaysia, Philippines. I just mentioned Indonesia because that's the poorest country in the world in terms of population and it's a whole new world to get into.

We also can do a lot of things in Europe. Europe has a lower consumption. But they also have consumption, even the United States, there's a lot to be done. It's a challenge that something the Company will face and will take on. But you may be sure, we'll carefully look at every investment we will make and we will analyze always the return for our shareholders. Each cent of our CapEx is going to be analyzed in terms of returns to our shareholders. And I, as the Chairman of the Board, will make sure that happens because I want to make sure that shareholders are really having a good return.

And the Company is ready to grow. In the industrial area, we have wonderful products. So I'm sure products are excellent, you all know about it. And when we have a good product, what is important is to know how to sell it, both in the domestic as well as international market. I'm not going to tell you where we are going to go first or more or less because we do have room to grow domestically. But the world is available to us and the Company is here to do what it knows what to do.

A - Unidentified Speaker

Just adding to Thiago's question, I'm talking about the synergy. If you remind we told you that we were going to bring you details up to 2012. So from now on we are not going to bring more details. But since this is a special meeting, we will give you some figures. Just to make sure you know that we are on track with our target of BRL1 billion, we are -- in our synergy, we are around BRL248 million. That's what we are having in terms of synergy with the projects identified in the beginning of the merging. So we are on track with our target.

Okay. Another question?

Operator

Excuse me, ladies and gentlemen. We will now begin the question-and-answer session. Each participant may ask only one question. (Operator Instructions) Our next question comes from the audio of Mr. Alexander Robarts from Citibank.

Q - Alexander Robarts {BIO 1499637 <GO>}

Hello. Good morning, everyone. And thank you. My question is also about the synergies. And thank you for the answer. I would like to better understand it. I know that a key source of synergies this year is the integration of the distribution network of Sadia/Perdigao. Can you tell us a little bit, how that integration process is going? We've seen -- have we seen an impact, a benefit from that integration?

And the second question is related to the foreign market. In the Fourth Quarter, you talked about the transformation process and the purpose of increasing -- deceleration in the foreign market reaching 30%. Can you give us an update on that process? Thank you.

A - Jose Antonio do Prado Fay {BIO 15337837 <GO>}

Alex, now, first talking about the foreign market. The acquisition of Federal Foods had this purpose. We already had developed a distribution in Europe. Also there, we have another standard. Our service to the market there, we have B2B and retail food service. This is our Europe brand -- we have talked about it already. In Argentina, we have a very sound distribution position with Patch. And they have 50% of the hamburger market. They're leaders in Argentina. We talked about other areas as well.

And now, we are in the Emirates and we have these two main areas, the acquisition of distribution structure -- some in our area, some are not. And also, something else that is essential, something that is going to increase our presence in processed foods, which is processing out of Brazil. We have a factory in Abu Dhabi. There was a major problem acquiring licenses. But now everything is okay. So by the end of this year and the beginning of the next year, that plant will be operating. And other will come -- we will do the same thing in that direction.

In terms of synergies. So far our main synergy source comes from supply. And that was already our project. We have established a supply process that is very effective, bringing good results to the Company. And the synergy is spreaded by the CPV and expenses. That's why sometimes it's difficult to identify. Because of that, we have that system that we used from 2009 and on. I had meetings -- one-on-one meetings where people asked me, where are these BRL1.5 billion? So that's why we have established those 12 months of 2009 and from then on we started measuring.

And our main source, as I said, is supply. Now, we need to work jointly with our front-end, that is, we can now from the second half of this year to operate our distribution capacities, all of them together. But we still will need some adjustments in the system. But I'm sure that from now on this is going to bring a lot of value to the Company. That is the possibility of being able to work jointly with our whole portfolio of brands and customers, because we still have a small overlap between customers from Sadia, Batavo, Perdigao, Qualy. And now we'll be able to work with the market on that after the second half of the year on.

A - Abilio dos Santos Diniz {BIO 1781457 <GO>}

Right now I would like to take this opportunity and say goodbye to you because I need to leave. I, once again, would like to highlight that it's been very good to be with this Company and also to have this role in the Board of Directors. And I'm feeling very well. And I see the Company has a good perspective and I can help to make this one of the most important food companies in the world. I believe that the next time we are together I'll have more learned lessons and will be able to talk a little bit more to you. Thank you very much.

Operator

Our next question comes from Mr. Fernando Ferreira from Bank of America.

Q - Fernando Ferreira {BIO 2389113 <GO>}

Good morning, everyone. You were talking about turning BRF into a global Company. So I would like to know if BRF '15 plan is still intact or if that strategic plan also can be revisited in the next month.

A - Jose Antonio do Prado Fay {BIO 15337837 <GO>}

BRF '15 plan was extremely important in this period of time because we needed a guidance to the Company and a quick guidance. Because we were joining companies such as Perdigao and Sadia. And each one of them had their own plan. So if we hadn't created a common plan, which is BRF '15, the Company would have a hard time going through that period with that growth strategy, delivering growth with no rupture.

So BRF '15 was very important in our planning and we are already going from the third to the fourth year. We are starting to write another plan, a new plan. That's why Abilio comes in in the right time. We will have a new Chairman with new strategic guidance for our Company. Anyway, everything that we have discussed, internationalization is still one of the main focuses of the Company, as we have been saying for a long time.

We need to become more globalized. We have been investing on that. And we have been preparing the Company for it, because during the merging we not only had a merging. But also it created infrastructure for growth. It's not enough to have the intent of becoming international. But we also need to create infrastructure. And that comes from the ability of the Company of managing the business globally. That is, to manage plants, people, sales. And that's why we're still in that major IT effort to be able to have the Company under the same SAP and ERP next year.

So we are rewriting our strategic plan with Abilio with us now in the board and the board changed a little bit. That's good, because he's coming in in the moment when we do not have any ruptures regarding BRF '15 and we are just writing a new period in our history.

A - Unidentified Speaker

Maybe we have time for one last question. Nobody from the internet. I don't know if you have any questions from the audience.

Operator

There are no further questions. So we'll give -- oh, there is one last question. No? No? No, no further questions.

A - Jose Antonio do Prado Fay {BIO 15337837 <GO>}

May I just do some closing remarks? I would just like to mention that -- well, if I were to summarize in a sentence if we are positive or not, we are bullish vis-a-vis the future. But we are cautious. We are bullish because in-house there are many things that give us a very clear vision of our capacity, of articulation of the Company cycle.

But why are we cautious? When you look at our fundamentals, think about this deep issue that has to do with volume and food inflation beating consumers. And consumers trying to find the right track. Cost shows good sign -- however, it still shows a couple of things. Chicago, for instance, that are high in corn, which is the pricing. But when you look at the fundamentals, the American corn crop is extremely delayed in plantation. We have about

5% today of the planted area in the US, where we should be with 37% or 38%. So that's an important warning sign.

When you concentrate the automation capacity of agri-business, well, this is really huge. They can recover over time. They can catch up. But when you contemplate planting, you also contemplate harvest. Any accident or environmental or weather accident during harvest always has a huge impact.

So we have volume, we also have cost. We are positive. But at the time same there is volatility. And on top of that, how should I put it, we also have -- well, the in-house things. We have some temporary expenses related to the merger.

In summary, I am positive about the year. But we have to be cautious constantly whenever we have to define or set costs and also come to a reposition of consumers trying to preserve their well being. Thank you very much. See you next time.

Operator

BRF SA conference call is concluded now. Thank you very much for joining us. Have a good day.