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Bloomberg Transcript

Q1 2016 Earnings Call

Company Participants

- José Alexandre Carneiro Borges
- Pedro de Andrade Faria

Other Participants

- Alexander Robarts
- Isabella Simonato
- Jeronimo De Guzman
- Lauren Torres

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen, and welcome to BRF SA Conference Call to discuss First Quarter 2016 Earnings. This conference call is being transmitted via webcast in our website, www.brf-br.com/ir. At this time, all participants are in a listen-only mode, and after the presentation, 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.

Forward-looking statements related to the company's businesses, perspectives, projections, results and the company's growth potential are provisions based on 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, thus, are subject to changes. As a reminder, this conference is being recorded.

This conference will be presented by Mr. Pedro Faria, Chief Executive Officer and Mr. José Alexandre Carneiro Borges, Chief Financial and Investor Relations Officer.

I will now hand the call over to Mr. Pedro Faria, who will begin the conference call. Mr. Pedro, you may begin.

Pedro de Andrade Faria {BIO 15115819 <GO>}

Good morning, ladies and gentlemen. Thank you for participating in our today's conference call. Despite of the challenging scenario due to the decline of the Brazilian economy and the rise of corn prices in Brazil, our first quarter result has proven the positive development of our business model. In the first quarter of 2016, we made important strategic progress. We announced another major acquisition, Calchaquí, enhancing our brand and products portfolio in the cold cut category in Argentina, creating relevant synergies with BRF operation and acquisitions in the region.

If we combine Calchaquí to the other acquisition, Campo Austral, the combined annual revenue will be around $190 million. With these two acquisitions, our (02:24) South Cone platform will have pro forma revenues of over $750 million, with iconic brandings portfolio such as Paty, Vieníssima, Calchaquí and Bocatti.

Despite this, we concluded the acquisitions of GFS in Thailand, Universal in the United Kingdom and our distributor in Qatar. In the case of GFS, we had positive surprises this quarter and we have already achieved higher-than-expected results. As of this first month, we have raised our internal projections and expect an EBITDA of around $50 million for 2016, which makes the acquisition really attractive in comparison to the prices we paid.

In addition to volume gains, we are working intensively on the commercial synergies of GFS and Universal EBITDA in our UK platform. We also have a dedicated supply team in – of Brazil working alongside our Thailand team, aiming for operational enhancement and neutral (03:24) learning, arising from the complementarity of the portfolios. We continue to work on synergy gains such as the better utilization of our global footprint and better agricultural feed conversion rate in GFS.

We also started exporting to new important markets such as Malaysia and Mexico, as well as some of the new plants that we have certified with export to (03:51) China. These actions combined not only brings growth and expand our global footprint, but 100% aligned with our strategy of advancing further down the value chain and transforming BRF into a global consumption company. Nevertheless, a perfect storm hit the sector this quarter, and its effects might extend until the end of the semester.

The main variables that guide the sector's profitability deteriorated at the same time. On one hand, Brazilian chicken production continues to be an all-time high, creating oversupply on the international market and strong availability in the domestic markets. This is also affecting pressure in dollar prices. On the other hand, we witnessed an appreciation of the FX rate in March that is pressuring our prices in reais, alongside, of course, the rise of about 50% year-over-year in corn prices that was completely uncorrelated with the global corn price dynamics, thus, reducing the profitability and the competitiveness of the Brazilian industry (04:56).

However, the results coming from our transformation we are implementing in our international are starting to appear. Volumes rose 17.2% year-over-year. And even if we exclude recent acquisitions, we would still record a double-digit growth in our international platform. Another important point I would like to highlight and I'd like to give you more details afterwards is the greater resilience of margins where we have moved forward in the local direct distribution models, analyzing both Middle East and Europe regions where this model is already more developed.

We noticed that the volatility in margin is much lower in comparison to the markets. We're still very much focused on the export of in-natura basic products, such as Eurasia and

African regions. Thus, in the midst of this very strong unfavorable cycle, our international market reported EBITDA margins of 12.5%, which compares to the maximum margins we used to achieve in previous cycles. Worth remembering that in some similar adverse cycles, our margins have hovered around zero margin sometimes.

In the Brazilian markets, our focus is to regain the profitability in our operations. Early January, we made a realignment in prices of 10% on average. This increase was done in a very granular and specific ways, enabling us to make a price repositioning between channels and regions, correcting some disparities (06:31) that exists. However, the pressure in costs coming from corn prices continues to be high. Total increase will not be enough to restore our margins as we would like. So, we have already registered a new round of price realignments for May of approximately 7%.

Another very important topic in Brazil is our innovation platform. We launched new products in the quarter such as Salamitos, a pioneer in the proteins mix (06:57) category, and absolute sales success. Also the new lines of ready meals of Sadia and Perdigão which continued to record very favorable sales metrics. These releases are 100% aligned with our strategy of revitalizing our portfolio and our innovation progress, especially to support our Sadia brands.

In addition, we continue to invest heavily in our teams and the improvement of our performance, building up a lot of projects around efficiency and service levels, along with our commercial and logistic teams (07:35) relationship with our customers, and bring further productivity gains to our results.

Regardless of the adverse short-term scenarios, we are maintaining our investment program of more than BRL 22 billion (07:47) in 2016 in order to support our global expansion, as well as the long-term strategy. Undoubtedly, this is only possible because of our strong cash position of around BRL 8 billion. We ended the first quarter with a net leverage of 1.69 times our EBITDA even after the payment of acquisitions, dividends and our buyback programs. Worth to remember that in 2012 when we had a similar unfavorable cycle, our leverage peak at (08:18) 3 times our EBITDA and quickly returned back to normal levels once the cycle reversed. We expect the same phenomenon to happen on top of our already very strong financial condition.

Finally, we continue very at ease from a financial point of view in order to pass through these challenging years. Without deviating from our long-term strategy, we continue our short-term efforts to intensify cost and expense cuts, and further enhance the commercial and logistic performance of our operation.

Now, I will give the floor to Alex Borges, our CFO, who will discuss in greater detail our financial highlights of first quarter 2016.

José Alexandre Carneiro Borges

Thank you, Pedro. I will sort out some relevant financial data for the first quarter 2016. Our net revenues increased 15.2%, reaching BRL 1.8 billion in the quarter. Our gross profit dropped by 6.1%, and we had a contraction of 5.7 percentile (09:22) points in our gross margin when compared to the last year. This result was a consequence of the cycle we are going through.

On the other hand, we managed to control our SG&A well. If we had to add to the base of the first quarter 2015, the expenses coming from the acquisitions and the increase in volumes as well as the impact of the foreign exchange variation and the dollar-based operation expenses and the impact of this inflation, we should have had an increase of approximately 23% in the SG&A quarter-over-quarter. Therefore, the increase of only 12.6% year-over-year in the SG&A represent the strong efforts to control our expenses and an operational efficiency gains of about BRL 125 million in this quarter alone.

In relation to the other operating results, we reported an expense of BRL 46 million. In this quarter, unlike previous quarters, we didn't have significant non-recurring events impacting the company's results. We'll reach in the quarter an EBITDA of BRL 1.025 billion in the quarter, an increase of 8.4% versus the previous year, with a margin of 12.6%. Starting from a gross margin that was 5.7 percentile points below last year, we had a decrease of only 0.9 percentile points in the consolidated EBITDA margins.

It's worth mentioning that this lower margin impacted mainly by the international markets is still around 4 percentile points higher than the margin that we achieved in 2012, a period when we also faced a down-cycle. About the financial results, I would like to give you more details about the impact behind this negative result of BRL 202 million on FX variation and others. In order to give you a better understanding, I would like to highlight that we have around $3 billion in assets and around $3 billion in liabilities running on average in our balance sheet.

In our hedge strategy, we actively try to match these assets and liabilities in order to have a neutral balance position. In other words, we do not take positions in either directions of the currency, and we try to maintain a neutral position as much as possible. But the reality is that this is not a perfect process, and we may have some mismatches here and there during the time and that generates impact in our FX variation.

Specifically March, we were holding an average loan position of around $200 million to match the payments of some acquisitions we had to do in the period and this generated a negative impact of BRL 90 million in our financial results.

Besides this negative result, we also had a low corn position of the CBOT as part of our commodities hedge policy to protect from potential variations of the corn price in the Brazilian market. The reality was this hedge really did not work mainly because the corn prices in Brazil significantly increased in price and completely decoupled to the Chicago prices expressed in reais terms. These generated a negative additional effect of BRL 50 million in the quarter.

Now, going to the results by region, I'd like to explain the new format of disclosure of results that we started to use this quarter. First, we started to disclose a gross profit in the EBITDA per region with their respective margins. Second, we now report Africa as autonomous region. And finally, to better understand our operational performance of each region, we have removed the non-core products, the sale of non-core products from the rest of respective results and now they can be followed in other segments. And we have also moved the impact of non-recurring and extraordinary expenses or revenues to the line that it's now called the corporate category.

We also started to disclose rich international regions, the CFR exports volume from our Brazilian platform (13:59) generally composed (14:03) low value-added and more exposure to the fluctuation of our industry cycles.

In relation to the results of the Brazilian region, the main highlight we had in the quarter was the increase on average prices invested (14:20) early in January of approximately 10%. Although this impact has increased, (14:27) has not been fully reflected in this last quarter. We were able to increase our average price in the quarter, 8.4% versus last year. Because of this price increase, we saw our volumes in Brazil reduced by 10% in the quarter against the previous years with an approximately 13% drop in the volumes in January and February and a 5% drop in the volumes of March.

For the second quarter, we will apply new price increases aiming to continue the process of recovering our profitability in this market even if it results in some additional pressure on our volumes. It's worth calling attention once again to our discipline in our expenses. Even with the retraction of the gross margin up to 3.8 percentile points in the quarter, we're able to keep our EBITDA margins flat in that year-on-year comparison.

In Middle East in the first quarter of 2016, we have 3.9% growth in volumes versus previous year with a special highlight to the 27.1% growth in the volumes of profit products. The result of the region was impacted by the cycle, mainly due to the decline of the margins of direct exports of in-natura products from Brazil. The initiatives to advance in the value chain especially those related to our own – to build our (16:00) own distribution network and increasing the volumes of processed products were very important initiatives to protect our margins in the regions.

To give an idea of the relevance of this process and the relevance of really advancing the supply chain, we have an average gross margins of about 15 percentage points in this last quarter, above the margins achieved in exports in (16:27) in-natura business directly from Brazil of 2016.

In Asia, we achieved, in the first quarter, a volume of 44.4%, higher than the previous year. A result of entering new markets and the consolidation of volume of the GFS, our acquisition in Thailand, which represented about half of this growth. On other hand, as the market is predominantly direct exports of in-natura products from Brazil, our results suffer strongly with the cycle. Thus, the region showed a decrease of 15.8 percentile points in EBITDA margin versus – in that first quarter 2006 versus the previous year. Still, we kept operation EBITDA margins above 14%, which we believe is very positive results for the region.

In Europe, our margins were also impacted by the cycle especially in Russia where we saw negative EBITDA margins in this market. However, just like Middle East where we moved forward in the value chain and improved our mix of products, the difference in margin between local distribution and exports was 14 percentile points. In other words, moving to direct distribution, advancing the chain and increasing our margins is a strategic direction to which we are pursuing in this international market.

Finally, I would like to end my comments by highlighting that we have ended the quarter with a net debt of BRL 10.1 billion and a net financial leverage of 1.69 times net debt to EBITDA. Excluding the payment of acquisitions that we have done in this quarter of approximately BRL 2.3 billion, our leverage would have been 3.37 times. It's worth noting that in 2002, we also faced unfavorable cycle. Our leverage got all the way up to nearly three times.

(18:45-18:50)

Q&A

Operator

Excuse me, ladies and gentlemen, we will now begin the question-and-answer session. Our first question comes from Lauren Torres, UBS.

Q - Lauren Torres {BIO 7323680 <GO>}

Yes. Hi. Good morning, everyone. I appreciate hearing your confidence on your long-term strategy or the ability to execute that strategy, right. And I don't want to be too short-term focused here, but you talked a lot about these moving parts more working against you, I guess, in the short term. So, could you (19:38) I mean, I don't know if your worst quarter now is behind you, but with respect to chicken supply, currency, corn prices, it seems like you are putting initiatives in place to manage this. But I guess I'm just trying to get a sense for the short term, if things get worst for you, if you feel you have enough things in place to offset this pressure or will see some continued pressure like we did in the first quarter. Thanks.

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

Lauren, thanks for your question. I don't think we're being too short-term. We are, of course, carefully managing the variables we control, and trying to position ourselves for the variables we cannot control. Of course, we're trying to create a clear distinction of what we think is the normal cycle of this industry, with oversupply trends which I think will tend to fade into the second half of the year, and abnormally high price in Brazil which represent a complete deviation from any kind (20:49) historically. We think those are the variables we cannot control. I think we have put in place a number of mitigating actions here. So, of course, we are not getting the full impact of increase of more than 60% in our most important raw material.

So, I think the set of numbers we are showing in here proves the resilience of the model in light of the variables we don't control. Should things get worst, which I think goes to your point , of course we will need to find additional measures to put in place, and of course, they would (21:13) go in the line of even strengthening the (21:18) and cost control of the variables we can control.

Q - Lauren Torres {BIO 7323680 <GO>}

Okay. Thank you.

Operator

The next question comes from Alex Robarts, Citi.

Q - Alexander Robarts {BIO 1499637 <GO>}

Thanks. Hi, everybody. I wanted to go back to the international business. And when you look at the five segments in the quarter including Brazil, the only segment where you get a very clear operating leverage and margin expansion is in Latin America. And so, it wasn't really touched on in the Portuguese call, but can you talk to us about how that region has evolved and kind of give yourselves a report card of where you are in the process of building out three pillars of the Middle East, like the local production, the brand and the direct distribution?

I mean, can we start thinking about Latin America as a double-digit EBITDA margin business this year? So, kind of where are you in this process of rolling out and kind of working toward this distribution, local production and branding process that you've done so well in the Middle East? Thanks. That's the first question.

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

Alex, thank you for your question. And I think you're right to say that we didn't touch much on the one region which we seem to have expansion in our profits. So, we are very excited with the progress we made in the South Cone. Okay? We announced a series of three acquisitions in the last six months to eight months. They all come together to create what we believe is a winning platform in Argentina.

To give you kind of a ballpark sense of it, once those integrations are in place, South Cone and Argentina, in particular, becomes a platform with total sales to the tune of $750 million annually, with, I think, a dramatic opportunity for us to integrate them in a way that we can see margin expansions coming from we have (23:40) a bigger cloud into the market with our clients with, of course, clear leadership in some important categories like burgers and franks and our cold cuts.

So once that lesson comes into play, and I think we've played that from our position of strength combining both Sadia as our global brand, but also uniquely position iconic brand in that market, we see a very bright future. Of course, short term, a lot of challenges integration, still too early to tell. Of course, a lot of these locations in Argentina with recent change in administration, so of course a big attempt of controlling (24:22) of the macroeconomic variables. But I'd like to say that we are excited to be building along the three pillars that you have mentioned, distribution, capability, local production and iconic brand.

A - José Alexandre Carneiro Borges

Alex, just to complement (24:41) the benefits for being a GM for the region for the last – a little bit of over two years. What we have seen in the region, it's a gradual improvement on profitability quarter-over-quarter. Starting from third quarter last year, we have consistently seen between 4 percentile points to 5 percentile points expansion in EBITDA margins versus the previous year. So this is – it's a lot of (25:04) exercise of recovering the profitability in the region and trying to grow exactly what you just say which is very, very strong local platform of our consumer-oriented business, strong brand distribution and also with the support of the local production.

So to see what we have disclosed this quarter as well, direct sales from Brazil to the region represent between 20% to 25%. So, among the regions, international regions that's the lowest percentage that we have, meaning that the local business with the local distribution, local dynamics is stronger. So, in one sense, this is the closest that we have to the Brazilian reality that we have. So, our expectations as we consolidate, integrate the acquisitions we have done, that should happen at least partially in the second quarter.

And we have also disclosed the numbers for the combined acquisition that we did recently, the Campo Austral and Calchaquí. Those two companies together had close to $190 million in revenues last year with EBITDA close to $30 million. So, if you add all this up, we should continue to see growth in the region. (26:34) in processed products in the regions. So, we are expecting to continue to see growth, and we're very confident with the long term.

But having said that, short term has been bumpy. It has been bumpy in Argentina. Inflation is putting a lot of pressure. We believe the government is taking the right measures and going to the right directions. But short term, it's been challenging in Argentina. But we're very confident that we are building a very solid platform in LatAm, and we expect this continue to deliver solid results going forward.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay. Great. And the last question is just on the Middle East, that was discussed earlier. And before saying this, I wanted – asking the question, just saying, I appreciate the increased financial disclosure at a time when certain companies are closing up. This has been a helpful press release.

But look, going into the Middle East, I mean, one of the things I don't think was kind of discussed a lot is how you're ramping up in Abu Dhabi. This was something that I guess you're coming into your second year. You started to sell in Q – in the Saudi Arabia. How are you feeling with the ramp-up of that plan? It seems to be obviously driving this 27% growth in the processed volume in the quarter.

But are we going to – do you think we'll get you on track to get to 1,000-ton capacity? Are we going to hold back on that? So, kind of talk a little bit about your production, local production footprint in the Gulf with Abu Dhabi. That'd be great. Thank you.

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

Thank you very much, Alex. I think we are, as we discussed before, ramping up ahead of the original plan, facing some important challenges that I think have been dealt adequately. I'll give you a sense that given the corn price situation in Brazil, a lot of the raw material inputs coming from Brazil have to be replaced by alternatives even locally. We are sourcing now raw materials most (28:47) in the region and globally. So, this is one point.

When it comes to indirect costs, I think we are diluting them in the factory much ahead of the plan. I'm very positively surprised with the work that the leaders of that factory are doing. We're still managing that plant, which is very satisfactory to me without – (29:09) accident and AGC ratios, the culture coming together.

So, yes, we already started the expansion of that plant which is going (29:20) seeing the biggest improvement. I'll give you one example. On the poultry part, we are now solidly moving into three shifts of their plant and we are even sourcing (29:33) high value-added poultry cuts from Brazil in the new ways of integration, so we are expanding there. We also have all the areas which we have seen a little bit less success, but I think it's all part of the game.

I think the main method here is yes, we're growing 27% year-on-year on the high value-added offering, now that we're integrating the silent platform, if you become also a supplier of Abu Dhabi factories in a way that we can sort very interesting products from Thailand, further process them into Abu Dhabi, and then onto Saudi.

I don't know if this is known, but Saudi Arabia doesn't have certifications approved for Thailand factories, but the fact that we can further process in Abu Dhabi allows us to pass into that market, so, I think it's coming together quite nicely. Of course, some challenges, as I said, the Brazilian raw materials which are now quote, unquote, more expensive than what we can find, but I think (30:36) sourcing platform there, so we're able to mitigate that with supplier from our fields globally.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay. Got it. Thank you.

Operator

The next question comes from Jeronimo De Guzman, Morgan Stanley.

Q - Jeronimo De Guzman {BIO 15888043 <GO>}

Hi. Good morning. I wanted to go back to the volume performance you had in Brazil. I just wanted to understand the processed food volume decline of 11.4% – in processed foods relative to the industry growth that you mentioned, which was 1.3%. So I just wanted to help – see if you can help us understand that gap. I understand that pricing had an impact on it, but I also had the impression that your main competitor had kicked in similar pricing. So, I wanted to understand what else then could be driving the gap? Is it competition? Is it channels or something else that we should keep in mind?

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

Thank you, Jeronimo. So, I think you are raising a very important point. As we mentioned in the call in Portuguese, we think that we, as leaders, we have been impacted by being kind of the first to try realigned prices, which had a big impact when you look at it in a more granular fashion into the channels because we were discussing a 10% realignment in prices. But the effect it had on some channels was much more pronounced than that. Meaningfully, wholesale and some indirect distribution channel that we operate with. So, I think there's also channel stocking – this stocking trends here which lead to this big fall in volumes. When we look at our market share losses, we lost about 0.9 percentage points here, which will translate kind of volume decrease of 2%.

You mentioned competitors are also realigning prices. This is true. But they are doing so with a lag from our movement. So, the natural trend will be for us to short term lose some market share, which we expect to gain coming from the several initiatives we have in place to deal with bigger distribution, higher levels of service to certain channels, and of course, the rollout of our innovation platform which is getting very strong reaction in the marketplace.

A - José Alexandre Carneiro Borges

And just to complement, Jeronimo, it's Alex. And you were talking about another price increase in the second quarter. And as Pedro said, the competition had a delay to flow it through in our price increase. And they had done so more strongly, more recently as (33:35) movement of the competition adjusting the price. So, that's why we're also confident that going forward we should successfully be able to make this movement.

Just to highlight, again as we disclosed in our report, the 11% was very concentrated in January and February. Those are the months where we saw the news of the (34:04) competition. And as of March, this gap is much lower, only 5%. And remember as Pedro say, this is a sell-in, sell-in from us to the channels, right? The sell-out, the market shares indicate that we have not lost as much as of a ground. So, that's what give us the confidence that in this process of recovering profitability, yes, we may see some pressure in volumes, but we're very confident that we are moving in the right direction here.

Q - Jeronimo De Guzman {BIO 15888043 <GO>}

Thanks. That's very helpful. And are you seeing any restocking in the channel already as you look at April or is the sell-in still under pressure?

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

We saw a bit of that in March. As we talked about April, of course, the market starts to have some kind of impact of already announced price increases. Another very important point, Jeronimo, we're discussing this, and it's not like the Brazilian market is standing still, okay? We're seeing a downtrend. We're still seeing a very difficult situation from the consumer standpoint. So, all of these also impacting the way that we are operating. Having said that, I agree with Alex. This is the moment that we as leaders we need to realign prices based on the cost pressures we've seen on corn and many of the other inputs. So, I think that certain things should translate into long-term gains if we execute well enough.

Q - Jeronimo De Guzman {BIO 15888043 <GO>}

Okay. Great. Well, thank you very much.

Operator

The next question comes from Fernando Ferreira, Bank of America.

Q - Isabella Simonato {BIO 16693071 <GO>}

Good morning. This is Isabella Simonato. I have two questions. First one, in the Middle East, again, if you could share with us your expectations in terms of what the mix of processed foods represent in the short term and in the midterm? We understand that volumes (36:00) have been performing pretty well, but still 8% of your mix, so what we can expect going forward?

And also, in the Middle East, if you could share with us the difference between own distribution and third-party on the EBIT margin basis. I mean, we understood the difference on a gross profit – gross margin basis, but if you could share with us on an EBIT margin basis which would be much appreciated. This is the first question. Thank you.

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

Thank you for your question. I'll start with the second part of the question around this local distribution and what it means. We try to provide some guidance around what are the kind of gross margin improvement we get from changing from our CFR model into DDP, in direct distribution in the Middle East, it's almost 50 percentage points as recorded in the first quarter. Remember, this gap is also dynamic over time. So, meaning that when we have a high cycle like we had maybe last year, that 50 percentage points will be likely less and when we have a low cycle, the resilience of our distribution model makes that gap increase, okay? So, this is what's happening right now.

Of course, we had a complete different layer of expenses to be able to operate. So, running (37:33) our distribution, having our own salespeople, incurring all kinds of trade marketing activity, promotion, et cetera. But of course, the improvement by the overall increase in our profitability in the Middle East, it really means that there's a big accretion in the EBIT margin. I'm not ready to disclose what it means, but essentially, it's a very positive impact, and I think you can correlate that from historical numbers we have disclosed to the market.

Can you repeat the second question?

Q - Isabella Simonato {BIO 16693071 <GO>}

The first quarter portfolio, how (38:09)...

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

Yeah, portfolio, you did mention that processed still represents shy 8%, but I think that's not the way we should look at it, because at the end of the day, our game is to increase market share and expand penetration of those categories. Of course, it's coming from being likely less than 2% or 3% in 2013 and coming to 8%, so the growth in that line is significant. I will also point out the growth we are having on poultry products which we expect to be really broad and meaningful in terms of shift (38:42). I think the Middle East consumer is really migrating fast from whole birds to poultry products which, of course, have the new layer of convenience to be offered with marination, with (39:00), et cetera. So, that's why we are excited with the – why I think is the one line that we roll out which -- the greater level of success on Abu Dhabi. So, you could expect a meaningful change in the mix. It will not translate in this becoming half of the business we do, but just because the fundamental base logo (39:17) that business continues to be the chicken supply, which, again, is not a commodity, is a branded offering. It commands a significant premium versus the competitive offering. And we continue to gain market share in all of those categories.

Q - Isabella Simonato {BIO 16693071 <GO>}

Perfect. Perfect. Thank you for your answer. And second question would be on working capital. We saw this quarter that there was a significant impact from suppliers and also other rights and obligations line, if you could give us more details on the reasons for this negative impact in this quarter and how that should perform going forward? Thank you.

A - José Alexandre Carneiro Borges

Isabella, it's Alex. Obviously as we move forward in our strategic model (40:35) distribution to get closer to our consumers, we do see (40:16) our working capital mainly in stocks, in accounts and receivables. In other words, for a model before when we ship out and once you put the goods on a ship, the goods are no longer in our balance sheet. Now, we still hold them in the water (40:35) the final, the warehouses until you get the final distribution and stuff. So, we are seeing some impact on average this change (40:49) model has impacted us about close to two days in the cycle or concluding (40:51) the cycle – the cash cycle. But you can see it's more than mitigated by the increase in profitability that we gained from this business (41:02).

So, what we saw (41:06) working capital has to do with that. It has to do also the acquisitions that we did, GFS, also the whole plant, and the inventories and the working capital coming from there and from acquisitions we did in Europe as well. So, this is a model that we continue to be very disciplined to pursue that savings and be as efficient as possible. But, yes, we should see some increase – some margin increase in our cash cycle reflected in the working capital.

Q - Isabella Simonato {BIO 16693071 <GO>}

That was very clear. Thank you.

Operator

This concludes today's question-and-answer session. I would like to pass the floor again to Mr. Pedro Faria.

A - Pedro de Andrade Faria {BIO 15115819 <GO>}

Thank you. I would like to appreciate all of those participants in our first quarter conference call. As we've said in the previous call in Portuguese, we remain very confident in the long-term strategy. I believe that in the line of what we have called a perfect storm from pressures coming from corn prices and, of course, oversupply hitting our price in dollars, and a lot of volatility effects, I think our model has proven resilient. We are still not satisfied. We think we have still room to improve internally in the areas we control. But I believe we are in solid grounds here and a difficult quarter has proven that our ability to unlock value for shareholders continue intact for the future. Thank you very much.

Operator

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