

THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

TSN - Q1 2015 Tyson Foods Earnings Conference Call

EVENT DATE/TIME: JANUARY 30, 2015 / 2:00PM GMT

OVERVIEW:

Co. reported 1Q15 revenue of \$10.8b and adjusted EPS of \$0.77. Expects FY15 revenues to be approx. \$42b and adjusted EPS to be \$0.30-3.40.



CORPORATE PARTICIPANTS

Jon Kathol *Tyson Foods, Inc. - VP of IR*

Donnie Smith *Tyson Foods, Inc. - President and CEO*

Dennis Leatherby *Tyson Foods, Inc. - EVP and CFO*

CONFERENCE CALL PARTICIPANTS

David Palmer *RBC Capital Markets - Analyst*

Akshay Jagdale *KeyBanc Capital Markets - Analyst*

Robert Moskow *Credit Suisse - Analyst*

Adam Samuelson *Goldman Sachs - Analyst*

Ken Goldman *JPMorgan - Analyst*

Tim Ramey *Pivotal Research Group - Analyst*

Farha Aslam *Stephens Inc. - Analyst*

Brett Hundley *BB&T Capital Markets - Analyst*

Tim Tiberio *Miller Tabak - Analyst*

Diane Geissler *CLSA Limited - Analyst*

Michael Piken *Cleveland Research Company - Analyst*

Ken Zaslow *Bank of Montreal - Analyst*

PRESENTATION

Operator

Welcome to the Tyson Quarterly Investor earnings call. This call is being recorded. If you have any objections, you may disconnect.

(Operator Instructions)

Now, I'd like to turn conference over to Mr. Jon Kathol, Vice President of Investor Relations. Sir, you may begin.

Jon Kathol - *Tyson Foods, Inc. - VP of IR*

Good morning and thank you for joining us today for Tyson Foods conference call for the first quarter of FY15. On today's call are Donnie Smith, President and Chief Executive Officer, and Dennis Leatherby, Executive Vice President and Chief Financial Officer. Our remarks today include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995.

These statements are subject to risks and uncertainties that could cause actual results to differ materially from our expectations and projections. I encourage you to read today's press release and our filings with the Securities and Exchange Commission for a discussion of the risks that can affect our business. Following our prepared marks, we'll go to Q&A.

To ensure we get to as many of you as possible, please limit yourself to one question and one follow-up and then get back into the queue for any additional questions. Because our annual meeting of shareholders takes place this morning, we will need to stay on schedule by ending Q&A at



the top of the hour. We hope to get to all of your questions, but we'll have to put a hard stop on the call to get to the shareholders meeting on time. I'll now turn the call over to Donnie Smith.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Thanks, Jon. Thanks to all of you for joining us today. Q1 was another great quarter with adjusted earnings of \$0.77 a share. Sales were a record \$10.8 billion, up 23% from last year. Adjusted operating income was a record \$564 million, which is a 37% improvement year over year. Our overall adjusted operating margin was 5.2% and we reduced debt by \$650 million in the quarter.

We realized \$60 million of synergies in Q1 and we're on pace to exceed \$225 million in synergies for the fiscal year in operational improvements, procurement, manufacturing logistics, and organizational change. We're off to a fast start and we're confident in our ability to achieve at least the \$500 million target set for the end of FY17. Let's take a look at the operating segments.

In Q1, the Chicken segment reported a record 12.6% return on sales with volume up 3.1% and average pricing up 1.5%. Industry-dollar growth for retail fresh chicken was up 8% and our growth was in step with the overall strong industry growth. We maintained the number one branded share in fresh, individually frozen, and cornish chicken and demand is very strong, especially for fresh tray pack. In fact, we're still short of supply in tray pack.

The food services industry saw much needed growth in our fiscal Q1 and I'm pleased to say that Tyson's chicken sales growth at food surface was more than double that of the restaurant industry on a sales-dollar basis. The production issues in two of our value-added chicken plants last year are resolved and all of our lines are operational. We're now working to fill the pipeline and fulfill the pent-up demand.

By the end of Q1, we had regained a little over 2 share points and we'll continue to expand our distribution and regain the lost share in Tyson's frozen cooked chicken. USDA indicates an increase in production of 3% this fiscal year. Although other more recent data might indicate a greater increase in supply, we believe demand will more than keep pace.

With this strong demand, a shift to a more profitable mix, strong pricing, and increased further processing capacity, we now think our return on sales will be above 11% for the remainder of the year. There looks to be more chicken supply to come in 2016 as well, and we're working on plans to capitalize on it. We created our buy-versus-grow strategy for this scenario and we see it as an opportunity to value up.

The Beef segment was just under breakeven for the quarter. Volume was down 2.7% with average pricing up nearly 21%. Continued record high beef prices at retail have caused a shift in consumption away from beef towards other proteins, leading to margin compression in our beef business. Despite marginal losses, we improved our position relative to industry indexes. We have adjusted our slaughter to recover margins and have already seen improvement in Q2; however, the segment will continue to be challenged in the quarter.

I'll hurry on to say that the pressure in our Beef segment has been more than offset by benefits we see from the balance of our portfolio. Our Pork segment had a 7.9% return on sales in the first quarter. Volume was up 1%, while average pricing increased 7% indicating strong demand. We expect further recovery from the PED virus and expect industry hog supplies to increase around 2% to 3% in FY15. It should be another good year for the Pork segment and we expect result similar to last year's.

The International segment had an operating loss of \$14 million, which was half of the loss compared to Q1 of 2014. The sale of our business in Brazil was finalized in Q1 and we expect the sale of our Mexico assets to be completed by the end of March. It's still a tough demand environment in China. Pork pricing has been pressured, which has also affected chicken. Wholesale poultry prices are down 10% since September and are now only about 2% above the trough we saw back in January of 2014.

We'll continue in a holding pattern with our operations in China as we await for demand to improve. Regarding our international exports, lower pricing has essentially offset the appreciation in the US dollar, allowing us to maintain our volume so far this year. Our primary concern about exports is coming from ongoing interruptions at West Coast ports, which is pressuring logistics that could eventually affect livestock producers if the situation isn't resolved soon.



Now moving on to Prepared Foods, the segment had an adjusted 5.2% return on sales for the first quarter. With the Hillshire brands integration, volume was up nearly 90% and average pricing was up 24%. On a pro forma basis, we had an unfavorable input cost impact of \$83 million, largely offset by synergy capture in pricing. We've streamlined our operation in Prepared Foods by closing plants, improving capacity utilization as we continue to tightly manage costs, invest in our brands, and drive our growth agenda.

The integration is going very well and it didn't take us long to realize that we're much stronger together. Let's use category [captaincies] as an example. Strategic retail customers see the benefit of leveraging our products, capabilities, and expertise to grow their business and, since combining Tyson and Hillshire, we've added 11 category captaincies for a total of 76, indicating our customers trust our insights and partnerships in leading category growth decisions.

In terms of macro trends affecting the industry, I'd like to address our perspective on the consumer marketplace and how we're capitalizing on shifting demand to grow our business and our customers' businesses. In the past quarter, consumer confidence, lower gas prices, and unemployment data were tailwinds that we expect will continue to favor food spending in the new year. But pressures like long-term unemployment and limited wage growth still weigh on a lot of people.

We've talked about this situation before as the bifurcated consumer, or the barbell economy, and it factors into consumer spending habits which, in part, drive our innovation agenda. We continue to see consumers moving from red meat to poultry and 68% say the cost of red meat is the reason they're making a shift. However, beef prices have remained at record levels because demand has been so strong among people who can afford it.

Chicken is the only protein to grow annual consumption during the past four years. Lower fuel prices appear to have benefited food purchases, both at grocery and food service, mainly at QSR. And casual dining, which saw traffic growth in our Q1 for the first time since the recession. There are also positive growth in on-site food service, such as lodging, deli, and healthcare, where we have a strong presence.

If lower gas prices continue into the summer, food service could see even more recovery. Our innovation pipeline is grounded in a strong understanding of these market dynamics, coupled with deep consumer insights. As you heard at Investor Day, we're gearing up for two new product platform launches for the back half of the year: Hillshire snacking and Ballpark jerky. This is in addition to our ongoing new product news that happens throughout the year.

We grew dollar sales in eight of nine tracked categories in Q1 behind pricing, but also supported by strong distribution in new products. We'll continue to build on this momentum with our advantage portfolio through brand building and innovation. We have a lot to be excited about at Tyson Foods. Q1 was a great quarter. While I don't expect our second quarter to be as good as Q1, because it's typically our most difficult, I do expect to be better than Q2 of last year.

We're reiterating our guidance of adjusted earnings in the range of \$3.30 to \$3.40 a share, with results weighted toward the back half of the year. We have a balanced, diversified business model and a focused growth agenda that give me confidence that, not only can we handle whatever challenges are ahead, we're going to thrive. Now, let's go to Dennis for the financial update.

Dennis Leatherby - *Tyson Foods, Inc. - EVP and CFO*

Thanks, Donnie, and good morning, everyone. This morning I will be referring to our first quarter adjusted operating income and EPS. Please refer to our press release issued earlier this morning for a full reconciliation of our GAAP to adjusted results. FY15 is off to a great start. With record sales, operating income, and operating cash flows, we were able to reduce debt by \$650 million.

First-quarter revenues were \$10.8 billion, representing over 23% growth compared to a year ago as we continue to execute our growth strategy, as evidenced by increased sales in Chicken, Beef, Pork, and Prepared Foods. Total Company adjusted return on sales for the quarter was 5.2% and adjusted operating income was \$564 million, representing a 37% increase over Q1 of 2014. Our adjusted earnings of \$0.77 per share represents a 7% increase over a strong comparative period a year ago.



We had record operating cash flow for the first quarter at \$812 million and we spent \$231 million on capital expenditures. This outpaced our depreciation by \$83 million, as we continued to invest in projects with a focus on delivering high ROIC. Our effective tax rate for the first quarter was 28.8%. On an adjusted basis, this rate was 34.8%. Net debt to EBITDA for the past 12 months was 3.5 times and on a gross debt to EBITDA basis, this measure was 3.7 times.

On a pro forma basis, including Hillshire's results for the past 12 months, net debt to EBITDA was 2.7 times on an adjusted basis. Including cash of \$381 million, net debt was \$7.1 billion. Total liquidity was just over \$1.6 billion, remaining above our goal of \$1.2 billion. Net interest expense was \$75 million during the first quarter. For the quarter, our diluted shares outstanding were 416 million. As Donnie pointed out, we closed on the sale of our Brazil chicken operation during the first quarter.

As a result of the sale, we received proceeds of \$130 million, with additional proceeds expected in the second quarter relating to the working-capital adjustment. The sale of our Mexico chicken operation is expected to close in the second quarter. Now, looking forward, here are some additional thoughts on 2015. Please note, our accounting cycle results in a 53-week year in FY15 as compared to a 52-week year in FY14.

Accordingly, this outlook is based on a 52-week year to make a better year-over-year comparison. We expect revenues of approximately \$42 billion for FY15, which is 12% growth over FY14. This is driven primarily by a full year of Hillshire Brands results, offset by a reduction from the sale of our Brazil and Mexico chicken operations. We expect to capture more than \$225 million in FY15 from our Prepared Foods, profit improvement initiatives, and Hillshire brands synergies.

Net interest expense should approximate \$280 million for FY15. We currently estimate our adjusted effective tax rate to be around 35.5%. CapEx is expected to be \$900 million, which represents approximately \$300 million, or 50% more than our depreciation expense, as we continue to focus on projects that will create long-term shareholder value. Based on our average share price in Q1, we expect our diluted shares in Q2 to remain around 416 million prior to considering any further changes in our stock price, which would impact the dilution from our tangible equity units.

Our priorities for the significant cash flows that our operations will continue to generate are for rapid deleveraging and strengthening our balance sheet, a continued focus on disciplined capital allocations to drive long-term shareholder value, and debt capacity to fund acquisitions to fulfill our growth strategies and to return cash to shareholders through share repurchases and dividends, all while ensuring we maintain plenty of liquidity.

We have a lot of momentum going into FY15 with the addition of the Hillshire business and team. We are pleased with our first quarter results, delivering 7% EPS growth over Q1 of FY14. Our Q2 should beat last year, but likely will be less than Q1, due to our typical seasonality, and the third and fourth quarters are expected to be really strong.

As we continue to capture synergies from combining two great businesses, we are confident we will deliver adjusted EPS within our range of \$3.30 to \$3.40 for FY15, which represents an increase of over 12% compared to FY14. This concludes our prepared remarks. Jane, we're ready to begin Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

David Palmer, RBC Capital Markets.

David Palmer - *RBC Capital Markets - Analyst*

You noted that chicken margins are expected to be above 11% for the remainder of the year and we've seen what's going on with supply growth. It seems to be inching up a little bit. What gives you confidence in that Chicken segment guidance?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

We've modeled our 2015 chicken performance using several models. I'm very confident in our ability to deliver 2015. If you look at, not only our brand leadership in fully cooked and in the fresh, IF, and Cornish categories at retail, plus our leadership in food service, we've got a great broad, balanced portfolio.

On top of that, we've made a lot of improvements in our sales mix. I mentioned in my prepared remarks that we've got great growth in tray pack. We going to have the FP capacity in place to be able to take advantage of further processing the business that we think will come our way in food service.

We've got a great innovation pipeline. We've made a lot of operational improvements and we'll continue to see benefit from our capital and investments. If you look at that balanced portfolio, our pricing structure, and these other factors, we'll deliver 2015.

David Palmer - *RBC Capital Markets - Analyst*

One question on the food service side, we're seeing a lot of demand, not just for protein but increasingly, there are players out there that want to upgrade the protein in some ways, assure consumers that it's all-natural. Maybe down the road, antibiotic-free chicken will be a bigger thing.

Is there an opportunity for Tyson with that? How big of a deal could that evolution or perhaps even a margin constraint -- could that be having to shift to perhaps a more natural product as demand shifts? Thanks.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

That's a great question. It appeals, frankly, both at food service and retail to a different consumer segment than what is broadly addressed by most of our portfolio today, which is great news for us. We've got a tremendous innovation engine. I think with our capabilities and our discovery center and our ability to drive innovation, I think we're advantaged in the ability to capture that.

I would also add that our live production team is about as good as there is in the industry when you look at benchmarking data. Actually, when you look at benchmarking data, they are the best in the industry, which, I think, gives us an advantage in what might be considered a little bit more challenging live production environment. I feel good about our opportunity to continue to capture on that in the future.

Our NAE line, which we launched May of a year ago or a little further, we've doubled it since the launch and our growth continues. We're adding about 100,000 birds a week to that business next month. We continue to see growth and we continue to use our supply chain to fill those needs.

David Palmer - *RBC Capital Markets - Analyst*

Thank you.

Operator

Akshay Jagdale, KeyBanc.

Akshay Jagdale - KeyBanc Capital Markets - Analyst

Congratulations on the chicken margin. I think as far as I can tell, it's the best I can remember in the history. Is that accurate?

Donnie Smith - Tyson Foods, Inc. - President and CEO

Yes.

Akshay Jagdale - KeyBanc Capital Markets - Analyst

My question, I'm going to start with -- I have two -- I'll start with, it's Hillshire-related, say acquisition-related, but it's more of an outlook on pork. Supply expected to increase on pork, all the hog prices have come down, the retail values have come down. Presumably, that should help a value-added pork business.

One, am I thinking of that generally correctly and two, what are the implications of that on your segment margins for Prepared Foods, which you maintained your guidance, as far as I can tell? That's my first question. I have a follow-up.

Donnie Smith - Tyson Foods, Inc. - President and CEO

Two things you should expect. Number one, with increased supply, that will likely also improve -- besides the Prepared Foods piece, which would come later, maybe Q4, Q1, Q2, Q1/Q2 of 2016, that type thing. You should also expect improvement in the back half in our Pork segment. So I think there, we will have a double advantage, if you will, inside of our portfolio.

But Akshay, you're absolutely thinking about it right, about an improvement in the raw material structure underneath our Prepared Foods business. At the retail brands, we're using our marketing support to position ourselves very well to take advantage of that.

Akshay Jagdale - KeyBanc Capital Markets - Analyst

So what does that mean for your -- how should we think of your guidance in relation to that?

Donnie Smith - Tyson Foods, Inc. - President and CEO

Got it. As we mentioned on the call, Q2 is always a bit challenging. We kind of made the right comments about that. We will see the improvements back-half loaded.

You'll see the run rate in Prepared Foods accelerating through the year and taking that momentum into 2016. It's still early in the year. So we're maintaining our current guidance at \$3.30 to \$3.40, but there's some things at play that could certainly advantage that.

Akshay Jagdale - KeyBanc Capital Markets - Analyst

Then, on Chicken, this quarter, obviously, very good, especially given that the spot margins sequentially declined. Yours expanded. So you're advantaged relative to spot expanded as well.

In light of that, you've obviously commented on your analyst day, that if and when the cycle turns, you'll be 500 basis points above on margins. Can you just conceptually help us understand why your business today is in a position to deliver those type of margins, even if the industry is not making money?



Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Sure. As we talked about in New York, we have a very balanced portfolio between the bird classes, the tray pack size, small birds, big birds, and the other sizes. That helps coupled with the pricing structures that we've worked with our customers on in the last couple of years.

Now, we have this balanced portfolio. We've got a very good balance of pricing structures and mechanisms, some that are tied to the market, some that aren't. Remember, we indexed -- we correlate a lot closer to the whole bird market values than we do to the breast meat values.

One of the things that might help is we do have -- I'm going to say X percent of our portfolio that is subject to, I'll call it market pricing, but we also have X percent of our portfolio that's very balanced to that, that we buy on the outside market. So when the price goes down on the portion of our portfolio that we sell based on market prices, we get a commensurate benefit in a different part of the portfolio from the lower cost of buying that raw material.

Add on top of that, we have a great brand presence, number one at retail in fully cooked, which we're rebuilding the category and we're number one in fresh tray pack. We're number one in IF. We're number one in Cornish. We have a leading brand in food service. You add all that together and our buy versus grow strategy positions us well to take advantage of this.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Great, I'll pass it on.

Operator

Robert Moskow, Credit Suisse.

Robert Moskow - *Credit Suisse - Analyst*

Thanks, Donnie. I think you've covered what happens when supply expands, but is it fair to say that the [excess] that came out in the industry data were above your expectations? I seem to remember, at the analyst day, you saying that you didn't think the 3% growth would continue. Is that fair to say?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

That is fair to say. Yes. What I was expecting was, we had that gap because people took cuts last season that they didn't take the season. I expected that to level off after January and that has not happened. That 3%-type number has continued.

Robert Moskow - *Credit Suisse - Analyst*

Okay. Whole bird prices, to your point, have done nothing but go up. You've seen some fluctuation in commodity fresh meat parts. What would stop that forward momentum in whole bird prices?

I always get concerned about the supply growing. You seem to think that the demand is going to be strong enough to offset all of it, but is 3% excess just not enough to offset that forward momentum in whole bird?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Frankly, we've model past that. Still, with our pricing structures and the balance of how we go to market, we're still in good shape if supply increases above what a 3% excess might indicate. Our buy versus grow strategy is we care a lot more about how much chicken we sell than how much chicken we grow. If you look at the last three weeks, supply, slaughter, we're over 1 billion slaughter pounds.

Since the beginning of the year, slaughter has increased something on the order of 7% and if you look at particularly front half pricing, wings, tenders, and breast meat, that's up 15%. So there's every indication that demand is more than going to offset the supply increases.

Robert Moskow - *Credit Suisse - Analyst*

Okay. Where I'll end it is on corn prices, obviously, very benign and your cost structure is getting better because of it. Let's say corn -- I'm sure you've been asked this question before -- but let's say we get another increase in corn and it goes up to \$6 instead of \$4. How much of that is contracted with your customers as a pass-through? I seem to remember it being a pretty large number now.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Yes, we call those fixed margin contracts. We have -- I won't necessarily mention the bird types, but we have, in particularly, two of our classes of business, we have extended those type of contracts fairly dramatically so that raw material cost doesn't impact our margins.

In super-high commodity price margins, like maybe we saw last summer, we give up a little bit. We know that, but we want to have stable, consistent earnings growth, which we're displaying now and using our buy versus grow strategy, our pricing models, and certainly, our innovative capability to continue to perform well for our customers, that's how we're going to continue the stable earnings growth.

Robert Moskow - *Credit Suisse - Analyst*

So that commodity benefit that you're talking about this year, that's gross, isn't it? That's not net of what you've passed back to customers, or is it net?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Yes, that's correct. That's correct. It's the change in like \$400 million, I think. We originally, when we went into the year, thought we'd have about \$450 million-plus maybe benefit and so far, it's only about \$400 million. That is in our cost of goods.

Robert Moskow - *Credit Suisse - Analyst*

So that's gross.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Frankly, some of that does leak in pricing.

Robert Moskow - *Credit Suisse - Analyst*

Can you say how much?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

No. (Laughter)

Robert Moskow - *Credit Suisse - Analyst*

Okay, all right. I'll make my own judgment. All right. Thank you.

Operator

Adam Samuelson, Goldman Sachs.

Adam Samuelson - *Goldman Sachs - Analyst*

Questions in Prepared Foods, I'm just trying to think about how, now that we have a full quarter of Hillshire under our belt, how we can evaluate the combined pro forma performance? Last year, your Prepared Food segment did \$16 million of profit. Hillshire, on a GAAP basis, did \$116 million and you talk about \$60 million of synergy capture. Is that synergy capture number a run rate or realized in the quarter?

I'm just trying to think about that, \$132 million pro forma versus the \$111 million realized and synergy is less the fire and other material inflation. Help us bridge some the performance to the pro forma.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Good question. In the Prepared Foods segment, the raw material impact was \$83 million. The synergy capture was captured in Q1. It's not a run rate. It's captured in Q1 and I think \$55 million of the \$60 million was in the Prepared Foods segment.

So think about it this way, in the front half -- I think we mentioned this at investor day that we, typically, in Hillshire locked in supply -- raw material supply -- for about six months. We've got, call it in our Q1, we've got that pretty high cost raw material in the summertime in the cost of goods. It's going to be about \$140 million or so impact in the front half of our fiscal year, but then we get relief in the back half of the fiscal year.

Another part of the improvement that we saw some in Q1, it will get more prevalent in subsequent quarters, is we closed these plants and we've taken that production and put it into other plants to increase our capacity utilization.

Demand is up. Demand's been strong. All of our brands -- I mentioned we grew sales in eight of nine categories and share in five of nine categories we look at. I feel very good about our building momentum out forward. Does that help?

Adam Samuelson - *Goldman Sachs - Analyst*

Okay. It does. Maybe as a follow-on, on the synergies, as you think about where you are today, \$60 million realized in the December quarter. What annualized run rate are you at today? Where in excess of \$225 million, what areas are driving the upside in the 2015 plan, relative to what you thought a few months ago?

Any thoughts moving forward? I know you've talked about things that are still not in the \$500-million plus number; internal raw material procurement or faster organic growth. Any thoughts on putting a finer point on those buckets at this point?



Donnie Smith - *Tyson Foods, Inc. - President and CEO*

I'll start at the back and work my way to the front. It's a bit too early. Although we have teams now that are beginning to action projects that will affect us in 2016 and 2017.

We're coming into a bit more clarity, but we've still got open projects -- we're still building projects that will affect us in 2016 and 2017. So it just a little bit too early for us to comment on that.

On 2015, the operational improvements in the legacy Prepared Foods business were a bit more than we were expecting. They came a little earlier. Frankly, we got some purchasing synergies in Q1 that we weren't expected to see a little bit -- to see until probably maybe Q2 or Q3. I feel comfortable we'll be better than the \$225 million.

It's a little too early to call because the over delivery in Q1 was really pulling forward some benefit that we had originally expected to get in Q2. I hope that helps.

Adam Samuelson - *Goldman Sachs - Analyst*

Very helpful. I'll pass it along. Thanks very much.

Operator

Ken Goldman, JPMorgan.

Ken Goldman - *JPMorgan - Analyst*

Thanks for the question. I just wanted to follow up on what Adam was asking. Because let's say you want to normalize year-on-year. Last year you had, just for Hillshire, \$1.1 billion in revenue and \$139 million in EBIT. This year, if you take out the synergies and you take out the \$83 million in costs, you're at exactly the same EBIT, \$139 million and yet, you've add a significant number of revenues.

Whether you want to look at it as Tyson adding onto Hillshire or Hillshire adding on to Tyson, I know there's D&A, I know there's some moving pieces. I just don't see how you can add that many revenues, \$1.2 billion, and not have EBIT go up a little more, even if you exclude all those costs and synergies.

You understand what I am saying? If not, I can clear it up after the call. I'm just having a hard time seeing why this margin wasn't higher.

Dennis Leatherby - *Tyson Foods, Inc. - EVP and CFO*

Ken, let me give you one point to bear in mind. Incremental depreciation and amortization year-over-year for Hillshire, because of the step-up around purchase price accounting is more than \$40 million, so part of it is in that story.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Yes, I think you're right. This is probably going to take a long time. Why don't we just take this one off-line?

Ken Goldman - *JPMorgan - Analyst*

We'll do it off-line then. I appreciate D&A's part of it.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Prepared Foods is front-loaded raw material costs that we'll recover in the back half and we'll take the margin improvement will improve sequentially quarter-over-quarter through our year and take that momentum, then, into 2016. We're very optimistic about the start, how we started, and have some possible tailwinds to make the end maybe even a little better than we're calling it today.

Ken Goldman - *JPMorgan - Analyst*

Okay. So 1Q didn't really come in that different than your expectations? Is that fair?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

No. Actually, our Q1 was slightly over plan, not by much, but it was slightly over plan.

Ken Goldman - *JPMorgan - Analyst*

Okay and then, let me shift subjects, then. Donnie, how are you thinking about export dynamics today, given where the dollar is trading? I might've expected some additional pressure on the back half of the bird by now. Are you surprised leg quarters are hanging in there? Are you modeling in some weakness going forward? I'm just curious what you guys are looking for down the road.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Two things I'm concerned about -- don't be thinking when I use the word concerned that it changes our guidance in any way. This West Coast port slowdown is now starting to back up a little bit of meat. We're starting to see some cuts like plates and that type thing go into grinding meats. We're not there yet, but we're starting to see ground beef prices drop little bit.

We're getting some fairly encouraging news, or at least we did in the front end of the week, about a possible resolution, but that is going to be a little bit of logistics upheaval probably for the next month, six weeks, two months, something like that. I don't see that, frankly, impacting our margins, because as the cutout drops, those are spread businesses, beef and pork are spread businesses and that will, frankly, move into livestock costs.

If you look at chicken, that's kind of the picture on beef and pork. If you look at chicken, we are starting to see softness in jumbo leg quarters. We've got the ban -- China has banned now because of the AI problems on the West Coast. We've had AI in Europe, Russia is not taking any US leg quarters.

So there's been a repositioning of leg quarter movement. The small and medium prices really haven't changed very much. They're still hanging around this [\$0.40-ish]-type number.

But recent trades in jumbo leg quarters for [Feb.-plus] time period are probably slightly below \$0.30 a pound. We have all of that factored into what we're talking about and we've dramatically reduced our exposure to leg quarters.

And there's some internal offsets like the fuel prices that we experienced in our live production area and feed haul and that kind of thing. Plus, we've dramatically increased our production in boneless dark meat and that's growing both at food service and retail. We continue to shift our leg quarter mix into the boneless category. I hope that's pretty good color.



Ken Goldman - *JPMorgan - Analyst*

It is. Thank you very much, gentlemen.

Operator

Tim Ramey, Pivotal Research.

Tim Ramey - *Pivotal Research Group - Analyst*

Good morning. Thanks for the opportunity. Donnie, thinking back over the last several years, I remember lots of commentary on high gas prices and weak consumer picture on QSR demand. You touched on that, but I expected a little more enthusiasm, maybe, for the outlook on QSRs.

I know I sure think that there's a lot of incremental spending that's going to shift out of gas tanks and into breakfast or various QSR revenues. What are your thoughts on that?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Seeing casual actually grow traffic for the first time since the recession is a very good sign. You're right, QSR is leading the growth. Frankly, if you take out one large QSR, QSR grew by 3.6%. There's a lot in that.

It's interesting to note, in food service, that you're seeing the younger brands outperform the more mature brands. That's an interesting dynamic that we'll be able to take advantage of.

One other thing, I mentioned off-site. We have a very strong presence in deli and retail and that business is very, very strong. We're seeing like 3.5% growth in deli. You're seeing lodging and these other off-site categories grow by 3.5%, where we have, by the way, a very strong presence.

We're very optimistic about -- we don't have that QSR promotional order today, but we're in a lot of conversations. We still think that ground beef prices are going to be relatively high and food services going to want to promote chicken this year. So we feel really good. By the way, that also plays a bit to our advantage in our buy versus grow strategy.

We'll have four incremental FP lines in production by late spring. So we're ready. Last year, we gave up some promotions because we just didn't have the capacity to do them. This year we can do them.

Tim Ramey - *Pivotal Research Group - Analyst*

Okay. Just a quick follow-up on beef. It sounds like you had adjusted slaughter rates down a little bit. Did beef catch you off guard in the first quarter? Were you a little out of position operating at too high of an operating rate? In other words, again, I would expect 2Q to be worse than Q1. I was surprised that you actually lost money in the Q1.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Yes, I wouldn't say we were out of position. I would say cattle availability, while it was in our area -- cattle continues to move to the Midwest to be fed just because of the freight rates that it takes to get the corn outside of the corn belt, so cattle continue to move towards us.

I think probably we pushed some cattle forward. The reason I say that, when I look at how quickly cattle prices responded to market signals in Q1, it told me they were in pretty strong hands.

Now when you look at this last cattle on feed report, it indicates to me that some cattle did get pushed forward which is probably going to help us in the latter part of Q2 and certainly going into the spring. The front half is always weaker than the back half. We tend to look at our cattle business not quarter to quarter, but throughout the season. It may have moved a month or two versus what we would have thought, but we are well-positioned to take advantage of it.

I mentioned our index has improved versus -- we keep an index of our performance versus the USDA numbers. We did improve. That's what I'm looking for.

Tim Ramey - Pivotal Research Group - Analyst

Thanks so much.

Operator

Farha Aslam, Stephens.

Farha Aslam - Stephens Inc. - Analyst

Hi, good morning. Two questions -- the first, Donnie, you had highlighted that tight supplies of pork and beef are supporting demand for chicken. Kind of go forward as pork becomes more available, how much pressure do you think that will put on chicken and is there any particular sector it'll have more of an impact versus less?

Donnie Smith - Tyson Foods, Inc. - President and CEO

It stands to reason it'll put some. Typically, if you look at the per capita consumption data, per capita consumption of pork is relatively flat and we export about 25% of the pork that we produce. There's a little bit of concern on the West Coast now, but in general, global demand for protein, for pork particularly, continues to grow. So, we'll export more. Like I said, the prices have dropped to offset the increase in the value of the dollar.

It's not so much a pork versus chicken story as it is a beef versus chicken story. Beef prices are going to remain relatively high. Plus don't forget, as pork prices drop, in our portfolio, we get a offsetting benefit or an additional benefit in Prepared Foods that might offset any softness in chicken prices, for example, that type thing.

Farha Aslam - Stephens Inc. - Analyst

That's helpful. Going on to Prepared Foods, you've said that this year you expect \$225 million or so in synergies and over three years, \$500 million. Could you just help bridge the \$225 million to the \$500 million? Kind of key buckets that you're looking for in terms of where those cost savings are going to come from?

Donnie Smith - Tyson Foods, Inc. - President and CEO

There's four buckets. Operational improvements in Prepared Foods, that largely comes in FY15. Procurement, frankly, we would get some benefit in 2015, but more benefit as we get out into 2016 and 2017. Then we'll also begin to pick up additional synergies in manufacturing and logistics as we get the network built out and that type thing. For this year, I think we said this in New York, that we're looking for about \$140 million in the operational improvement bucket in 2015; \$40 million in procurement, \$25 million in the plants and in logistics, and then \$20 million from G&A savings, if you will.



If you move forward, you get more and more savings in procurement, you get more savings in manufacturing and logistics and network optimization and then into 2016 and 2017, those buckets begin taking the majority of the synergy versus the initial legacy Prepared Foods changes in 2015. Does that help?

Farha Aslam - *Stephens Inc. - Analyst*

That's very helpful. Thank you.

Operator

Brett Hundley, BB&T.

Brett Hundley - *BB&T Capital Markets - Analyst*

I had a question, Donnie, on Prepared Foods. I just wanted to understand more of the competitive dynamic within packaged meat right now, what you are seeing and hearing? Really what I'm getting at here is as some of these raws come off, I want to try and understand Tyson's ability to drive margin alongside its innovation schedule, if that makes sense. Just wanted to see what you're hearing and seeing on the competitive dynamic front within packaged meat.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Sure. So, you're right. We will be able to continue to drive our profitability. The real reason behind that is we're continuing to support the innovation that we have in the marketplace today. We're building for more innovation in the back half of our year and extending into some other categories. So that's going to continue to help.

I believe what we have seen as we have entered the year, we're exactly on plan with where we thought we would be. By the way, we're going to adjust the marketing support a little bit for our anytime launch. Velocity is not exactly where we want it to be there. Distribution's great, but we need to tune up velocity there which will happen in the back half of the year. We're in, I think, great shape in our categories and the categories are very strong.

If you add our positioning, how we will adjust map spending throughout the year to keep a good balance between volume and profit and then we're positioning ourselves, because we have a pretty good feel for what the raw material will do. We're positioning ourselves to maintain that margin growth and accelerate through this quarter and then accelerate it in the back half of the year.

Brett Hundley - *BB&T Capital Markets - Analyst*

Good point about the categories being in such good shape that they are.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

We have advantaged brands in advantaged categories and that is very good for the long-term potential of both our Prepared Foods and our Chicken business.



Brett Hundley - *BB&T Capital Markets - Analyst*

Okay. You just offered me a segue back to chicken, rather. It's nice to hear you guys acknowledge some of the bigger numbers that we're seeing here recently and your confidence in being able to not only perform but take your expectations higher. You talk about the strong demand. I've seen you quoted in an article where you said that higher beef prices were maybe driving a 3% improvement in chicken demand.

We understand there's a very large QSR out there buying chicken for an H1 promo. I suppose that this demand step up can help eat its way through these extra supplies that we're seeing, but you're going to continue to see that supply growth with where we see smooth pullet data. That portends a 3% or higher headcount. You have weights that have been running higher.

As we get past summer, when maybe some of this demand comes off a little bit, we worry a little bit about that supply demand pricing dynamic. So I'd love for you to just address as we move 2015 into 2016 here, what protects you, again, better than the rest? I know you've said some things regarding that.

But also more so, I don't want to put you on the spot with 2016, but your confidence alongside chicken with the rest of your business in this Company being able to drive earnings growth in years ahead? Not just 2015, but beyond. I appreciate it.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Let's talk about four components. I don't disagree that recent data or I agree with you, recent data would indicate that supply will be higher in the year. Remember, we don't really care how much we grow. We care how much we sell.

And so we will manage our production based on our forecasted demand. We balance to the nearest whole bird increment in whatever size that is and then our buy versus grow strategy puts us in a position to buy raw materials that are out of balance, which doesn't leave us stranded with parts who may be in excess, that type thing.

That's kind of the general framework, but on top of that, think about this. Explosive growth in tray pack. We're a tremendous tray pack supplier. We're adding capacity and we are going to be unencumbered in our growth in tray pack.

Tray pack, fresh tray pack at retail is really benefiting from high retail beef prices. That, plus we're increasing our further processing capability to be able to take advantage of growth both in retail, frozen, fully cooked, as we take this great innovation engine and grow that category with new news, plus at food services, the food service operators want to grow there.

We have a very balanced and broad portfolio. We have a good balance between the bird sizes in tray pack and small bird and all those things. Plus, you take our pricing structures, which we have a blend and some are based on the market, some are based on raw materials. But what we've done is established a way to protect our margins and grow our customers' business using our great service and our great innovative capability, which is very valuable to them and they, frankly, don't get anything like it from anyone else.

Add on top of that, we've continued to spend pretty strong against our chicken business and we continue to be more and more efficient. One quick case in point, when we solved our production issue in our fully cooked business, we actually added an incremental million pounds a week of capacity to one of those locations and created an even more efficient operation. That will pay off in the future.

If you take a blend of the consumer benefits that we can take advantage of with our portfolio and then the customer who depends on us for innovation, quality, service, and those components, and the balance of our portfolio, on top of our buy versus grow strategy, it's a winning combination and it stabilizes our earnings. That's why -- we took 2015 up and we feel very strong about 2016 because the same dynamics will be in play.

Brett Hundley - *BB&T Capital Markets - Analyst*

All right. Thanks, Donnie.

Operator

Tim Tiberio, Miller Tabak.

Tim Tiberio - *Miller Tabak - Analyst*

Good morning and thanks for taking my question. My first question is around your buy versus grow strategy. Now that supply growth seems to be a little bit ahead of your initial expectations, can you give us an update of what percentage you're buying in the second quarter and how much you see that growing year-over-year in FY15?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

I'll give you a general answer. I don't want to be very specific. The amount we buy will be balanced against the amount of our other pricing that has market exposure. So we're very balanced there. It kind of gives us an internal hedge. Plus, there are some parts of our business where, tray pack or small bird, we have to grow the bird. In other parts of the business, we don't.

The way we're set up, we think we have a very good demand picture and we see demand very strong out in front and we have built our supply chain to be able to buy raw material to fill that demand. We'll buy it, put it in our further processing plants and fill the demand.

Tim Tiberio - *Miller Tabak - Analyst*

Great. My second question, I may have missed this earlier, have you set a target for full-year debt reduction in 2015? It seems like that's a key component of potentially driving accretive earnings power from 2015 into 2016.

Dennis Leatherby - *Tyson Foods, Inc. - EVP and CFO*

Sure, Tim. We're expecting at least \$1.2 billion, maybe a little bit more.

Tim Tiberio - *Miller Tabak - Analyst*

Perfect. Thanks for your time.

Operator

Diane Geissler, CLSA.

Diane Geissler - *CLSA Limited - Analyst*

Congratulations on your quarter. I just wanted to ask about -- I think it's pretty widely observed that 2015 is going to be a good year, but I'm sort of getting the sense from clients that I talk to that it all falls apart in 2016.

I just want to get to this point about the QSI and this idea that chicken purchases are durable goods. To me, I look at it and say, if gas prices are down and stay low, maybe they move a little bit higher, but I don't think anybody's predicting that they go back to where they were 12 months ago.

Wage rates, we know, are up this year and most of the states that raised their minimum wages are raising them again next year. We know we don't have any supply on the beef side coming for at least two to three years. So I look at 2016 and just say, is there anything you're hearing from QSR, any of your major channels that would suggest to you that demand is just going to -- it's just pent-up demand for chicken over the summer and then it just evaporates? Because I really can't believe that.

My follow-up, which I'll ask just now is, based on that answer, I look at your changes to your outlook in your major segments and all of them are positive like lower interest expense, better margins in chicken, et cetera, et cetera. So, I look at the guidance range of \$3.30 to \$3.40 and there's been no movement there, yet, you have guided to mostly positive changes in the outlook on a segment basis. Is there any reason why you're not taking your earnings range up today? The two questions are sort of linked. Thanks.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

I agree with you. I'm not hearing anything that would indicate to me that there is a cliff in demand; frankly, quite the opposite. Here's how I think about -- let's say, 2016. It's early, to your point, on guidance. It's early in our year.

You're right. The outlook is positive when you balance all the factors, but it's just early for us. Here's how I think about it. Number one, we've got advantaged brands in advantaged categories. We've got leading brands with leading share in categories that are very meaningful to consumers.

We will continue to see growth, not just based on categories, but also, and more importantly, based on our brand building capabilities and our innovation pipeline. In 2016, obviously, we'll have an accelerated -- an incremental year in capturing the synergies. As I mentioned earlier, we're setting our supply up to be able to take advantage of whatever industry supply we see to meet that demand.

I believe we'll continue, because of the shortness in the cattle supply, we'll continue to see red meat pricing high and that'll provide an umbrella for the alternative proteins. Because the relative value of chicken to beef, I think, remains largely unchanged over the next couple three years. We're going to have new tray pack capacity, we'll have new fully cooked capacity and that will be in our results.

I think cattle, frankly, and hogs are moving closer to us so that advantages us there. As you mentioned, we're going to be generating a lot of cash and we'll continue to improve the balance sheet and create optionality for us. We've got a strong CapEx agenda to continue to grow the business and add to our profitability. If you just look at the lower interest costs in the future and the stock price goes up, the changeable [actuary] units will help bps. Again, there's just a lot of reasons to be optimistic about our 2015 guidance. It's just early.

Diane Geissler - *CLSA Limited - Analyst*

Okay. Great. Thank you.

Operator

Michael Piken, Cleveland Research Company.

Michael Piken - *Cleveland Research Company - Analyst*

Just wanted to circle back and take sort of a multiple year view and maybe you could talk a little bit, specifically, first on beef, when you think we might be able to get back to normalized margins or if cattle supplies are going to remain tight through 2016 and may be in the beginning of 2017, when we might be expected to return to normalized margins?

The second follow-up question would be on the Prepared Foods. It definitely sounds like there's a headwind from the raw material costs that will continue into 2Q. What is the pathway to 10% to 12% margins and should we expect straight line growth from this point forward? Thanks.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

In terms of beef, the supply will probably be flat to down 1% again in next year and I think it may take four or five years to rebuild the herd back to the 2013 level. I think, over time, the margins in our beef business will improve.

In Prepared Foods, you're right, we've got some front-end headwinds on raw materials. We've talked about that. It will dramatically improve in the back half and we'll continue to grow our margin potential, one, as we gain the synergies in the out years, plus we continue to grow the brands.

Operator

Ken Zaslow, Bank of Montreal.

Ken Zaslow - *Bank of Montreal - Analyst*

Let me just go back to this hog issue, it seems like, again, the supply of hogs is far greater than anybody expected. It seems like we might actually be swimming in hogs in the next year or two. When you were thinking about your forecast on the 10% to 12% longer-term, as well as the nearer term, how much of this recent movement in the hog supply, as well as the lower pork costs were incorporated into your expectations? Both on the pork packer side on, as well as the input costs for the Hillshire.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Frankly, none, Ken. As you look out front, what we did is we took, let's say, five-year average pork prices and then layered in the synergy capture and then what we felt like we could do by organic growth in those categories, that's how we came to the 10% to 12% number. Any benefit that, frankly, our Pork segment and our Prepared Foods segment would see from an increased hog supply has not been factored in.

Ken Zaslow - *Bank of Montreal - Analyst*

Let me just make sure I understand this. You took up your chicken margins to 11%. You hit more synergies than the \$225 million because you're on a run rate of \$240 million. You're seeing more hog supply. You started buying back stock and you lowered your interest expense and yet, you think the expectations are still \$3.30 to \$3.40?

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

I think it's early, but I like your story.

Ken Zaslow - *Bank of Montreal - Analyst*

I'm just making sure I wasn't confused.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

You've got it. You absolutely have it.

Ken Zaslow - *Bank of Montreal - Analyst*

My last question is cash flow, just to make sure I understand this. You actually started buying stock, although it's only to offset compensation, earlier than I think you expected, so I think your cash flow is better than you expected. What is that attributable to?

Dennis Leatherby - *Tyson Foods, Inc. - EVP and CFO*

Seasonally, in the first quarter, we typically have our cattle and hog producers. They don't want to be paid in December for cash tax reasons. Typically, that deferral that carries over at the end of December is in the neighborhood of \$200 million to \$250 million. This year it was more than \$400 million. There was a little bit of extra cash that we were able to redeploy in the quarter.

Ken Zaslow - *Bank of Montreal - Analyst*

Maybe you guys will stop buying back stock today. Thanks a lot.

Donnie Smith - *Tyson Foods, Inc. - President and CEO*

Thanks, Ken. Thanks, everyone. We're off to a great start towards another record-setting year for our Company and we'll continue to accelerate our growth as an insights-driven consumer centric branded food company. As always, we appreciate your interest in our Company. I hope you have a great weekend.

Operator

That does conclude today's conference. Thank you for participating. You may disconnect at this time.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2015, Thomson Reuters. All Rights Reserved.