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Hormel Foods Corp. (HRL)

Q2 2015 Earnings Call

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Chairman, President & Chief Executive Officer

Jody H. Feragen
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Goldman Sachs & Co.

Farha Aslam
Stephens, Inc.

Diane R. Geissler
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Eric J. Larson
Janney Montgomery Scott LLC

Mario Contreras
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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the Hormel Foods Second Quarter 2015 Earnings Conference Call. All participants are in a listen-only mode. Today's conference is being recorded.

At this time, I'd like to turn the conference over to Jana Haynes, Director of Investor Relations. Please go ahead.

Jana L. Haynes
Director-Investor Relations

Thank you. Good morning. Welcome to the Hormel Foods conference call for the second quarter of fiscal 2015. We released our results this morning before the market opened around 6:30 AM Eastern Time. If you did not receive a copy of the release, you can find it on our website at hormelfoods.com under the Investors section.

On our call today is Jeff Ettinger, Chairman of the board, President and Chief Executive Officer; and Jody Feragen, Executive Vice President and Chief Financial Officer. Jeff will provide a review of the operating results for the quarter; then Jody will share detailed financial results for the quarter; the line will be opened for questions following Jody's remarks.

As a courtesy to the other analysts, please limit yourself to one question with one follow-up. If you have additional queries, you are welcome to get back in the queue. An audio replay of this call will be available beginning at 10:00 AM, Central Time today, May 20, 2015. The dial-in number is 888-203-1112 and the access code is 3883596. The audio replay will also be posted to our website and archived for one year.

Before we get started with the results of the quarter, I need to reference the Safe Harbor statement. Some of the comments made today will be forward-looking and are made under the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those expressed in or implied by the statements we will be making. Among the factors that may affect the operating results of the company are fluctuations in the cost and availability of raw materials and outbreaks of disease among livestock and poultry flocks. Please refer to pages 29 through 36 in the company's Form 10-Q for the quarter ended January 25, 2015 for more details. It can be accessed on our website.

Now, I'll turn the call over to Jeff.

Jeffrey M. Ettinger

Chairman, President & Chief Executive Officer

Good morning, everyone. We announced record second quarter earnings this morning of $0.67 per share, up 29% over last year. Segment operating profit increased by 29% with all 5 segments registering gains this quarter. We also generated record sales of $2.3 billion, an increase of 2% over last year on a 5% volume increase.

In terms of segment performance, Refrigerated Foods grew segment profit 52%, driven by strong performance by our value-added businesses and lower pork input costs. Segment sales were down 8% this quarter despite a 1% volume increase. Lower sales were primarily due to pricing decreases on items such as bacon, driven by declining pork market values. Additionally, the dissolution of our Precept Foods joint venture announced at the beginning of the year impacts Refrigerated Foods segment sales by approximately 2.5% each quarter in fiscal 2015.

We enjoyed strong sales of many of our value-added items during the quarter, including retail sales of HORMEL pepperoni, HORMEL GATHERINGSTM party trays and Lloyd's Ribs. Foodservice sales of HORMEL BACON 1 fully cooked bacon, OLD SMOKEHOUSE bacon, and HORMEL pizza toppings also delivered solid growth.

We launched a new AUSTIN BLUES competition-style barbecue meats line in the Foodservice channel this quarter as we continue to drive innovation in the category.

Grocery Products segment profit increased 1% on a 1% increase in sales. Segment results were aided by lower pork input costs along with strong sales growth from SPAM luncheon meat and WHOLLY GUACAMOLE dips. Sales volumes of SKIPPY peanut butter grew this quarter, benefiting from our new advertising campaign, however, dollar sales decreased as a result of the category price decline earlier this year pressuring segment margins. Sales of HORMEL COMPLEATS microwave meals were lower this quarter.

Grocery Products continues to drive sales by leveraging our iconic brands in new and innovative ways. We recently kicked off the coast-to-coast SPAMERICAN Tour with our food truck travelling to popular events across the country this summer, featuring SPAM creations by Food Network Chef, Sunny Anderson.

Our Specialty Foods segment reported an operating profit increase of 11% and a sales increase of 32%, largely led by the recently acquired CytoSport business. During the second quarter, we announced that we will be closing the Benicia, California CytoSport manufacturing facility in June and moving portions of the production to our Century Foods operation in Wisconsin and to a third party facility near Benicia. The planned closure of the facility negatively impacted second quarter segment results by $4.5 million. The team continues to achieve additional distribution of our MUSCLE MILK protein-rich products, delivering gains in the club, food, drug and mass and convenience channels this quarter.

International and other segment profit increased 2%, while sales fell 7%. Improved joint venture results were mostly offset by lower exports, a result of port issues and a strong U.S. dollar during the quarter. We did experience higher sales of SPAM luncheon meat gift packs, which are popular gifts in South Korea during celebration of the Lunar New Year. Meat sales in our China operations were also up, primarily driven by growth in the Foodservice business.

Jennie-O Turkey Store increased segment profit 41% and grew sales 15%. Results were driven by robust sales of value-added products and lower grain and fuel costs as compared to last year. Sales growth was led by Jennie-O lean ground turkey and Jennie-O rotisserie turkey.

The Midwest began experiencing significant outbreaks of highly pathogenic avian influenza in late March. To date, approximately 55 farms have been impacted that were to supply Jennie-O Turkey Store with turkeys. While we experienced modest financial impact from the outbreak in the second quarter, Jennie-O Turkey Store is estimating a loss of approximately 15% of second half sales. This sizeable estimated loss of volume is not only due to bird losses over the past month, but also takes into account the fact that many of our barns remain empty under quarantine. Due to lack of internal turkey supply, we will be purchasing some additional meat from external sources but at a higher cost. We are also planning for lower sales as we are forced to rationalize some business.

As a result of the turkey supply shortages, on May 5, we regrettably announced a temporary layoff of our second shift employees at our Faribault, Minnesota facility. We look forward to welcoming our team members back when bird numbers and production levels return to normal.

Our team is working closely with government agencies and other organizations as they study this virus and work to control the spread. As always, employee safety and food safety are top priorities in our organization, and we remain focused on safety even as we work through these unprecedented challenges. Looking ahead to the second half, operating margins of Jennie-O Turkey Store will be significantly challenged due to the impacts of avian influenza on our turkey supply chain, reducing expected segment operating margins in the back half to the 10% to 12% range.

Refrigerated Foods should continue to benefit from strong value-added sales and lower input costs, although segment earnings growth is expected to be less robust in light of difficult comparisons to last year's third quarter. We look for Grocery Products to deliver strong segment profit growth in the back half, benefiting from lower input costs, and softer prior year comparisons.

Specialty Foods is positioned for strong performance in the second half as the team has realized synergies, achieved distribution gains and ignited innovation in the recently acquired Muscle Milk business. We expect our International segment to deliver growth in the second half as well with improved export sales and solid results from our China business.

Based on our assessment of the impact of avian influenza on Jennie-O Turkey Store to date, and given that Refrigerated Foods and Jennie-O Turkey Store segments delivered excellent results in the first half, we are maintaining our fiscal 2015 adjusted guidance range of $2.50 to $2.60 per share, but expect full year earnings to be near the lower end of this range.

Our balanced business model provides Hormel Foods the ability to navigate challenges, such as this year's unprecedented turkey supply shortage and continue to deliver consistent growth over the long term.

At this time, I will turn the call over to Jody Feragen to discuss the financial information relating to the second quarter.

Jody H. Feragen
Chief Financial Officer, Director & Executive VP

Thank you, Jeff. Good morning, everyone. Earnings for the second quarter of fiscal 2015 totaled $180.2 million, or $0.67 per share, compared to $140.1 million, or $0.52 per share a year ago. Dollar sales for the second quarter totaled $2.28 billion, compared to $2.24 billion last year, a 2% increase. Sales excluding the incremental impact of CytoSport and MegaMex products were down 3%. Lower pork prices, the dissolution of the Precept Foods joint venture, lower exports and the price reduction on SKIPPY peanut butter products were the primary drivers.

Volume for the second quarter was 1.29 billion pounds, increasing 5% from the same period last year. Tonnage was up 1% excluding the incremental impact of CytoSport and MegaMex products. Selling, general and administrative expenses in the second quarter were 8.3% of sales, up from 7.4% last year. Selling, general and administrative expenses were higher this year due to employee-related expenses along with higher advertising expense. For the full year, we expect selling, general and administrative expenses to be between 7.5% and 7.8% of sales.

Advertising expense for the quarter was $39.5 million, compared to $34.8 million last year. The increase was due mostly to advertising expense at CytoSport for the MUSCLE MILK brand, which was acquired last August. Equity and earnings of affiliates was $7.9 million in the second quarter versus $3.6 million last year. The increase is largely the result of prior year incentive expenses related to the Fresherized Foods acquisition not repeated this year, and also savings associated with the exit of the international joint ventures last quarter.

Interest expense for the quarter was $3.1 million, unchanged from last year. Our effective tax rate in the second quarter was 34.6% versus 34% in fiscal 2014. For fiscal 2015 full year, we expect the effective tax rate to be between 34% and 35%. The basic weighted average number of shares outstanding for the second quarter was 264 million. The diluted weighted average number of shares outstanding for the second quarter was 270.4 million.

Depreciation and amortization for the quarter was $33 million versus $31.9 million last year. We expect depreciation and amortization to be approximately $125 million in fiscal 2015. Total long term debt at the end of the quarter was $250 million, unchanged from last year. Capital expenditures for the quarter totaled $27.3 million, down $12.7 million compared to last year. For fiscal 2015, we expect capital expenditures to be approximately $165 million to $180 million.

At this time, I will turn the call over to Hanna for the question-and-answer portion of the call. Hanna?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And we'll take our first question from Adam Samuelson with Goldman Sachs.

Adam Samuelson
Goldman Sachs & Co.

Q

Hi. Thanks. Good morning, everyone.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

Good morning, Adam

Adam Samuelson
Goldman Sachs & Co.

Q

So, I guess the first question in Jennie-O, I want to understand – it seems like, Jeff, the details you gave about a $0.09 to $0.12 or so EPS impact in the second half from AI guidance and the full-year range maintained despite moving towards the low end. First, help us bridge what got better in the rest of the business as you think about the outlook that has allowed you to maintain the EPS range.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

Well, the first half has been a very strong half for us. Q1, as you recall we were able to raise the guidance range at the conclusion of Q1. Q2 was also a very strong quarter for us. And honestly, but the for the avian influenza incident, we would be talking to you today about raising the guidance range. So, clearly that provided some momentum. I also have the expectation that the other four business segments will generate positive results year-over-year during the second quarter and we'll then be able to offset much of what's going on at Jennie-O for the half.

Adam Samuelson
Goldman Sachs & Co.

Q

Okay, that's great. And maybe at Jennie-O specifically, I want to – the guidance – is it – I mean does it reflect kind of the status quo today? I know no more – no further cases of AI in Minnesota or in your facilities or does it give you some cushion for some further outbreaks? And how do you think about the impact into 2016 at this point as you still have to get the barns repopulated and potential volume impact as it slips into next year?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

We did attempt to bake in at least some sense of, okay, if there's some added percolation going on, there where there might be another outbreak or two and indeed, if you look at it over the last two weeks, we had one fairly significant barn complex encountered the disease. So, we have tried to factor in that somewhat, but also are expecting that the thing should slow down during the summer. The fall is a wildcard in terms of if and when it comes back.

In terms of next year, and we really are not in a position to give you any quantifiable new range for Jennie-O or for the whole company for that matter. We're just beginning our planning process. But I do believe it would be fair to say that at this point, the outlook for the first half of the year for Jennie-O Turkey Store should be somewhat subdued based on the issues that you've raised. I mean, it is going to take them some time to get back into full production. I just – I can't tell you whether that 10% to 12% range though that we gave you for the second half is the right range for the first half yet, but it probably will be something short of what we experienced this year.

Adam Samuelson
Goldman Sachs & Co.

Q

Okay. And maybe just quickly on that point. The repopulation of the barns, can you walk us through the timeline there? Just help us think through how long it will take to get your volume back to where it was in March?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

I can't really give you any precision with that because we're in somewhat new territory. We're working with the government on that. It's going to depend in part upon the continuation of no outbreaks for a timeframe. We do understand that there's recently in Wisconsin the repopulation of a chicken-based facility, so it wasn't one of ours, but – so the process is at least beginning. But I really can't give that to you with great precision, I mean other than to tell you, obviously once we do get the poults in barn, I mean it's 22 weeks after that before we would be bringing them to the manufacturing facility for our tom based turkeys.

Adam Samuelson
Goldman Sachs & Co.

Q

All right. Great. Thanks very much. I'll pass it on.

Operator: Our next question comes from Farha Aslam with Stephens.

Farha Aslam
Stephens, Inc.

Q

Hi. Good morning.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

Hi, Farha.

Farha Aslam
Stephens, Inc.

Q

Could we talk about your Refrigerated Foods business? The results there were exceptional. How sustainable are the results in the second quarter? How long do you think the hog commodity tailwind is going to benefit you? And how are you thinking of product innovation in that segment?

Jody H. Feragen
Chief Financial Officer, Director & Executive VP

A

Wow, you loaded a lot of questions into one there, Farha.

Farha Aslam
Stephens, Inc.
Q

That's all one, yeah.

Jody H. Feragen
Chief Financial Officer, Director & Executive VP
A

She is counting it as one. The hogs, we expect supply to be up 5% to 6% for the year, so I would assume, particularly given the extremely high comps that we had last year due to the disease issues in the industry, that we'll see some reasonable hog prices, so that's a good thing. Domestic demand seems to be pretty robust at this point in time. We do see that exports have fallen a bit so we'll keep an eye on that.

But it's really our value-added businesses that are driving the results for Refrigerated Foods. They didn't have a big benefit from any pork operating margins this quarter. It really was the value-added side of the portfolio that was delivering for them. They came in above our guided range, but we'll continue to monitor given the amount of volatility that can occur in that segment. So, I'm not willing to call that this is the new norm going forward.

And innovation?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer
A

I just would mention – I mean we received notice here recently that both the REV product and our WHOLLY GUACAMOLE minis were named IRI Pacesetter Top 100 New Items from kind of the last 12 to 18 months of introduction. Our Foodservice group has really enjoyed some excellent results with their BACON 1 product and also their Fire Braised meats, so innovation still is a key component to what we're seeing for success for Refrigerated Foods and our other segments.

Farha Aslam
Stephens, Inc.
Q

Great. And then in terms of CytoSport, that acquisition was expected to be roughly $0.05 accretive to EPS this year. Is it on track, is it ahead or behind pace?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer
A

Well, I mean, the first quarter was probably slightly behind. The second quarter, if you look at operating results, we were very happy with the results. They did have the additional $4 million plus charge as we made the decision to close the Benicia plant. Over time, that should enhance operating returns and heading into next year then hopefully, we'll be able to increase on that. But we're still comfortable with that number.

Farha Aslam
Stephens, Inc.
Q

So still around that $0.05 number?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer
A

For this year.

Farha Aslam
Stephens, Inc.
Q

Perfect. Thank you so much.

Operator: Our next question comes from Diane Geissler with CLSA.

Diane R. Geissler
CLSA Americas LLC
Q

Good morning.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer
A

Hi, Diane.

Diane R. Geissler
CLSA Americas LLC
Q

I wanted to ask on the Turkey business, so could you give us an idea about given where things stand today, and obviously can't know about future outbreaks if that happens, but what you expect industry production volumes to be this year down kind of year-on-year for the full year?

And then I was also curious to know, do you expect sort of ramped up CapEx to maybe, I don't know, fortify your positions around the barns or whatever to protect from potential future outbreaks? I know we don't get high path AI very often, I think the last outbreak was over 10 years ago. But I guess I'm just curious – it seems to have decimated turkeys and I guess table egg layers. And so, I guess the question is should the industry be spending more to defend against potential future outbreaks and would that include you as well?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer
A

Okay. Both good questions. On the expected turkey volumes. I mean, I can tell you the USDA has not modified their number from the 3% to 4% increase that they expected for the industry. I mean, given our experience and given that we're sort of tied for one of the lead players in terms of volume in the industry, I guess I have a hard time seeing how those numbers happen if we're going to be short 20% in terms of at least turkeys coming into our system and about 15% net of the meat we're going to have to buy. So, I don't have an adjusted total industry number for you, but I guess I'm skeptical as to the industry's ability to hit that 3% to 4% gain number.

In terms of ramped up CapEx, I think the theory that you've laid out is probably correct. We're still a little too early to know exactly what might be required. But in talking with APHIS and just kind of studying, okay, what are better ways to potentially prevent this in the future. And also given the fact that there seems to have been airborne introduction this time, and so that may cause some added fan and ventilation requirements that will be different than what we've done in the past. I think it probably would be safe to assume some additional level of CapEx spending, but I don't have any ability to tell you whether – what the delta is versus normal either for Jennie-O or for the total company heading into next year.

Diane R. Geissler
CLSA Americas LLC
Q

Is the AI outbreak covered under any insurance plan you might have, business interruption or any other – or is it seen as sort of an act of God and is non-insurable?

Jody H. Feragen
Chief Financial Officer, Director & Executive VP

A

It's a non-insurable event, although as it has been in the press, the government helps farmers with birds that they have to euthanize.

Diane R. Geissler
CLSA Americas LLC

Q

Okay. All right. Thank you.

Operator: [Operator Instructions] And we'll take our next question from Eric Larson with Janney Capital Markets.

Eric J. Larson
Janney Montgomery Scott LLC

Q

Yes. Thanks for taking the question, and good morning, everyone.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

Hi, Eric.

Jody H. Feragen
Chief Financial Officer, Director & Executive VP

A

Good morning.

Eric J. Larson
Janney Montgomery Scott LLC

Q

Jeff, just kind of a strategic question with Jennie-O. I mean, obviously your production is highly concentrated and it is highly efficient obviously with your manufacturing facilities in the upper Midwest, Minnesota. Is there any thought that maybe you should geographically diversify some of your production over time? I mean maybe via an acquisition somewhere that gives you – maybe try to get off the Mississippi flyway or some other thing. I mean, does this prompt some different thoughts strategically how you might run the business?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

Well, I guess I would concede that this is – given this unprecedented and rare incident that's kind of exposed a little bit an Achilles' heel to the strategy of being very centralized. It had been a tremendous advantage in the past in terms of just knowledge of feed within an area and growing practices, the ability to move meat from plant to optimize products and so forth.

And indeed, all of our facilities are either in Minnesota or Wisconsin. So, whether this is something that then prompts a change in that, we're still on the triage mode right now and I guess that's something on a strategic long-term basis I'll be talking with the team about. But it's a valid question.

Eric J. Larson
Janney Montgomery Scott LLC

Q

Okay, thanks. And then just back to the Refrigerated division again, it's very impressive to see the fact that your hog prices are so low, but you're able to hold your pricing at retail with your value-added products. Can you give us a rough idea of what percent of your Refrigerated volume today would be, quote, value added? And I don't know how you want to define that necessarily, whether it's your all marinated products and flavored products. And is there a way that we can think about that, that helps us – because it looks like it's a longer-term positive margin shift for you that's become more apparent in the last 12 months.

Jody H. Feragen
Chief Financial Officer, Director & Executive VP

A

So, I think we've discussed before that about 70% of our Refrigerated Foods portfolio would be considered value-added. But understand included in that 70% would even be things that have pricing that's more market-driven such as bacon and hams and our marinated fresh meat. And even on the Foodservice side, some of the contracts they have for items are driven by market forces. So, yeah, the team has performed well, they have a focus on providing great value for our customers, but also making sure that there's a margin left for us.

Eric J. Larson
Janney Montgomery Scott LLC

Q

Okay. Thanks. I'll pass it on.

Operator: Next, we'll go to Mario Contreras with Deutsche Bank.

Mario Contreras
Deutsche Bank Securities, Inc.

Q

Hi. Good morning.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

Good morning, Mario.

Mario Contreras
Deutsche Bank Securities, Inc.

Q

In terms of M&A, how is the company's acquisition pipeline relative to recent quarters? And then secondly, does the increased company resources focused on avian flu limit the company's interest in pursuing M&A, at least in the near-term?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

I guess from a pipeline standpoint, I mean, we're – I don't have anything different to report than normal. I mean, we certainly have a track record of generating growth through M&A along with our product innovations and doing a better job with our traditional items. And we continue to look for both family-owned businesses and institutional properties that might come out, but I don't have anything to report specifically on that.

In terms of AI, clearly it is a time-consuming challenge, particularly for the Jennie-O Turkey Store team, but it's not having any impact in terms of our overall team's ability to seek out M&A opportunities, nor would it have any issues in regard to our ability to finance such a transaction.

Mario Contreras
Deutsche Bank Securities, Inc.

Q

Okay, thanks. And then, just as a follow-up, I guess maybe stepping back a little bit, there's been a pretty significant or increasing industry focus on ZBB and overhead reductions. So, how do you feel about Hormel's overall overhead spending? And do you anticipate any changes to the company's strategy regarding that?

Jody H. Feragen
Chief Financial Officer, Director & Executive VP

A

Well, I do not plan to announce any special cost reduction initiative. I think that's kind of the culture that we live by day-by-day. We always run a pretty lean operation with a lot of processes in place such as Jeff signing off on any salaried employee that's being added to the payroll. So, everything gets a pretty difficult look. We do – I would argue that we already have been doing zero-based budgeting for many years, but we just didn't call it that. So, I'm pleased with the initiatives we have underway with the constant look at expenses and keeping things in line.

Mario Contreras
Deutsche Bank Securities, Inc.

Q

Okay. Thank you very much.

Operator: We'll go next to Akshay Jagdale with KeyBanc Capital Markets.

Lubi J. Kutua
KeyBanc Capital Markets, Inc.

Q

Hey, good morning. This is actually Lubi on for Akshay. Just with regards to your Jennie-O outlook for the second half, can you just talk a little bit about how we should be thinking about the cadence between third quarter and fourth quarter? I mean, will it be fairly evenly distributed, or do you think things sort of get progressively worse before stabilizing again?

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

I mean, they're both significantly challenged and to a pretty close level, is our best shot at it right now. And we're short the birds already in terms of what's been going on over the last several weeks, so we're in it.

Lubi J. Kutua
KeyBanc Capital Markets, Inc.

Q

Okay, thank you. And then, could you provide us maybe an update on how SKIPPY performed during the quarter domestically and internationally, and also REV Wraps? Thank you.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

A

Okay. SKIPPY on a domestic basis, we were pleased that we returned to volume growth and expect that to continue going forward. We did see with the price decline, our net sale number was down. And as I mentioned in the introductory comments, that did squeeze our operating margins a little bit on SKIPPY. We're happy, thus far, with the performance of the ad campaign. We've been able to see demonstrable results in advertised markets that were enhanced over the non-advertised markets. And we also continue to look for new product innovation, and we'll have some things to show the marketplace later this year in that regard in terms of the SKIPPY brand.

Outside of the United States, so far, our experience in China has been – it's kind of an up and down quarter-to-quarter business. The second quarter wasn't particularly strong this last quarter, but in visiting with the team, they're very comfortable that they will see overall growth in terms of the SKIPPY international portfolio for the second half of the year as they have programs in place to generate that.

In terms of REV, we're kind of making a little bit of a transition with that product. We, upon advice of some of our trade customers, we've changed the case, we've changed the product packaging somewhat. We're trying to attain a price point that we think is going to be able to stimulate the next wave of growth for that item. And so, second quarter kind of was the transition quarter for that. The new products are now in the marketplace and then we're complementing that with a new ad campaign that just launched at the very end of April. And early reads on that are positive, but we'll be able to give you that full report when Q3 is done.

Lubi J. Kutua
KeyBanc Capital Markets, Inc.
Q

Thank you. I'll pass it on.

Operator: Next, we'll go to Rachel Nabatian with Credit Suisse.

Rachel N. Nabatian
Credit Suisse Securities (USA) LLC (Broker)
Q

Hey. Good morning.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer
A

Good morning.

Rachel N. Nabatian
Credit Suisse Securities (USA) LLC (Broker)
Q

So I wanted to ask about the normalized margin range for Refrigerated Foods. With demand for protein being quite strong and pork input costs going longer due to the rising supplies, isn't this pretty much an ideal scenario for the Refrigerated Foods division and maybe even Grocery? And do you think that we can assume that margins can stay at the high end of this normalized range for quite some time?

Jody H. Feragen
Chief Financial Officer, Director & Executive VP
A

I think I addressed it earlier, but never hurts to reemphasize. We're certainly pleased with how the value-added portfolio within Refrigerated Foods delivered for this quarter. But given the fact that we have pork operating margins, as well as a component of commodity sales within that portfolio, we're still sticking to our 5% to 8% range, and when we see that, that's been sustained for a period of time then we'll take a relook at it. The guidance we've given is for over the longer term and through different types of market cycles. So I would expect that the value-added piece should still keep going. Grocery Products definitely should benefit from lower pork input prices particularly on the SPAM family of products, and that should help drive their results in the back half.

Rachel N. Nabatian
Credit Suisse Securities (USA) LLC (Broker)
Q

Great. And then the pork packing margins that we track has been very good so far this year. Can you just remind us how this – how the pork processing [ph] trend (33:38) flows through your Refrigerated Foods business and how maybe excess supply might benefit that business later on in the year?

Jody H. Feragen
Chief Financial Officer, Director & Executive VP
A

So, it's all in – the pork packing margins, or the pork operating margins, as we call it, are included in the Refrigerated Foods. And, yes, they were – they have been lower than last year. Part of that is due to the – what they call the dropped credits, the parts of the animal that traditionally are sold overseas. And with the port issues and the continued strong dollar, we've seen those values go down. So, I think that's impacted the whole industry. I would expect that some of that may pick up in the back half, as we work through the port issues. I'm not recalling the last part of your question.

Rachel N. Nabatian
Credit Suisse Securities (USA) LLC (Broker)
Q

Oh, yeah, I was just wondering if maybe there was too much supply, if that might be a benefit for the processing operations.

Jody H. Feragen
Chief Financial Officer, Director & Executive VP
A

Usually, we like to see – low hog prices are the best thing for our operating divisions.

Rachel N. Nabatian
Credit Suisse Securities (USA) LLC (Broker)
Q

Okay. Great. Thank you.

Operator: [Operator Instructions] And there are no further questions in queue. I'd like to turn it back over to the speakers for any additional or closing remarks.

Jeffrey M. Ettinger
Chairman, President & Chief Executive Officer

Well, this is Jeff. I just wanted to conclude by saying we're very pleased with the record second quarter earnings we were able to announce today. While the next few months certainly will be challenging for our Jennie-O Turkey Store segment, we will look to our experienced team and our balanced business model to deliver a successful year in fiscal 2015. Thanks, everyone, for joining us today.

Operator: This concludes today's conference. Thank you for your participation.