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Hormel Foods Corp. (HRL)
Q3 2019 Earnings Call
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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen, and thank you for standing by. Welcome to the Hormel Foods' Third Quarter 2019 Earnings Release Conference Call. At this time, all participants are in a listen-only mode. As a reminder, this conference is being recorded Thursday, August 22, 2019.

I'd now like to turn the conference over to Nathan Annis, Director of Investor Relations. Please go ahead, Mr. Annis.

Nathan P. Annis  
Director-Investor Relations, Hormel Foods Corp.

Good morning. Welcome to the Hormel Foods conference call for the third quarter of fiscal 2019. We released our results this morning before the market opened around 6:30 AM Eastern. 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 Jim Snee, Chairman of the Board, President and Chief Executive Officer; and Jim Sheehan, Executive Vice President and Chief Financial Officer. Jim Snee will provide a review of each segment performance for the quarter and our outlook for the remainder of 2019. Jim Sheehan will provide detailed financial results and further assumptions relating to our outlook. The line will be open for questions following Jim Sheehan's remarks.

As a courtesy to the other analysts, please limit yourself to one question with one follow up. If you have additional question, you are welcome to get back in the queue. An audio replay of this call will be available beginning at
Before we get started, I need to reference the Safe Harbor statement. Some of the comments made today will be forward-looking and actual results may differ materially from those expressed in or implied by the statement we will be making. Please refer to pages 35 through 41 in the company's Form 10-Q for the quarter ended April 28, 2019 for more details. It can be accessed on our website.

Additionally, please note the company uses non-GAAP results to provide investors with a better understanding of the company's operating performance by excluding volume and sales impact of the CytoSport divestiture.

Discussion on non-GAAP information is detailed in our press release located on our corporate website. Please note that during our call, we will refer to these non-GAAP results as organic volume and organic sales.

I will now turn the call over to Jim Snee.

James P. Snee  
*Chairman, President & Chief Executive Officer, Hormel Foods Corp.*

Thank you, Nathan. Good morning, everyone. Hormel Foods is an uncommon company, unique in our industry. We have a tenured management team who is able to quickly adjust to dynamic and volatile market condition, a balanced portfolio of branded products sold through the retail food service, deli, and international channels, a direct sales force that is able to build and maintain relationships to help our customers grow their businesses, a reputation for bringing industry-leading innovations to the marketplace and an increasingly agile and efficient supply chain.

Our financial position and business fundamentals remain strong. This enables us to deliver growth organically and through strategic acquisition. Our leadership position as a global branded food company allows us to take a long-term perspective as we navigate near-term uncertainty related to various market condition.

Our third quarter results demonstrate many of the qualities that make us uncommon. This morning, we announced earnings per share of $0.37, a 5% decrease compared to last year but in-line with our expectation. The decline in earnings per share was driven by a higher tax rate. Pre-tax profits grew 1% as excellent results from Refrigerated Foods offset declines from Grocery Products. Net sales declined 3% due to the divestiture of CytoSport. On an organic basis, sales were flat on a volume decline of 1%.

Looking at the segment, Refrigerated Foods sales increased 1% on a volume decline of 1%. Segment profit increased 13% driven by higher value-added profitability. Lower operational costs and higher commodity profit played a smaller role in the profit improvement.

Refrigerated Foods achieved record third quarter net sales, value-added sales, segment profit and value-added profit. This was quite an accomplishment by the Refrigerated Foods team. Our Hormel Foodservice division had another solid quarter. The team continues to leverage their direct sales organization to grow brands such as Hormel Bacon 1, Hormel Fire Braised, Natural Choice, Fontanini and Old Smokehouse.

I remain impressed with the innovation this team continuously delivers to the foodservice industry. They are also making excellent progress filling the new capacity for pre-cooked bacon and Fontanini products. We remain very confident in our ability to grow the Applegate brand. Our foodservice team is making great progress growing Applegate with healthcare providers, colleges and universities.
These operators appreciate the point-of-difference the Applegate brand provides for the needs of their patron. For example, the Applegate blend burger is filling a need in the college and university segment as students look for more ways to enjoy natural and organic alternative protein product. The new Hormel Deli Solutions division continues to pursue its vision of helping retailers create the deli of the future, while the Columbus brand and our prepared foods portfolio of products are showing solid growth, the lower margin behind-the-glass category continues to decline.

Consumer preferences are changing as shoppers are looking for more convenient options such as grab-and-go products like our Hormel Gatherings party tray and our authentic line of Columbus charcuterie. While this shift away from the behind-the-glass category presents a near-term challenge to sales volume, I'm confident the ongoing shift benefits the consumer, the retailer and our company over the long-term.

As category leaders, we took price increases across many of our branded value-added products when we started to see sharp increases in input cost. During the third quarter, we were priced high relative to others in many retail category which created higher elasticities than we would typically expect. When higher input cost did not materialize as forecasted, we realigned our pricing to more closely match the commodity market.

Once again, Refrigerated Foods has demonstrated an ability to generate growth in volatile market condition. The long-term growth of this segment continues to be driven by value-added products, disciplined pricing and a clear focus on innovation.

While we have seen how rapid changes in input cost can create noise in its quarterly results, the clarity, focus and alignment Refrigerated Foods demonstrate will continue to deliver sustainable growth. Grocery Products volume declined 10%, while sales declined 11%. Organic volume and sales increased by 1%. Segment profit declined 30% year-over-year due to the divestiture of CytoSport, higher avocado costs for our Wholly Guacamole business and lower earnings from our SKIPPY Peanut Butter spreads business.

Similar to what we experienced in 2017, avocado costs increased by over 100% during the quarter. A smaller California crop and a strong global demand are driving the avocado market prices. In response, the MegaMex team is actively managing promotional tactics and will be evaluating pricing as the new crop is harvested during September. As always, we continue to focus on growing the Wholly Guacamole brand through effective brand building, advertising and innovation.

Our SKIPPY spreads business was negatively impacted by the price decline we took last quarter in response to a competitor's deflationary pricing. While we are disappointed in the category dynamic, we remain focused on building the SKIPPY brand through revenue growth management, effective advertising and continued innovation. A key reason for acquiring the SKIPPY brand was to deliver out-of-the-jar innovation to the category.

The recent launch of SKIPPY P.B. & Jelly Minis has been met with great retailer and consumer acceptance. This innovative item sold in the frozen section is versatile, portable and perfect for today's busy families. We have now reached national distribution, and trial and repeat rates continue to improve. I'm very optimistic about the success of this product line.

While SKIPPY spreads and Wholly Guacamole had a difficult quarter, the balance of the Grocery Products portfolio performed well. Many of our center-store brands such as SPAM, Dinty Moore, Herdez, Black Label bacon bits and Hormel Compleats all had a great quarter. I fully expect all of these brands will show growth for the full year.
Jennie-O Turkey Store volume decreased 4% while sales decreased 5%. Segment profit declined 9% due to lower value-added sale. As we discussed last quarter, we are reactivating promotional activity to gain back lost retail distribution. While we continue to lap distribution losses, we have had a few small wins. We expect the process of regaining distribution will go well into 2020. Over the last few months, we have made changes to the Jennie-O organization to bring in several experienced leaders from other parts of the company who are charged with restoring growth through new and bold ideas for this business.

From an industry perspective, we continue to see lower [indiscernible] (12:40) placements but cold storage remains at elevated levels. Turkey market prices have not materially changed since last quarter. International volume and sales were flat. Organic volume and sales increased 2% while segment profit was up 1%. Our team in China delivered strong results, driven by our foodservice business in addition to growth from the SKIPPY and SPAM [ph] brand (13:11). Exports continue to be affected by global trade uncertainty related to African Swine Fever and tariffs.

Similar to the prior quarter, the uncertainty in the protein industry is related to the outbreak of African Swine Fever. On our second quarter call, we discussed our view that commodity markets would start to increase on higher demand for pork from China. While we have not seen consistently higher prices, we have seen higher volatility and expect that trend to continue. As we evaluate the global impact of African Swine Fever, we are still confident that pork markets will eventually increase. At the appropriate time, we will take the necessary price increases to manage our profitability, which may create short-term margin compression as pricing generally lags input cost increase.

Taking all factors into account, we are reaffirming our full-year guidance of $1.71 to $1.85 per share. We are also reaffirming our sales guidance of $9.5 billion to $10 billion but expect to be on the lower end of the range given market prices have not increased as we previously expected. I have confidence in our team’s ability to adjust to the changing market conditions and deliver our full-year outlook.

At this time, I will turn the call over to Jim Sheehan to discuss our financial information relating to the quarter and our earnings guidance, in addition to key assumptions for the remainder of fiscal 2019.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Thanks, Jim. Good morning. Net sales for the third quarter were $2.3 billion. Organic sales growth in three of the four business segments was offset by declines at Jennie-O Turkey Store. Pre-tax earnings were $261 million, up 1% from last year. Net earnings were $199 million and diluted earnings per share was $0.37, down 5% due to a higher effective tax rate. The significant increase in the tax rate was driven primarily by lapping the one-time gain from re-measuring the deferred tax liability last year. The tax rate was higher than we anticipated because of the lower volume of options exercised in the quarter. The full-year tax rate is now expected to be between 18.3% and 20.3%, up from the previous estimate of 17.5% to 19.5%. SG&A, excluding advertising was 6.5% of sales compared to 7.3% last year. The decline was due to the impact of the CytoSport transaction and lower employee-related expenses.

Net unallocated expense declined $10 million, driven by lower interest expense and universal stock option expenses in the prior year. Advertising for the quarter was $32 million, down from $40 million last year. Advertising investments are expected to be lower primarily due to the sale of CytoSport. Operating margins were 11.2% compared to 10.9% last year. Strong results in Refrigerated Foods and favorable SG&A led to the improved performance.
Year-to-date cash flow from operations was $573 million, down 23%. The primary driver was increased levels of working capital, as we build inventory in anticipation of higher raw material cost. This thoughtful approach to building inventory should mitigate some of the input cost volatility as markets rise. For the quarter, capital expenditures were $67 million compared to $103 million last year. We expect to spend approximately $250 million in 2019. Weather delays and changes in project scope impacted the projected capital spend.

We paid the 364th consecutive quarterly dividend effective August 15 at an annual rate of $0.84 per share, a 12% increase over the prior year. This completes our 91st year of consecutive dividend. Share repurchases in the quarter were $107 million, representing 2.7 million shares. We will continue to repurchase stock to offset dilution from stock option exercises and based on our internal valuation. Our balance sheet remains strong, that allows us to fund strategic investments to grow the business.

Fundamentals in the turkey industry are mixed. Poult placements are down 4% year-to-date, breast meat in cold storage is above last year and the five year average. Turkey prices remained above $2 for the quarter, a 10% increase from last year. Feed cost for the quarter was similar to last year. Avocado prices are expected to decline through October but remain above last year. We will have better visibility as the Mexican crop is harvested in the next few weeks.

Pork input cost in the third quarter did not dramatically increase as we forecasted last quarter. Cold storage reserves in China, uncertainty caused by global trade dynamics, and robust hog production likely contributed to lower markets. Pork input cost in the third quarter did not dramatically increase as we forecasted last quarter. Cold storage reserves in China, uncertainty caused by global trade dynamics, and robust hog production likely contributed to lower markets. The USDA cut out traded between a wide range of $72 and $89 per hundredweight during the quarter, never reaching our forecasted level. Hog markets exhibited similar behavior, trading between $68 and $85 per hundredweight. Belly prices for the quarter were significantly below the forecast, trading in a $49 range between $127 and $176 per hundredweight. Trim briefly met the forecasted highs before dropping 40%.

The third quarter clearly demonstrated our team's ability to manage through extreme volatility in core commodity markets, to deliver results in line with our expectations. The guidance for the fourth quarter assumes higher prices for our key inputs with potential for volatility like we experienced in the past quarter. The overall fundamentals still support a sustained high cost environment in pork market beginning as soon as the fourth quarter due to African swine fever. Hog supplies in China, Southeast Asia, and now regions in Europe are being affected. The exact timing and magnitude of the impact remains uncertain. We will provide a detailed view of market assumptions and the outlook for fiscal 2020 on the November call.

We were making significant progress on Project Orion and our one supply chain initiative. For example, we are in the process of opening two new distribution centers in the coming month. On a combined basis, we will save over three million miles in our Grocery business alone. Project Orion will unlock more opportunities for cost savings similar to this project. The team is focused on implementing major phases related to finance, HR and supply chain during fiscal 2020.

At this time, I'll turn the call over to the operator for the question-and-answer portion of the call.
QUESTION AND ANSWER SECTION

Operator: Thank you. The question-and-answer session will be conducted electronically. [Operator Instructions] We'll take our first question from Rupesh Parikh with Oppenheimer.

Erica Eiler
Analyst, Oppenheimer & Co., Inc.

Good morning. This is actually Erica Eiler for Rupesh. Thanks a lot for taking our questions. So first, as we look at SG&A here, down nearly 15% this quarter, I was just hoping to better understand what the SG&A expense run rate was ex-CytoSport? What's driving that performance and how you're thinking about the expense opportunities going forward?

James N. Sheehan
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Well, we think – good morning. We think that the run rate will be generally lower than it was in the fourth quarter of last year because – primarily because of the CytoSport sale.

Erica Eiler
Analyst, Oppenheimer & Co., Inc.

Okay. And then just, I mean given a lot of moving pieces in your business, from CytoSport to Skippy, Jennie-O, African swine fever, just wondering if there are any early thoughts you can provide on fiscal 2020 at this juncture. Just any puts or takes we should be thinking about would be helpful.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. It is early for 2020 given the uncertainty and the volatility that we've seen in the markets. But as we think about all of the different business segments, Refrigerated Foods continues to be very well-positioned and they have demonstrated their ability, their long-term ability to grow in volatile markets across foodservice, deli, retail. Grocery Products, although we had some noise in the quarter with avocados, we remain positive on many, many of the brands. And of course, we could have some input pressure there but I think the longer term brand story and the insights-led innovation have us poised for growth.

JOTS continues to be a work in progress, as I said in my prepared comments. We've had some small wins, but we do expect the recovery to spill over well into 2020. We think the business has stabilized and now we do need to get back to growth. International is obviously a wildcard, uncertainty based on African swine fever and tariffs. But we're optimistic about the business that we have in China. We feel like we can reflect pricing to accommodate any of the input costs that we have. And then also the SPAM and Skippy businesses that we've developed are very strong.

And then any conversation about our business has to finish with a strong balance sheet, so we are poised for M&A, we're always ready to make acquisitions when the time is right. But it's early for 2020 given some of the uncertainty in the marketplace but we are confident in our ability to grow over the long-term.
Okay, great, that's helpful. Thank you so much.

**Operator:** And next we'll go to Ben Bienvenu with Stephens Inc.

**Ben Bienvenu**  
*Analyst, Stephens, Inc.*

Yeah, thank you, good morning. I want to ask a clarifier question about the guidance for this year. Jim, you said that you expect full-year sales guidance to be toward the lower end of the range. The earnings guidance for 4Q is quite wide. Would you expect the EPS guidance to reflect your commentary on the sales guidance?

**James P. Snee**  
*Chairman, President & Chief Executive Officer, Hormel Foods Corp.*

Yeah, no, I don't think that's a fair assumption Ben. I think from a top line perspective it is how we are pricing. And as we mentioned in the prepared comments, as markets did not materialize the way we thought. We did realign pricing in the quarter to make sure that we remained in very competitive position. So I think the sales guidance is one thing and it is different from the earnings guidance.

**Ben Bienvenu**  
*Analyst, Stephens, Inc.*

Okay. Great. And a follow up on the pricing, can you help us think about how you think about using trade promotion spend to reduce the pricing increases that you had put in place versus actual list price reductions, particularly on an environment where input costs are as volatile as they've been over the last several months.

**James P. Snee**  
*Chairman, President & Chief Executive Officer, Hormel Foods Corp.*

Yeah, I mean the interesting thing is it is unique and different retailer by retailer. And we've talked about that over the last several quarters, about how that's important to engage our direct selling organization with the customers, to understand what the optimal solution is for their customer base. And so, we do move promotional dollars or trade dollars around to make sure that we've got them priced properly on a net basis. We work closely, of course, to make sure that the shelf price is reflective of where it needs to be. But, I mean, we -- again, depending on the situation, we're willing to invest the trade dollars, but it is a customer-by-customer decision.

**Ben Bienvenu**  
*Analyst, Stephens, Inc.*

Okay. Thanks.

**Operator:** And next we'll go to Heather Jones with Heather Jones Research LLC.

**Heather Jones**  
*Analyst, Heather Jones Research, LLC*

Good morning. Thanks for taking the question. I want to go back to a comment you made about raw material. I think you were talking about cash flow, use of cash. And so, just wondering if you could flesh that out more? Which segments are you building raw materials in? And like -- any practical limitations? I mean, do you have the
capacity to build substantial raw material inventories that could cover portions of 2020 or is it more limited to a quarter? Just wonder if you could help us understand that more?

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Certainly. The inventories are really being built in the Refrigerated, GP and International areas. Are there limits? Yeah, there's a supply limit as to how much you can build inventory. We take a look at the trends that we believe are going to take place and we build selectively in certain commodities and certain finished goods.

Heather Jones  
Analyst, Heather Jones Research, LLC

Okay. Thank you. And then my next question is on Jennie-O. So, just – you mentioned that the recovery is going to spill over into 2020, so trying to – in your efforts to regain distribution, I would assume you have to be somewhat sharper on price. I was wondering, is the anticipation that, that would be only for like a year or so? Or how long do you think you would have to lock in the pricing to regain the distribution? Basically, I'm trying to get a sense of what kind of lag could we see in Jennie-O recovering with [ph] water protein (00:29:56) markets over the next year or so?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

I think as we said, Heather, this does remain a distribution issue. Our velocities, where we're in distribution, remain very strong. We have had some small wins, as I said in my prepared remarks, so we are gaining some momentum. We've turned on advertising in select markets, and we'll be – we'll have the opportunity to evaluate the effectiveness before expanding.

And I also mentioned in my prepared remarks that we have brought in some additional experienced sales and marketing leaders from other parts of the organization to really jumpstart that business. But it's still going to take time. And so, as we're thinking about it, it's probably going to be mid-2020. And you're right, there are some investments that have to be made to regain distribution, but we're prepared to make those investments. And, really, the big thing is that we do feel like this business is stabilized and it is time for us to get this business back to growth.

Heather Jones  
Analyst, Heather Jones Research, LLC

Okay. Thank you so much.

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yes.

Operator: And next, we'll go to Adam Samuelson with Goldman Sachs.

Adam Samuelson  
Analyst, Goldman Sachs & Co. LLC

Yes. Thanks. Good morning, everyone.
James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.  

Morning.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.  

Morning.

Adam Samuelson  
Analyst, Goldman Sachs & Co. LLC  

So, I guess, just digging a little bit more into the outlook for the fourth quarter and just – it is a wide range on the earnings side, and Jim I appreciate the comments that the sales and earnings don’t necessarily align at the lower end of the range, but just help me understand kind of the range of outcomes that get you towards the low and high-end of the range, presumably the bigger variable is for raw material costs. But just help me think about kind of the range of outcomes as you’ve laid out in your outlook.

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.  

Sure, I mean you hit it right on the head, Adam. It is, I mean, it is all about the input cost, and that will impact pricing, and of course the elasticities that come along with the pricing moves. So if we get some additional false positives like we had in the second quarter, that could be problematic. But the run up in input costs as you know, I mean it does create that short-term margin compression, but we’ll be aggressive with our pricing as category leaders. That’s what we do. But we know that pricing does lag the input costs. So, and you hit it right on the head, that is going to be the primary driver for that range. And we do believe that the range is warranted, given some of the volatility that we’ve seen in the third quarter.

Adam Samuelson  
Analyst, Goldman Sachs & Co. LLC  

Okay. And then I was hoping to understand a little bit more, digging into 2020, just the things that are in your control, maybe on Project Orion specifically and some of the supply chain initiatives. I mean how – can you quantify how much those actually benefited the quarter on a net basis? How much they’re benefiting 2019 on a net basis or kind of what your run rate exiting the year looks like to think about kind of potential savings into 2020 before we then layer on sales or raw material input cost view?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.  

Sure. If we go back to my earlier comments starting with the segments, from a 2020 outlook, the food service business continues to be hitting on all cylinders. We feel really good about the deli business, the retail business, whether it’s our Hormel retail business, the Applegate retail business, and we’re optimistic about all of them. We know that there could be some of that short term noise, that margin compression, as a result of input cost.

But Refrigerated Foods has really been on a nice run, and we expect that to continue. Grocery Products, the work that the team has done around brand building with [ph] several other store brands has been really, really impressive. We do think that the avocado crop that’s coming in, we’ll have a better read on that. Probably some more favorable input costs that’ll give us some relief there. That’s outside of our control, but what’s
in our control is our ability to make sure that we're building that brand through promotion and advertising and innovation. We'll continue to do that. So we do feel good about Grocery Products.

Probably the one that's outside of our control the most will be International based on what happens with African swine fever and tariffs, and really the global trade uncertainty. Part of it is in our control with our ability to run our business in China, but there are going to be some market impacts. And then, the jobs piece is going to be in our control and our ability to execute the business, so – or execute distribution gains. We've got to get that done, continue to get that done in the fourth quarter and into 2020.

From a supply chain perspective, we're not going to get into the 2020 outlook for that. But we're committed to the savings number that we gave this year, the $75 million. We've had a lot of success with a lot of projects. We referenced in Jim Sheehan's comments the fact that we've got our new Grocery Products DC opening that'll save us 3 million miles, and there is a corresponding financial benefit. We're evaluating our Refrigerated Foods network, and we've had a better global view of plant performance. So, I mean, there's a lot of benefits that we've seen from not only our one supply chain but Project Orion, and we expect that to continue over the next several years.

**Adam Samuelson**
Analyst, Goldman Sachs & Co. LLC

And if I could just sneak one quick kind of follow-up. The CapEx reduction for this year, there was some timing with the results allusion to project scope changes. I mean, how much of that – I think it was $100 million reduction – really comes in next year versus the actual cost of the programs or their projects goes down.

**James P. Snee**
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. The majority of that is timing. We had a really wet spring here in the Midwest, and we've got a very big project going on at Burke, and so that's shifted some of those expenditures back. But the one thing I want everyone to know is that there is not a lack of commitment. Our commitment to CapEx spending and investing in our value-added business is as strong as it's ever been.

**Adam Samuelson**
Analyst, Goldman Sachs & Co. LLC

Okay. I appreciate the color. Thanks.

**James N. Sheehan**
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Yeah.

**Operator:** [Operator Instructions] Next, we'll go to Eric Larson with Buckingham Research Group.

**Eric J. Larson**
Analyst, The Buckingham Research Group, Inc.

Yeah. Good morning, everyone. Thanks for taking my question. Either Jim can answer this question, but we've seen just a lot of hog supplies on the market, particularly June and July and et cetera, and again a lot of volatilities with lean hog pricing. My question is, have farmers anticipated ASF? Do you think there's been expansion in the herd industry because of ASF or not, or what might be some of the dynamics that you see going on there?
Obviously, we’ve got corn prices back down sharply as well soybean meal as well. But what might be the mentality for a hog expansion that we see out there for the next 12 months? And what's happened recently do you think?

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Well, I think some of it is a reaction to the additional hog processing capacity that's in the industry right now, and it anticipating that capacity increasing, they've increased their production. We certainly do see that hogs today are about $70. They're relatively cheap input – there's cheap input, as you said, the grain is at a low cost basis right now. So, I think there are encouragements to increase hog production. It's in line with what expectations were. But, I think, probably the biggest driver was that there's been probably two years or more of discussion about the additional capacity coming online. They've had time to react and those hogs are available to us.

Eric J. Larson  
Analyst, The Buckingham Research Group, Inc.

Okay, and then, just a broader follow-up. As to your comments Mr. Snee, Jim, about your supply chain efforts and it's a multi-year kind of project, and so you've quantified what you thought your supply chain savings would be this year. I mean, without getting into specifics, is this – this is something that is a multi-year project. Is there a way to try to quantify what that might be or are you in a position you can talk about that?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. I mean, I think when we get into our fourth quarter call, we'll obviously give a little more color and clarity. And then, the other variable is, as we continue down the path with Project Orion, we'll have more opportunities that will reveal themselves.

But the part about this being a multi-year project, I mean, I don't even know if I would refer to it as a project. I mean, this is a permanent part, a permanent structure that we have in our organization that we've needed. I cited a couple of specific examples. As we think about just having that global view of plant performance, better meat utilization, and then even some of the, I'll say, some of the softer things about how we're better prepared to approach training and recruitment in an environment where workers are harder than ever to come by, it's important that we have one standard approach to how we're doing things. And so, the benefits of the one supply chain initiative have been very impressive and far reaching in the organization on a number different fronts.

Eric J. Larson  
Analyst, The Buckingham Research Group, Inc.

Okay. Thank you.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Yes.

Operator: And next, we’ll go to Robert Moskow with Credit Suisse.
Hi. Thanks. Couple questions. The price increases that you took in May, are they all reversed now or are there – is there any residue of that pricing still on the market?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Hey, Rob. Good morning. It really depends on the category. So, if you think about what happened in bacon, for example, that pricing does tend to realign itself more frequently. And so, we've seen realignment down and the market now has taken another run back up. So, it has moved a couple of times since we last talked, but we know that that's what we have to do to remain competitive. In terms of pepperoni, the pricing that we took there was realigned because the trim market did not at all sustain what we thought it was going to do and remains low today.

In our Grocery Products front, the SPAM pricing that we took, that helped. But that is – that was really, was less related to raw material, more other inflationary measures. So, it's really been a mixed bag across the different categories. But, I mean, we feel good about the pricing actions we took and the corresponding realignment.

Robert Moskow  
Analyst, Credit Suisse Securities (USA) LLC

Got it. And then, a follow-up. The Grocery division, I mean, I haven't seen the margins dip below 11% in a quarter. I don't remember the last time. I think you're kind of hinting around here that, hey, a lot of it is transitory, related to the crop availability and all that. But why wasn't the crop availability this big of an issue in second and first quarter for avocados? Like why is it suddenly hurting the margin to this degree? And then, as we look forward, how quickly can we assume that a normal crop in September will adjust the margins higher?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. That's a great question. So, the secondary crop impacts our supply situation primarily in Q3. And if you go back to 2017, not on an overall GP margin structure, but if you go back, I mean, we had a very similar situation 2017. And at that time, we were very aggressive with our pricing. And this time, we've – we reevaluated and thought we were going to be in a better position to just wait to see what the next crop looks like.

So, this secondary crop primarily impacts us in Q3. And then, in early Q4, we start to get a better read on the primary crop. And so, early indications are that that's more favorable. So, that will have some impact in Q4. But then, we'll have the primary impact again in Q1 and Q2.

Robert Moskow  
Analyst, Credit Suisse Securities (USA) LLC

Okay. That's very helpful. And it's August, so I'm going to ask question number three here. Jim Sheehan, I think you talked about Project Orion and the supply chain efforts. And I get that. But I think you also mentioned finance, HR, as well as supply chain as areas where you'll be evaluating more productivity. Can you be more specific on what that means?

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Certainly. We will be implementing a single instance of all of our ERP systems across finance, HR, and the supply chain, meaning that all operations will be operated on a common platform, will create great efficiencies in the
Robert Moskow  
Analyst, Credit Suisse Securities (USA) LLC  
Got it.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.  
...the other issue is, is the quality of information and the decisions that we can make based on that data. Where, before, we'd have to mine through multiple systems to get information, where this will provide a common platform, the information will be readily available, and we can do analysis across all aspects of the business.

Robert Moskow  
Analyst, Credit Suisse Securities (USA) LLC  
Very good. Thank you.

Operator: [Operator Instructions] Next we'll go to Thomas Palmer with JPMorgan.

Thomas Palmer  
Analyst, JPMorgan Securities LLC  
Good morning. Thanks for the questions. Wanted to, I guess, first kick off just talking about the price elasticities that you saw on pork products. Was it as you expected? Do you think it was a little more severe because you were out of line with the industry? And kind of what insight does that give you as you think about potentially layering on new price increases in the coming year?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.  
We saw greater elasticities than we thought, especially in bacon and pepperoni. And it really was the fact that the markets did not perform on a continuous basis. So, we reached some point of elevation in the belly market and the trim market that really put us into action on the pricing front. What changed was we took pricing, some of the others in the category didn't, and then the market didn't sustain. And so, when that happened, we were priced higher than the category which created those higher than expected elasticities. And that's where our pricing realignment came in.

Once we got our pricing realigned, we felt like the elasticities were in line with what we expected. Bacon's back on track, we think pepperoni is. And then, we did talk a little bit about the Grocery Products pricing that we held with SPAM. And from SPAM's perspective, volume was relatively flat and sales were up 4%. So, if anything, that outperformed the elasticity we expected. So, as I said earlier, it really was a mixed bag across all of the different categories where we took pricing.

Thomas Palmer  
Analyst, JPMorgan Securities LLC  
Okay. Thanks for that. And then, I just wanted to circle on the avocado side. Though it sounds like you elected not to take pricing in part because you think that at least a portion of the severe inflation you're experiencing is temporary, if you do decide early in the fourth quarter as you get the read-through, how long does it take to
implement pricing? When does that start to materialize in terms of the P&L impact from a COGS standpoint that either the crop's favorable or not? Is this – come the first quarter, we would see both kind of pricing in COGS basket changing for the new crop or the timing different than that?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Got it. You would expect to see impact tail end of the fourth quarter, really into the first quarter, either way. From a pricing perspective, if we do choose to take pricing, it's very consistent with the other retail pricing dynamics that we see, and I expect it to take approximately 60 days to get into the marketplace. So, the team will have a pretty good read on it in short order, and we'll be able to make the right business decision.

Thomas Palmer  
Analyst, JPMorgan Securities LLC

Great. Thank you.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Yes.

Operator: Okay. Next, we'll go to Rebecca Scheuneman with Morningstar.

Rebecca Scheuneman  
Analyst, Morningstar, Inc. (Research)

Good morning. So, I have a question about the Grocery Products margin. Was there any part of the margin decline there that can be attributed to the sale of the CytoSport business, or is that entirely explained by avocados and peanut butter pricing?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Go ahead, Jim.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Yeah, from a margin standpoint, it's really about the avocado prices and the peanut butter.

Rebecca Scheuneman  
Analyst, Morningstar, Inc. (Research)

Okay, so nothing at all from CytoSport?

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

No, I mean, as we stated, the CytoSport would have about a $0.04 impact for the back half of the year from a P&L standpoint. But for margins, it's really driven by the avocado costs...
Rebecca Scheuneman  
Analyst, Morningstar, Inc. (Research)  
Yeah.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.  
...and the peanut butter.

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.  
[indiscernible] (00:50:11)...

Rebecca Scheuneman  
Analyst, Morningstar, Inc. (Research)  
Yeah, okay.

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.  
...that we have.

James N. Sheehan  
Executive Vice President & Chief Financial Officer, Hormel Foods Corp.  
Yeah.

Rebecca Scheuneman  
Analyst, Morningstar, Inc. (Research)  
Okay, thanks. And then, my second question is, with this global protein shortage resulting from ASF, is there any reason to believe that this wouldn't improve the demand for turkey heading into next year?

James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.  
I think that's a fair assumption. I mean, we need to see how this all plays out through this global trade uncertainty and how the global supply reorganizes. But I do think there is a point of view out there that says poultry products, turkey in particular, could benefit. So, I mean, we'll see how that materializes the balance of this year and into 2020. But I think that's a fair assumption.

Rebecca Scheuneman  
Analyst, Morningstar, Inc. (Research)  
Yeah. Okay, great. Thank you so much.

**Operator:** [Operator Instructions] And I show we have no further questions. I'll now turn the call back over to our speakers for any additional comments or closing remarks.
James P. Snee  
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Great. Thank you. Thanks all of you for your participation and interest this morning. While our team continues to navigate near-term uncertainty, I remain very certain in our team's ability to deliver our key results and finish 2019 in a very strong manner.

Thank you. Have a great day.

Operator: And that does conclude today's conference. We thank you for your participation. You may now disconnect.