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Hormel Foods Corp. (HRL)

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MANAGEMENT DISCUSSION SECTION

Jonathan P. Feeney
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Will you please find your seats? Good morning, everyone. Once again, I'm Jon Feeney CAGNY Conference co-chair, and once again I have the pleasure of introducing Jeff Ettinger, Chairman and Chief Executive Officer of Hormel Foods. But first, I'd like to take this opportunity to thank Hormel for hosting lunch today, featuring many of their leading branded retail and foodservice items. That will be immediately after this presentation.

Hormel was nice enough to move up their strong earnings release this morning for this presentation, which you probably saw this morning. Just like they've been nice enough to lead the industry in returns for the past 15 years, and to grow dividends every year for the past 50. For 125 years, they've been the protein company everyone else would like to be. And through the recent acquisitions like SKIPPY and MUSCLE MILK, they're very quickly becoming the food and CPG company everyone would like to be.

Today, their Chief Financial Officer Jody Feragen will cover the highlights of their earnings in lieu of an earnings call first. Well, both Jeff and recently-named President and Chief Operating Officer Jim Snee will follow up and focus on their long-term strategic efforts, of course followed by your questions.

So, Jody welcome, thank you. Take it away.

Jody H. Feragen
Chief Financial Officer, Executive Vice President & Director

Thank you, Jon for that introduction. Before we get started this morning, I need to remind you that certain statements will be forward-looking and they're based on current conditions. And I would refer you to the risk

factors on our 2015 annual report. Additionally, 2015 results are non-GAAP numbers, that excludes certain adjustments and those two are detailed in the annual report and also in the back of the presentation that you received when you walked in today.

As Jon said, we did wait to deliver our record quarter for this morning, \$0.43 per share, our 11th consecutive quarter of record earnings and we were pleased that four of our five business segments contributed to the growth. Now, sales were down 4% due to lower pork markets as well as the turkey harvest supply issues that we'll talk about later.

You'll note that the earnings per share and all the earnings per share numbers in the presentation have been adjusted for the two-for-one stock split that our shareholders approved on January 26 and became effective on February 9. So, taking a look at the segments, Grocery Products segment operating profit was up 26% really benefiting from improved operational and supply chain efficiencies.

In the first quarter of 2015, we rationalized our plant in Stockton, California and moved that production into other facilities, so they're seeing a nice benefit from that and they're also winning with favorable raw material costs. Sales were down 4% as we saw some softness in the canned meats area, but we were really pleased with the results of our HORMEL bacon toppings, our CHI-CHI foods products and our WHOLLY GUACAMOLE items.

Refrigerated Foods had an outstanding quarter, segment profit up 65% and really it was great improvement, a great performance across all our value-added businesses, as well as strong operating margins. This segment also benefited from the inclusion of the Applegate Farm operations, that was a business we acquired in July of 2015 and it continues to perform as we expect it. I think you'll hear a little bit more about that later in the presentation today.

Sales were up 2% on a 5% volume increase as the higher sales were offset by those lower pork prices. We did see nice gains in our HORMEL refrigerated entrees or HORMEL party trays in the retail side, as well as OLD SMOKEHOUSE bacon and FIRE BRAISED meat from the food service side.

Jennie-O Turkey Store operating profit was down 2% for the quarter, really still recovering from the impact of highly pathogenic avian influenza did hit our farms in Wisconsin and Minnesota midway through 2015 last year. We're seeing improved bird performance and we would expect that by the end of our second quarter, they should be back at normalized operations providing we see no further widespread outbreaks of AI.

And then, they'll also benefit from lower feed cost as grain prices have been lowered. Sales were down 15%, volume down 23%, and really that was just a supply issue as we are vertically integrated in the turkey side of the business.

Specialty Foods operating profit was up 44% on a 10% decline in sales. They too benefited from favorable input costs and also some supply chain efficiencies as we look to rationalize the MUSCLE MILK production into some of our existing facilities. We were pleased with the growth of our MUSCLE MILK product, particularly the ready-to-drink item, but we did see decreased sales of some contract packaging for its nutritional items that were at a low margin basis.

International saw a 1% increase in operating profit on a 7% decline in sales. We were very pleased with the strong SKIPPY sales both on an export basis as well as SKIPPY sales within our China operation, but they couldn't offset softer pork exports as we continue to battle challenging market conditions.

Our China results were lower year-over-year. First quarter 2015, we were able to import SPAM and sell that in the domestic marketplace in China, and that's not – no longer an option, so they are up against those difficult comparisons, but we are fully looking forward to our plants that we are building in China to provide us the opportunity to sell SPAM to that marketplace.

Some other financial metrics that we traditionally go over on our call. Advertising spend was \$48.1 million, up nicely from last year. We would expect full-year to be at low double-digit area. Our effective tax rate was 33.6% and we are expecting approximately 33.5% to 34% for the full-year. Depreciation and amortization was slightly under \$32 million, while our capital expenditures were \$33.5 million. As a reminder, we guided at the end of our fourth quarter that we were expecting approximately \$250 million in CapEx. And you'll hear about some of the projects later in the presentation.

From a market outlook – outlook perspective, we are expecting hog production to be up about 2%. And while we benefited from historically high favorable pork operating margins in the first quarter, we would expect those to moderate as the year goes on. Turkey production, assuming no widespread outbreaks of avian influenza, is expected to be up 5% to 6%. And as that production increases, we should see prices moderate in the back half. Grains will be favorable year-over-year versus 2015 and as a reminder, we traditionally look to hedge between 25% and 75% of our needs on a two-year forward-looking. We have a very strong balance sheet, the \$185 million of short-term debt that was on the balance sheet at the end of our fourth quarter related to the Applegate transaction was repaid and we now have \$250 million of long-term debt on our balance sheet, which we really believe gives us the opportunity to continue to look at all types of investments, and I believe we could have \$3 billion of additional debt on our balance sheet and still remain investment grade.

Our excellent earnings results coupled with our disciplined capital model has allowed us to generate cash flows over the last five years of 21% growth rates, and if you look at the trailing 12 months ended in the first quarter, we were up over 65%, so certainly generating the nice cash flow.

And our priorities have remained the same, pretty consistent year-over-year. We look to invest in our businesses as well as to return to our shareholders. We've invested about \$2.8 billion in growing our business, some of that organic, being capital investments. We'll talk about adding capacity to meet some of the demand for our value-added products and then about \$2.1 billion in strategic acquisitions. The way we look at these investments is the same regardless if I'm adding internal capacity or looking at a strategic acquisition, we build the base case business model, we use a long-term cost of capital, and we do a discounted cash flow and we believe that that allows us to make the best decision for our shareholders.

Speaking of shareholders, we believe in returning to our shareholders our excess cash flow. Our share repurchase is a little more opportunistic given our ownership structure, but we certainly are pleased with our dividend results, and as Jon referenced, 50 consecutive years of dividend increases, our board of directors approved a 16% increase for 2016. And our average growth rate over the near term has been about 18% in excess of the excellent bottom line that we've been able to deliver, as we try to get a payout ratio and a dividend yield closer to our packaged food peers. So, excellent earnings results, disciplined capital allows us to put up a return on invested capital that's in the top quartile of our peer group.

And with that, I'm going to turn it over to Jeff Ettinger.

Jeffrey M. Ettinger
Chairman & Chief Executive Officer

It was our pleasure to be with you here this morning to be able to share what was an outstanding quarter for Hormel Foods, and to be back at CAGNY after a few-year hiatus and let you know what we've been up to and what our priorities are going forward in terms of our brands and our team.

As Jon was nice enough to mention, we are also hosting lunch. So we don't have a formal Q&A session after this, but we'll all be available including others of our team during lunch to take any additional questions you might have.

One of the questions you could ask anybody and that is, what does 5 and 10 mean to Hormel Foods? 5 and 10 has been our consistent goals within our corporation for the past 10 years. We strive to achieve 5% revenue growth each year and 10% earnings or operating income growth. These are among the most aggressive goals within the food industry, and even in our past presentations here at CAGNY that Jody and I have done, you should have consistently seen that these were our goals at those sessions as well.

Importantly, we've really done a nice job at achieving those aggressive goals. Our track record over the past five years on the top line is indeed at that 5% rate, we're now a \$9.3 billion company. And in – area of earnings, we've actually been able to exceed our 10% goal with a 12% CAGR capping out last year. What I want to share with you is kind of how we've done that, and a little bit of our thinking behind some of the decisions we've made that have led to these types of results. We've grown our company on a top-line basis and certainly significant profit contributions in three ways, through M&A, through new product innovation and by continuing to expand our traditional product portfolio.

In the area of M&A, we certainly had an active decade during the 2000s with a number of deals, somewhat smaller deals ranging from about \$50 million to \$200 million in deal value over a broad spectrum of products. This array of deals enabled us to gain confidence in our ability to integrate and to look for new prospects, but as we headed into the most recent timeframe, we kind of did make a couple of changes in our mentality toward acquisitions.

We look for somewhat larger deals, our company is getting bigger and in order to move the needle, we recognized we needed to look at bigger opportunities. And so four out of the five largest deals in the company's history have come in the past four years, WHOLLY GUACAMOLE at a total deal value of north of \$200 million counting an earn-out, SKIPPY which was done – we've completed in 2013, a \$700 million deal. MUSCLE MILK in 2014 was a \$450 million deal and then most recently Applegate at \$775 million.

In additions to the deals being larger, we also looked critically at our portfolio and said, you know I mean, our core portfolio, we love a lot of the items that have been with us a long time, and we're continuing to grow those items. But honestly, it was a very American-dominated portfolio with a lot of kind of traditional American food type items, neither SPAM, nor our bacon items are probably going to be accused of being health-oriented items anytime soon. And we recognized that consumers are more and more on the go, and our portfolio is really dominated by kind of sit-down meal type items.

So all four of these acquisitions and Jim is going to give you more detail on these, really are aimed at making our portfolio more global, more multi-cultural to add that element of health and holistic attributes and to provide on-the-go solutions.

Another decision you have to make when you acquire something is how are you going to run this operation. There – we're still headquartered in Austin, Minnesota, a small town, two hours south of Minneapolis, and indeed, for some of these properties, particularly businesses or brands that we buy from another company or corporation, we tend to fold those and run those in-house, and so that was true of the domestic SKIPPY business, it was true of the Lloyd's barbecue line, it was true of the Country Crock side dishes who are now named Hormel side dishes.

For some of these recent deals, however, we have looked at those deals and said, look, to really optimize the consumer connection and the uniqueness that some of these opportunities provide, we may need to look at running them a little bit differently. We still try to find ways to harmonize and gain synergies on a back-room basis in every chance we get. But in terms of that direct-to-consumer connection point, for example, SKIPPY in China, it came at the plant in China, from which we sell to most of Asia and so they are Chinese team that have been in place for over 15 years that's taken on that business.

MUSCLE MILK had a strong presence in Northern California, was kind of a young, vibrant market, and we wanted to maintain that, so we've left that team there, supplementing with a few folks in the Hormel organization. MegaMex, into which we put the WHOLLY GUACAMOLE acquisition, is a joint venture. Our partners are two companies from Mexico, Grupo Herdez and Grupo KUO, and so on a combined basis, we run that entity from Southern California, which certainly is a hot market for understanding the Mexican food experience.

And then very recently with Applegate. This team and this business really had both a unique supply chain of organic and antibiotic-free natural products, and also a very strong consumer connection to a unique set of folks that we wanted to make sure we preserve that connection. So, in order to go with this theme of kind of providing you with a little bit of a behind-the-scenes mentality of what we've been seeking to do, I want to share with you now a video that kind of depicts what the Applegate experience is all about from the mouth of their team members.

[Video Presentation] (16:02-18:30)

New production innovation is also a key element of our growth story at Hormel Foods. Indeed, our Founder, George Hormel, founded the company on the principle of innovate, don't imitate. We've had a number of notable successes over the years, including our party trays franchise, Natural Choice, our BACON 1 items for the foodservice trade.

Within the retail world, we recently were recognized as an IRI Pacesetter for three of our items. This is a tracking of the last 52-week sales by the IRI organization of the best-selling new products in the United States. And so, we were pleased that our MUSCLE MILK Pro Series, our REV snack wraps, and our WHOLLY GUACAMOLE minis all made this list. And then each year, the editors from Progressive Grocer magazine bring in products from all over the country and have their editors try these items and see what they're excited by, and we were excited to see that we had eight items from our overall organization, ranging from FARMER JOHN to Jennie-O Turkey Store to our meat products group to our Grocery Products group, that made this list.

The third area of growth I mentioned in top of M&A and innovation is continuing to emphasize the growth of our core items. More often when we're talking to the press, we're kind of known as Hormel, maker of SPAM still, so that's a long-term core item we've had. And I'm going to let you in on a secret, SPAM is still growing. It's growing at a 3% CAGR over the last five years in the U.S. and a 7% CAGR outside of the U.S.

But in addition to SPAM, we own a number of other items within the portfolio that we've been able to create really nice household penetration growth, ranging from our flavor bacon portfolio to our HERDEZ authentic Mexican sauces, to Jennie-O Turkey Store Lean Ground Tray pack and Chub items to our Hormel Pepperoni items.

And the story is a little bit different for each of them in terms of what's driven that growth. For the flavor bacons, these were items that, frankly, we borrowed from our foodservice team. We came up with these innovative flavors for the restaurant trade, and they were so popular there that we created retail versions of the items.

For HERDEZ, it's been geographic and consumer expansion as authentic Mexican food is going into more and more cities in the U.S., and is seen as an authentic eating experience by more and more consumers who are looking for that kind of local item.

For Jennie-O Turkey Store, it's been the advertising, the Make The Switch campaign that has enhanced awareness of overall Jennie-O and has enabled us to ride the wave of consumers looking for more health-oriented items. And even pepperoni menus that have been around for 100 years, we've been able to grow households recently, and in that case, I think recipes have driven a lot of it as we've encouraged consumers to put pepperoni pieces and slices on many more items.

I mentioned to you though that this growth of our overall company, the top line were all the items I just mentioned, and that some of the bottom line has come from the enhancement of these portfolio items. But clearly, some of that 12% CAGR on the bottom line has come from cost efficiency gains. We don't tend to have kind of active projects going on. We try to really watch this on a continual basis. Another one of the founding principles of George Hormel was continuous improvement, always seeking to find a way to do the job a little bit better day in and day out. One of the ways this manifests itself is through our Best of the Best projects. We encourage our teams from throughout the corporation to have projects during the course of the year to offset inflation and may be even be able to provide enhanced bottom-line returns as well.

We had over 1,500 such projects during the past year, and these projects drive cost controls, they allow us to better utilize our raw materials. They can create yield improvements and they can allow us to better utilize our capacity.

An example of the enhanced returns within two of our most vertical oriented units are seen in Refrigerated Foods and Jennie-O Turkey Store, as over the past 5 years, Refrigerated Foods has enhanced their overall operating income percentage by 250 basis points, and at Jennie-O Turkey Store, that's at about a 590 basis point increase.

One other way to see the leveraging of efficiency is the growth versus the kind of the overhead within the company or the corporate team. So we've grown the top-line in the past five years at an aggregate 28%, but our corporate staff team during that same timeframe grew at 14%, so a 50% leverage opportunity there. Or if you look at overall sales, the CAGR at 5.11% versus SG&A without advertising at 3.95%, again, about a 20% leverage point of versus – our sales versus that total cost picture.

One last aspect of the kind of, sort of the secret behind Hormel Foods that I'd like to share with you really relates to our team. We are – I mentioned to you, we're in a small town in Minnesota, we're a little bit of a throwback in that regard. When someone joins our organization, they tend to join it for life, and indeed, our average tenure of our officer team at Hormel Foods is 26 years. That's not 26 years of industry experience, that's 26 years of experience at Hormel, which I think does make us somewhat unique in the industry.

We had our chance of – I saw the earlier presentation from General Mills and they're celebrating their 150th anniversary, which is fantastic. Hormel Foods is celebrating our 125th anniversary this year. And in anticipation of that event, I had a little gathering here recently with my two predecessors in the CEO, President roles at Hormel Foods, Joel Johnson and Dick Knowlton. We were taping some things for that 125th anniversary celebration. And then we kind of had a little breakfast session and – for some of our favorite SPAM recipes and had a chance to share some of the things we thought have made the company strong over the last few years. And I want to share a couple of minutes of that, a video with you right now.

[Video Presentation] (24:24-25:38)

So between Dick, Joel and I, we've been President of the organization for the past 35 years, and it's been our privilege to do that. But this last October, we had an exciting announcement, was the announcement of just the 10th President in our company's 125-year history, Jim Snee, and let me tell you a couple things about Jim. So this may be the first time for many of you to be introduced to Jim. Jim also has 26 years of Hormel Foods, so he hits the average on the nose, so we don't have to change that slide with him moving into this. He came up through our organization from the foodservice sales and marketing piece. He ran three different regions for our foodservice team. Jim was then asked to head up our corporate-wide purchasing function. After that, he was the inaugural Vice President of our Affiliated Foods group within Refrigerated Foods, running FARMER JOHN, Burke, and Dan's Prize. And then for the past 4.5 years, he led the International team. And during his tenure, his team grew segment profit for International from \$26 million to \$88 million.

So without further adieu, I'm going to bring Jim up to the podium, and he's going to share with you many of the exciting initiatives we have going forward.

James P. Snee

President, Chief Operating Officer & Director

Thank you, Jeff. First, since this presentation is doubling as our first quarter earnings call, I'd like to take this opportunity to update all of you on our outlook for the rest of 2016.

And during our fourth quarter conference call, we set our 2016 earnings per share guidance at \$1.43 to \$1.48 per share. And those numbers are adjusted for the recent stock split. Now, while sales growth will continue to be challenged as we navigate lower pork markets and the reduced Turkey volumes at Jennie-O, especially through the first half of the year, we do expect our earnings to continue to be favorable. And our strong earnings performance in the first quarter led by Refrigerated Foods, Grocery Products, Specialty Foods, as well as improvement in our Jennie-O Turkey segment as we recover from the Turkey supply pressures, has given us the confidence to raise our guidance for the full year to \$1.50 to \$1.56 per share. And that represents a 14% to 18% increase over 2015.

Now, while the Jennie-O Turkey Store business is still recovering from the impact of avian influenza last year, production volumes are expected to return to more normalized volumes by the end of the second quarter. And that will position them for strong growth in the back half of the year. Now, the expectation for normalized production volumes does assume that we do not have any new outbreaks of avian influenza in our operations, which are located in Minnesota and Wisconsin.

We look for continued favorable input costs for our Grocery Products and Refrigerated Foods segments. Refrigerated Foods will also benefit from strong pork operating margins. However, we do expect those pork operating margins to moderate as the year progresses.

Specialty Foods should continue to benefit from an improved mix of higher value-added items as our MUSCLE MILK franchise grows and we shift away from some lower margin business in other parts of that segment. That team has done a nice job capitalizing on operational efficiencies between our existing Century Foods business, but also our recently acquired CytoSport business. And we expect Specialty Foods to continue to benefit from those efforts.

And we do expect our International segment to be able to deliver improved results as the year progresses with improved export sales of both SPAM and SKIPPY. Now in terms of total company performance, one of the reasons we're able to consistently set and hit our aggressive long-term growth goals is the balance that's built into our

business segments. And when you put it all together, our business model supports growth that exceeds the average for packaged food companies, but is also inherently less volatile than our protein peers.

Now in the first quarter, you've heard it several times, we certainly are pleased to post another record in terms of earnings, which grew at a significant double digit rate with four of our five segments delivering earnings growth, really demonstrating our balanced model. But the long-term success of this model really is borne out over time as we've delivered year-over-year earnings growth in 27 years of the past 30 years.

And as financial consistency is not only due to the diversity across the business segments, but also the balance built throughout our business model. And so, we have product offerings that are both protein-centric, but also packaged foods, and that has really served as well over time. And the deep investments that we've made in both our pork and turkey supply chains allow us to better control the quality and consistency of our products, and remove cost from our system. Now this is balanced by our position of buying other key inputs such as peanuts, avocados and tomatoes on the outside. And that reduces our exposure to potentially volatile growing cycles, but it also minimizes our capital investment.

And we have a very strong presence in both the retail and foodservice channels, which allows us to serve consumers with meal solutions both at home and away from home. And both our retail and foodservice businesses are strengthened by our dedicated sales force that concentrates exclusively on our family of brands. We have a strong sense of financial conservatism that serves the company well, and as you saw earlier from Jody, we certainly have a strong balance sheet that gives us great flexibility.

Now, this conservative nature is complemented by our relentless pursuit of innovation that's allowed us to maintain relevancy with consumers. And it drives our success in both process and product improvements. So, this right balance allows us to prosper in various commodity cycles, and our diversified portfolio helps insulate the business in various market conditions.

And we have purposely prioritized our investments to expand the growth platforms that we think positioned our company for long-term growth while complementing our existing portfolio of very strong brands, ultimately creating a platform of foods that fit the many consumer needs.

Now, even with the faster growth that we've seen in our International business over the last several years, we acknowledge that our business is still primarily a U.S.-based business. But we continue to seek opportunities to expand our global footprint. We also view multicultural items with new and adventurous flavors such as those items that you'd find in our MegaMex portfolio of items, as a strong growth platform. We believe there are more opportunities to expand our multicultural food offerings going forward.

Additionally, our innovation and acquisition efforts have been focused on delivering foods that fit today's busy, on-the-go lifestyles, and the growing interest in products that are not only nutritious, but have significant holistic attributes. So now, let's take a deeper look at each of these platforms.

Our International business has achieved significant top line growth over the last five years. We've seen a 15% compound annual sales growth rate. And this segment is built on some longstanding partnerships that we have with Purefoods in the Philippines, CJ in South Korea, as well as a very well-developed export business with iconic brands like SPAM and SKIPPY.

And in China, we've developed businesses in both foodservice and retail channels, leading to our decision to expand production capacity in that country. We broke ground this past April on our new production facility in Jiaxing, China that will be completed by the end of calendar 2016. This facility will not only produce refrigerated

and frozen meat items, but it will include in-country SPAM production, allowing us to manufacture SPAM family of products in-country for the first time in our history. And this significant investment will give us much needed capacity, and allow us to meet the growing demands for our products in China from both consumers and foodservice operators.

Now while we're pleased with the great work that our team has done to deliver this organic growth, we continue to seek opportunities to increase our global exposure in a more meaningful way.

And I want to spend some time this morning talking about some specific brands in our portfolio that support our growth platforms, and the efforts made by our team to deliver innovation to meet the needs of today's consumers with food that fit their lifestyles.

As Jeff mentioned earlier, we have had and will continue to have aggressive expectations to grow our business at a rate of 5% on the top line and 10% on the bottom line. The brands I'll be highlighting today are going to be key drivers to support this aggressive growth trajectory.

So, the Jennie-O brand has become a clear market leader through our teams' efforts to build awareness. Their innovation and marketing efforts have led to 15 different items that hold the number one or number two market share position in their respective categories. And their Make The Switch advertising campaign, highlighting turkey's versatility as an alternative to beef, has been a huge success for their brand, driving both awareness and trial. Consumer awareness for Jennie-O brand now exceeds 95%, and it's driving purchase intent and share growth as consumers continue to look for fresh, nutritious meal solutions, using Jennie-O Turkey products.

In addition to the growing demand for these Jennie-O Turkey products, we believe our fresh supply chain focused on ground turkey is the best in the industry. And these efforts show up at the retailer as Jennie-O's share of the ground meats business has shown fantastic growth over the last five years. We hold the number two item in the retail exactly meat category, the only turkey item in the top 10. We've worked hard to achieve that success, and we have great retailer support as they recognize the importance of these types of items and their growing demand from consumers. The healthy attributes of the Jennie-O Turkey product portfolio, our brand leadership, and our rapidly growing share of the ground meats category position the Jennie-O Turkey segment to be a strong growth driver for our business for many years to come.

Now WHOLLY GUACAMOLE is part of our MegaMex portfolio of brands. And it's another brand that meets the growing demand from consumers for fresh, natural, fun, organic products. This cool on-trend brand holds a 42% market share in the refrigerated guacamole category. And much of that growth has been built through digital media campaigns in conjunction with a strong social media presence, and aligns well with our targeted growth areas with its healthy and holistic attributes.

And of course, it has multi-cultural appeal. And from an innovation perspective, our introduction of WHOLLY GUACAMOLE minis has been a huge success as it's made this great product easy for consumers to take on the go and have anytime, anywhere they want.

And when we acquired the SKIPPY brand in 2013, we knew there were immediate opportunities to capitalize on the brand's existing recognition among consumers. We were able to make early distribution and share gains commensurate with the SKIPPY brand position. We also knew that we could grow the brand by going back to the basics with a commitment to advertising and innovation. And when we looked at innovation, we were not only looking for closed ideas, but we wanted to bring to consumers the great flavor of SKIPPY beyond the jar. And we were able to do that with the introduction of SKIPPY P.B. Bites. It's a terrific combination of SKIPPY peanut

butter with a pretzel or peanut butter center for a delicious, protein-infused snack that's perfect for on the go and anywhere snacking.

Our SKIPPY peanut butter also enjoys the leading peanut butter brand from a natural perspective, allowing us to provide more choices for consumers. And while the team has done a lot of great work since the time of acquisition, we believe that there are so many opportunities to grow and innovate with this iconic brand.

And our Specialty Foods team is capitalizing on the 2014 acquisition of the MUSCLE MILK brand. MUSCLE MILK holds the number one market share position in the ready to drink protein beverage category. They've also been able to reinvigorate the brand's innovation efforts, introducing new items like MUSCLE MILK Pro Series and MUSCLE MILK organic products. With innovation even more critical in this fast-growing protein category, our team has developed a robust pipeline of exciting innovation that we'll be sharing with you in the months to come.

And we've also been able to leverage our team's capabilities to significantly expand distribution of MUSCLE MILK products with traditional retailers. And we expect our MUSCLE MILK franchise to continue to grow this premium protein category well into the future.

We got a peek at the Applegate brand earlier, but I can tell you that we are so very excited about the addition of this great Applegate business to our portfolio of strong brands. Applegate is the number one brand in the natural and organic value-added protein category.

And the acquisition was perfectly aligned with our interest in adding brands that resonate with consumers that are younger and more socially engaged. This acquisition has also expanded our distribution into the natural and Specialty Foods channel that's provided us a faster path to creating a significant presence in this high growth attractive margin segment. It also affords consumers more choice, providing access to foods that fit the demand for more holistic products.

Now, as we anticipated and we communicated when we announced the acquisition, our team continues to work on securing supply to meet the high demand for some of our Applegate products. The team continues to deliver nice growth with chicken-based products such as our Applegate Natural Breakfast Sausage and Applegate Organic and Natural Breaded Chicken.

I believe Jody said it earlier, if not, I'll say it for the first time that I'm pleased to share with you that our Applegate business continues to perform in line with our expectations. And so our approach of supporting our core items, driving innovation, and strategically investing in acquisitions has allowed us to create a product portfolio that resonates with consumers of all ages, foods that fit many different lifestyles.

So, many of our core brands have been well-represented in shopping carts for years. Our efforts on new product innovation and acquisitions have been focused on keeping our products relevant with changing consumer needs and trends, brands such as WHOLLY GUACAMOLE, Natural Choice, Applegate, MUSCLE MILK and Jennie-O have broad appeal with millennials and a younger, more socially engaged consumer. This broad and balanced portfolio of brands is another key to our long-term sustained growth.

And these are strong brands. We have 30 – we have over 30 brands that hold the number one or number two market share in their respective categories, helped in no small part by our dedicated sales team's efforts to communicate the power of our brands and their value proposition in both the retail and foodservice channels. Many of these brands are familiar to consumers for generations. They've grown and strengthened over time, and we strive to keep them as relevant with today's consumer as when they were first introduced. And we remain committed to supporting these brands and strengthening these brands, and advertising is an important

component. We expect a double-digit increase in our advertising spend this year on the heels of a similar sized increase last year.

Now, I'd like to show you an example of some of our most recent investments, which represents a nice mix of both traditional and digital media.

[Video Presentation] (45:56-50:07)

We certainly have some creative individuals working across the company on these ideas. Jeff shared with you earlier a slide sharing some of the great household penetration gains that we've made over the last five years. And while – yes, we have made a lot of gains, another reason we're optimistic about our ability to continue deliver strong growth is that many of the products still have a long runway ahead of them.

I spoke earlier about the growth in Jennie-O ground turkey products, and they're only scratching the surface with a household penetration rate of 9%. Items such as Applegate sliced meats, HORMEL NATURAL CHOICE deli meats, WHOLLY GUACAMOLE, still all in the single-digits with great consumer demand for these types of items.

And even our iconic brands, such as SPAM, HORMEL pepperoni and SKIPPY peanut butter have significant runway growth ahead of them. And Jody mentioned our CapEx plans earlier for fiscal 2016 of approximately \$250 million. Now some key items in that plan are the China plant that I mentioned earlier, as well as some production capacity expansion for select bacon items, including HORMEL BACON 1 Fully Cooked Bacon, which is an item that is developed for our food service group. Bacon continues to be on trend and it's been a great growth vehicle for us.

We're also expanding production capacity for Jennie-O ground turkey products. Now this was a project that we had scheduled last year, but we put it on hold with the outbreak of avian influenza, so we're just refreshing it this year.

And then, not all projects are about production capacity or plant efficiencies. And to keep pace with our innovation efforts, new technology and to maintain our laser-like focus on food, quality and safety, we're making a significant investment in our research and development facility, which will be online at the end of this fiscal year.

And so our efforts to innovate and keep our products relevant with consumers have delivered strong financial results. And clearly, we've been rewarded for those results in the marketplace. We've enjoyed stock performance that exceeds the S&P 500 and an index of our food peers. In fact, an investment at the end of our fiscal year 2010 would have tripled by the end of our fiscal year 2015.

And while we're pleased with this stock performance, our team understands that we must remain focused on those things that we can control. We will continue to concentrate on building our branded value-added portfolios and making the right investments today that will drive sustainable growth in our business over the long term.

So, thank you for your attention this morning. We're now prepared to take your questions and I do want to introduce Jana Haynes, who's our Director of Investor Relations.

QUESTION AND ANSWER SECTION

Jana L. Haynes

Director-Investor Relations

A

I see Akshay has his hand up there. Go ahead, Akshay.

A

[ph] Step away from the mike, mike one (53:18).

Akshay Jagdale

Jefferies LLC

Q

Akshay Jagdale, Jefferies. Thanks for taking the question. So, congratulations on another great quarter. Can you talk a little bit about M&A? Obviously, your returns have been above and beyond any of your peers, but your balance sheet's still under-levered, you mentioned \$3 billion in dry powder. The last three deals on average have added, I think, 4% to your earnings growth on average. What do you expect M&A to add to your growth algorithm going forward?

Jeffrey M. Ettinger

Chairman & Chief Executive Officer

A

We talk about 5% and 10%, but we've – that's inclusive of M&A. I think over maybe a 10-year timeframe, the M&A has been more like 1% to 1.5% of the 5%. Over the last five years, it's been a little bit more robust as we have done some bigger deals. We clearly have the financial wherewithal to tackle more acquisitions. We've talked in the past, but I mean, if you look at even the recent ones, I mean some are corporate properties, so SKIPPY came from a corporation, Lloyd's – from time-to-time, companies are changing their portfolio, most certainly we look at items within those portfolios that makes sense to Hormel.

But a number of our more successful acquisitions have been family-owned businesses that frankly we've tried to establish a relationship over many years with the hope that at some point, if that family has made the decision to sell the business, that we might be a preferred buyer.

We certainly have a number of hooks in the water and keep looking for things. We know we can handle it financially. We also know we can handle it in terms of the capacity of our company to integrate and handle more businesses.

Jana L. Haynes

Director-Investor Relations

A

And I think importantly is the disciplined model that we put around when we are looking at whatever our investments are and taking a long-term view because we do buy things that we intend to keep for the next 125 years.

James P. Snee

President, Chief Operating Officer & Director

A

And I would add that we'd probably keep them tied to those growth platforms I discussed. So, when we think about global, multi-cultural, healthy, holistic and on-the-go, those are going to be key drivers for us as we go on in the future. It doesn't mean that we wouldn't look at a business that perhaps adds scale to an existing portfolio that we have, but really we want to focus on those growth platforms in the years ahead.

Go ahead [indiscernible] (55:39).

Jana L. Haynes
Director-Investor Relations

A

Farha here.

Farha Aslam
Stephens, Inc.

Q

Results today really highlighted the success of your allocating raw material to the highest opportunity, particularly your Jennie-O Turkey Store had volumes that were down kind of 20% plus, but your earnings were nearly flat. So, kind of as you look forward, what more opportunity do you see in both turkey and pork going forward?

James P. Snee
President, Chief Operating Officer & Director

A

Yeah. I think from a turkey perspective, clearly, it's exactly what you said, I mean, the team has done a great job allocating those raw materials. But as we get into the back half of the year, we will see a return to more normalized returns. We need to make sure that we've got our business, our distribution back to where it was pre-avian influenza because there was some rationalization that had to take place. And so, we've got the great fundamentals of the Jennie-O Turkey Store business and now if we can go back and put the supply on top of that, we think that we're going to be well positioned for future growth.

On the pork side, again, it's a pork operating margins could have an impact in the back half of the year, but when you look across Refrigerated Foods in total, we're talking about meat products, foodservice, a number of different businesses that all – they don't all have the same direct impact. So, we expect to be fine on the pork side.

Jana L. Haynes
Director-Investor Relations

A

[indiscernible] (57:12) Rob Moskow.

Robert Moskow
Credit Suisse Securities (USA) LLC (Broker)

Q

Thanks. Also I thought what helped the quarter was – were bacon margins, deli prices were way down and bacon at retail seemed really high. Was that a big driver of Refrigerated margin in the quarter and is that also sustainable given the volatility in deli prices historically?

James P. Snee
President, Chief Operating Officer & Director

A

That was – that was a piece of it. I mean, clearly because if you look at the portfolio of items that we have available, whether it's Hormel pepperoni, bacon, certainly the Refrigerated Foods or the items in our Foodservice group also has a bacon component to it as well. And so, our team does do a good job of staying current on pricing as that does – there is some volatility and fluctuation.

So I mean, I think the margin management piece of it, the discipline, our team does a pretty nice job and I would expect that we would keep that going forward.

Robert Moskow

Credit Suisse Securities (USA) LLC (Broker)

Q

As to follow-up, in turkey, is the industry going to come out of this AI event in a stronger position than it was before because maybe some excess capacity came out? I mean, your pricing is up at a time when all other proteins are down. Can you explain how turkey pricing kind of fits into all that?

Jeffrey M. Ettinger

Chairman & Chief Executive Officer

A

Yeah, I – I think turkey is kind of unique in the sense that it is the niche protein, even as great a job as our Jennie-O brand has done in proliferating the brand in the marketplace and adding new value-added items, I mean, it's not the lead item that the retailers are going to feature in their ads except for Thanksgiving.

So, I think the pricing model for us is really fairly consistent one; as long as we build innovative items with true points of difference, we can attain a good margin with those and we clearly want to support that with the advertising position.

Hard to tell from a macro standpoint, I mean, this year, that the whole industry is obviously going to be closely watching this spring to see if there are any further outbreaks, you're seeing cold storage stocks go up a little bit already. I think that frankly folks are holding on to any surplus breast meat or other items they have in anticipation of a potential challenge.

We didn't see any recurrence within our region in the fall, there was a recent incident in Indiana, but it was a fairly limited one, of a different strain – so I think the AI dynamic is going to continue to affect the marketplace at least through the spring and then if turns out, we have a clean spring and we are kind of out of that mode, then things could change by next year.

Jana L. Haynes

Director-Investor Relations

A

[ph] Mario Contreras next (59:42).

Mario Contreras

Deutsche Bank Securities, Inc.

Q

Mario Contreras, Deutsche Bank. So, I wanted to ask you about your long-term targets, 5% sales, 10% earnings growth, it's obviously implying a decent amount of margin expansion over time, but if we look at your specific segment margin ranges, you're already kind of at the high end or even above the high end in some cases. So can you talk a little bit about where you expect to see the end margin expansion come from over time?

Jody H. Feragen

Chief Financial Officer, Executive Vice President & Director

A

Well, certainly. Excuse me. Certainly, we'll look to some of that leveraging on that corporate and G&A side of things like Jeff talked about. But really it's about focusing on what the consumers are looking for and trying to find the value-added products that fit within the growth platforms that we've put out there.

Some will come from one of the things that we – criteria we look for, when we are looking at M&A transactions or even those internal investments are – we expect the margin profile, over those investments over the long-term, be accretive to the segment that they're in. So, lots of different things working towards those goals.

Jeffrey M. Ettinger
Chairman & Chief Executive Officer

A

As Jon mentioned at the introduction, we certainly have endeavored to shift the portfolio to become more and more of a prepared foods player, but our aggregate margins are still well below the average of that universe. So, we think over time and we will certainly move the segment margins as we see a logic behind that. We think over time, the total company margins can definitely migrate northward.

Jonathan P. Feeney
Athlos Research

Well, thank you. I think that's all the time we have in the webcast. Just as a reminder, lunch is immediately after this and I believe the Hormel management team will be available for your questions. Let's take this opportunity to thank Hormel once again for what's sure to be a great lunch for their support of CAGNY and a great presentation. Thank you.

Jeffrey M. Ettinger
Chairman & Chief Executive Officer

Nice job.

Jana L. Haynes
Director-Investor Relations

Nice job.

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