

Pilgrim's Pride Corporation

NasdaqGS:PPC

Analyst: Etienne Lehideux

Sector: Consumer Goods

BUY

Target Price: \$40

Key Statistics as of 3/4/2014

Market Price:	\$28.03
Industry:	Food – Major Diversified
Market Cap:	\$7,340 M
52-Week Range:	\$38.64 - 17.18
Beta:	0.12

Thesis Points:

- Favorable industry outlook
- Strong Management and efficient strategy
- Diversified product portfolio that resists industry's peaks and troughs
- Excessively low valuation

Company Description:

Pilgrim's Pride Corporation engages in the production, processing, marketing, and distribution of fresh, frozen, and value-added chicken products to retailers, distributors, and foodservice operators in the United States, Mexico, and Puerto Rico. It offers fresh chicken products comprising pre-marinated or non-marinated, and prepackaged refrigerated (nonfrozen) whole or cut-up chicken in various combinations of refrigerated whole chickens and chicken parts. The company also provides prepared chicken products, such as portion-controlled breast fillets, tenderloins and strips, delicatessen products, salads, formed nuggets and patties, and bone-in chicken parts. In addition, it exports whole chickens and chicken parts to approximately 95 countries. Pilgrim's Pride Corporation sells its products to foodservice market, including chain restaurants, food processors, broad-line distributors, and other institutions; and retail market customers that primarily include grocery store chains, wholesale clubs, and other retail distributors. The company was founded in 1946 and is headquartered in Greeley, Colorado. As of December 28, 2014, Pilgrim's Pride Corporation operates as a subsidiary of JBS USA Holdings, Inc.

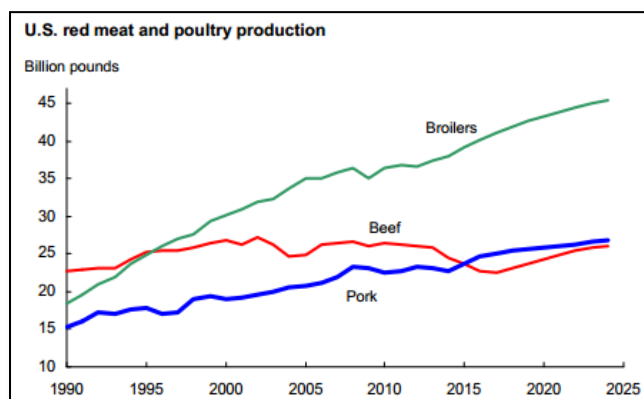


Thesis

Pilgrim's Pride Corporation is the second largest producer of chicken products in the U.S. The company was saved from bankruptcy in 2011 by JBS S.A., the largest food processing company in the world. Since then, a new management took over the company and the strategy they have been applying is very successful so far. Margins are improving at all levels, their market share is growing, and the company seeks overseas expansion through acquisitions and product portfolio diversification. The favorable industry outlook, as well as the increase in chicken products' price and production, position Pilgrim's Pride Corporation on track to become the top company in the industry. Moreover, the debt-free company rewards its shareholders with the strong cash flows it generates. Finally, the recent short interest spike scared away many investors, who left the stock undervalued. PPC is currently trading at 9.88x earnings while its main competitor, Tyson Foods, trades at 17.59x earnings.

Industry Overview

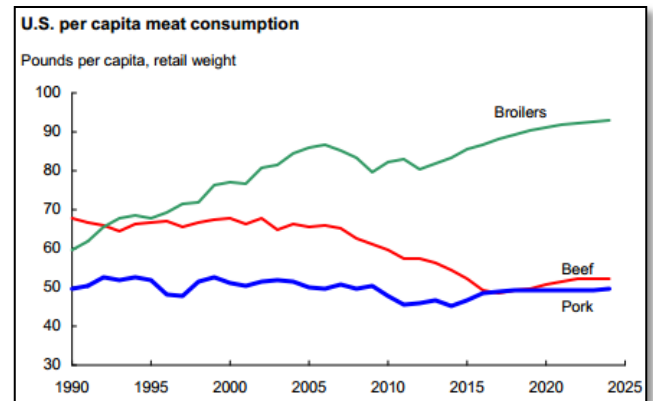
The U.S. is the world's largest producer of chicken and is projected to produce approximately 39.2 billion pounds of ready-to-cook broiler meat in calendar year 2015, representing 20.3% of the total world production. Brazil and China produce the second and third most broiler meat, with 15.0% and 14.9% of the world market, respectively, according to the USDA. Based on their long term projections, poultry production in the U.S. should expand faster than beef and pork until 2025. USDA affirms that production growth is expected to come from both higher numbers of birds and higher average weights at slaughter.



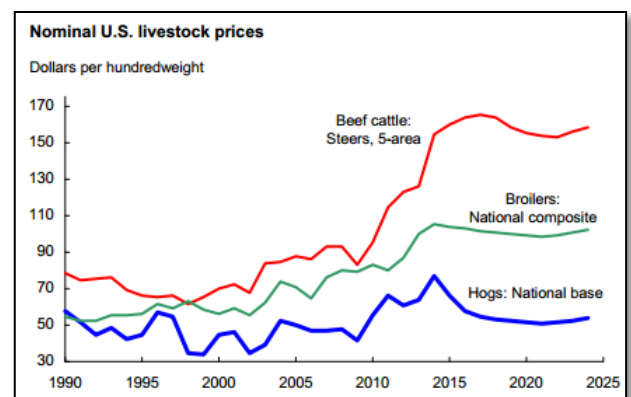
The chicken industry in the U.S. is vertically integrated, with main producers operating feed mills and processing

plants while contracting out breeding and broiler production to independent farmers.

Poultry consumption in the U.S. is expected to increase faster than other meats. In 2014, Pricedynamics reported that American ate more chicken than beef for the first time. These trends can be explained by American becoming more health conscious but also by the increasing price of beef. Poultry is also a cheaper protein substitute.



Prices of poultry reached a peak in the end of 2014, and analysts do not expect them to rise much further. The graph below shows that poultry prices are expected to remain stable compared to beef and hogs.



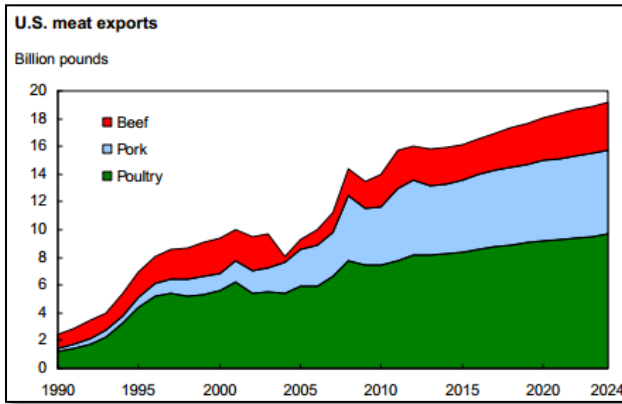
The table below provides updated production and prices data. The increased number of chicks placed for grow out anticipates for increased slaughters in the coming months.

Selected broiler market indicators				
Production		December 2013	December 2014	% Change
Monthly Chicks placed for growout		774,784	795,735	2.7%
Number of birds slaughtered		687,163	728,227	6.0%
Average live-weight (lbs)		5.99	6.10	1.8%
Stocks at end of month		668,673	680,262	1.7%
Prices		January 2014	January 2015	% Change
National Composite Weighted Average, wholesale price (US\$/lb)		\$0.97	\$1.00	2.9%
Boneless/skinless breast meat (Northeast price, US\$/lb)		\$1.26	\$1.35	7.4%
Leg quarters (Northeast price, US\$/lb)		\$0.42	\$0.42	-2.1%

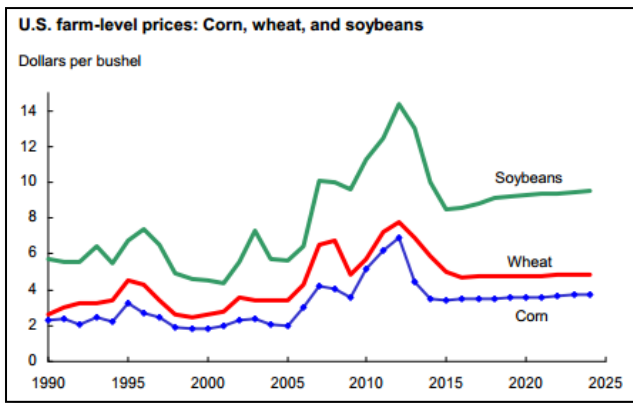
Source: USDA, National Agricultural Statistical Service and Agricultural Marketing Service.

Finally, USDA projects U.S. broiler exports to rise

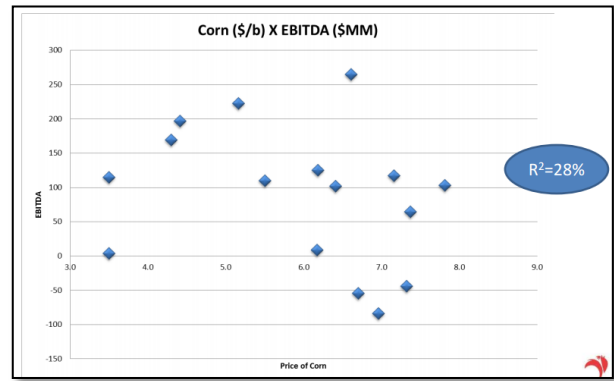
through 2025. The main export markets are China, Mexico, and other countries which economic growth will support the demand for poultry products. Brazil is the third largest producer of broiler and the main competitor on the export side.



All in all, the outlook for chicken production and consumption is fairly positive. Also, the recent drop in corn and soybeans prices allowed poultry producers to decrease their feeding costs and increase their margins. Although USDA projects grains prices to stabilize in the coming years, a surge in price could negatively impact the industry’s margins; therefore the trend has to be carefully monitored. Although, investors should be confident with the stable outlook for the near future, as yields and stocks for both the US and South America were recently at near record highs.

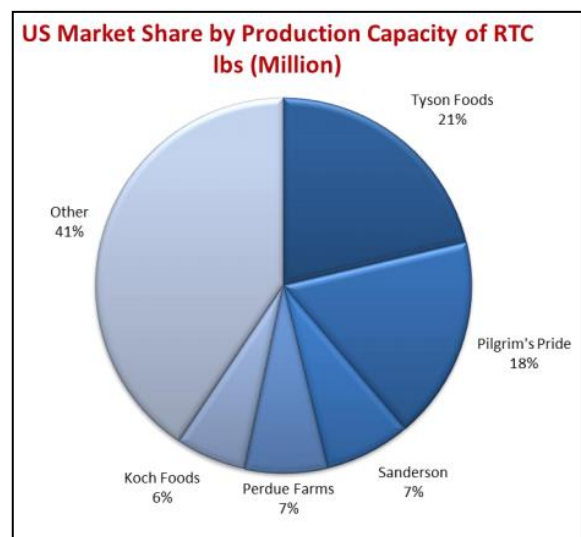


It should be noted that certain investors believe the earnings of companies similar to PPC are linked to corn prices, because of their direct impact on feed costs. Such reasoning is dubious as PPC hedges against commodities’ price fluctuations by investing in futures contracts. The chart below shows that there is no correlation between PPC’s EBITDA and corn prices.



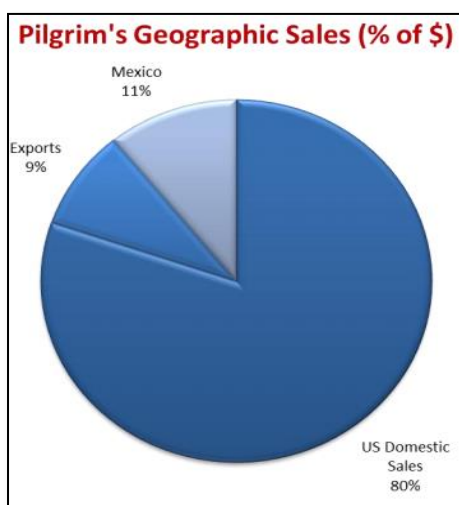
Competitive advantages

Pilgrim’s Pride Corp. is the second largest chicken company in the world. According to the company’s latest 10-K filing, PPC’s main competitive advantage are its leading market position (18% of the U.S. market share) in a growing industry, a broad product portfolio, its Blue Chip and diverse customer base across all industry segments, the efficiency and synergy brought by being a subsidiary of JBS USA, robust cash flow generation with disciplined capital allocation, and an experienced management team and results oriented corporate culture.



PPC’s main competitor is Tyson Foods, Inc., which owns 21% of the U.S. chicken market share. The company is increasing its branded product portfolio, notably with the acquisition in 2014 of Hillshire Brands Co., owner of Jimmy Dean sausages and Ball Park hot dogs. Tyson recently closed three plants in the U.S. in an effort to reduce costs. It is important to note that Tyson’s relationship with Wal-Mart Stores, Inc. accounted for 14.6% of their fiscal 2014 consolidated sales. Therefore, any extended discontinuance of sales to this customer could have a material impact on their operations.

PPC has operations in Mexico, where it is the third largest producer and owns a 10% market share. There, the company owns 3 poultry complexes and 7 sales offices, employs 5,400 persons working on all segments from live chicken to fully cooked products, and owns the Del Dia brands. Their expansion in Mexico has been strong thanks to the strategic acquisition of Tyson's local poultry business in 2014. This acquisition allows PPC to have presence in Northern Mexico, which provides the company with geographic diversity. Also, Tyson agreed to sell its Brazilian poultry business to PPC, a transaction that will occur during the first quarter of fiscal 2015.



PPC has relationships with very powerful companies in different consumer segments, that include Chick-fil-A, Sysco, US Foods, Yum! Brands, Kroger, Wal-Mart, Costco, Publix, Sam's Club and ConAgra Foods. It sells its products to a large and diverse customer base, with over 5,000 customers and no single one accounting for more than 10% of total sales.



Finally, PPC is a majority-owned subsidiary of JBS USA, an indirect subsidiary of Brazil-based JBS S.A., which beneficially owns approximately 75.5% of PPC's outstanding common stock. As such, the company works closely with JBS USA's management to identify areas where both companies can achieve synergies. As part of the integration plan, PPC moved its headquarters

to Greeley, Colorado, the headquarters of JBS USA. In addition to cost savings through the integration of certain corporate functions and the rationalization of facilities, the relationship with JBS USA allows PPC to enjoy several advantages given its diversified international operations and strong record in commodity risk management. PPC also leverages JBS USA's international network by expanding into untapped international markets and strengthening its presence in geographies in which it already operates. In addition, JBS USA's expertise in managing the risk associated with volatile commodity inputs helps PPC to improve its operations and strengthen its margins.

Products and Segments

Pilgrim's Pride Corp. produces and markets three types of chicken products.

The *fresh chicken products* are sold to the foodservice and retail markets. Fresh chicken products consist of refrigerated (non-frozen) whole or cut-up chicken, either pre-marinated or non-marinated and prepackaged case-ready chicken. Fresh chicken sales accounted for 66.2% of PPC's total U.S. chicken sales in 2014.

The company also sells *prepared chicken products*, including portion-controlled breast fillets, tenderloins and strips, delicatessen products, salads, formed nuggets and patties and bone-in chicken parts. These products are sold either refrigerated or frozen and may be fully cooked, partially cooked or raw. In addition, these products are breaded or non-breaded and either pre-marinated or non-marinated. Prepared chicken products sales accounted for 25.1% of PPC's total U.S. chicken sales in 2014.

Finally, *value-added export and other chicken products* primarily consist of whole chickens and chicken parts sold either refrigerated for distributors in the U.S. or frozen for distribution to export markets. PPC sells U.S.-produced chicken products for export to Mexico, the Middle East, Asia, countries within the Commonwealth of Independent States (the "CIS") and other world markets. Value-added export and other chicken products sales accounted for 8.7% of PPC's total U.S. chicken sales in 2014.

Management & Strategy

Pilgrim's Pride Corp. has a proven senior management team with long time experience in the chicken industry.

Mr. William W. Lovette, (Bill) has been the Chief Executive Officer and President of Pilgrim's Pride Corporation since January 3, 2011. Mr. Lovette served as the President and Chief Operating Officer of Case Foods, Inc. from October 2008 to December 2010. He has more than 29 years of industry leadership experience. He spent 25 years with Tyson Foods in various roles in senior management, including President of its International Business Unit.

The CEO's main focus since he took office in 2011 is to make PPC the top operator in the poultry industry. First, he applies a portfolio diversification strategy that enables the company not to follow the full peaks and troughs of the broader industry pricing trends. The company's diversified sales mix ensures they can adapt quickly to the market supply and mitigate volatility. For example, high spot prices for parts such as boneless skinless breasts and wings benefit their large bird deboning business. When these prices decline, other businesses such as prepared foods benefit from the change. In the Q3 earnings call transcript, the CEO says he thinks PPC is the only company in the industry to achieve such positioning. The executive also insists that he is far from having reached his goal. Management's focus is currently on strengthening customers' relationships, exiting unprofitable business, diversifying customer base and maximizing product mix.

Mr. Fabio Sandri has been the Chief Financial Officer of Pilgrim's Pride Corporation since June 3, 2011 and serves as its Principal Accounting Officer. He has several other experiences as CFO at other companies and holds an MBA from Wharton school at University of Pennsylvania.

His focus has been to reduce the company's SG&A expenses trying to reach "operational excellence", which he managed to reach with 2.2% of revenues in Q4 2014. His current concern is to manage the impressive growth in free cash flow the company is generating. His goal is to increase his plans for capital projects throughout 2015, while continuing to focus on opportunities with a rapid return on investment and projects that increase the

company's efficiency, quality, and safety. The company announced earlier this year a special dividend of \$5.77 per share outstanding. The CFO mentioned a capital restructuring in Q3 2014 earnings call, which should increase shareholders value should it take the form of a share buyback.

Overall, the management is implementing a strategy, originally thought of back in 2011, which has proven to be very efficient. Improvements are being made on the product side, the customer base side, the operational side, and on the financial side. Should the strategy continue to benefit the company, it seems like the management knows how to build and grow valuable businesses.

Financials

As introduced earlier, the company took a sharp turn in 2011 when the new management took office. Revenues grew almost 14% since 2011 to reach \$8,583.4 in FY 2014. As a comparison, Tyson Foods' chicken segment only grew its sales by 10% over the same period. But the main improvement is on the operational side. Before the new management took office, PPC was filing for bankruptcy due to its debt load and bad management of feed prices. The table below shows great improvement at all levels of the income statement. Gross margins tripled to reach 16.2% during FY 2014. Operating margins grew to 14% in FY 2014, while Tyson Foods' chicken segment is lagging below 10%. Finally, the bottom line margin for Pilgrim's Pride Corp. is strong with 8% in FY 2014. As a comparison, Tyson Foods' overall net income margin was 2.3% during FY 2014.

	FY 2011	FY 2012	FY 2013	FY 2014
Pilgrim's Pride Corp.				
Revenues	\$ 7,535.7	\$ 8,121.4	\$ 8,411.1	\$ 8,583.4
Gross Margin	-1.90%	5.40%	10.10%	16.20%
Operating margin	-5%	3%	8%	14%
SG&A	2.7%	2.1%	2.1%	2.2%
Net Margin	-7%	2%	7%	8%
Tyson Foods' Chicken Segment				
Revenues	\$ 11,017.0	\$ 11,368.0	\$ 10,988.0	\$ 11,116.0
Operating margin	1%	4%	6%	8%

PPC is almost debt free, and has more than \$550 million in cash on hand. Its current ratio and quick ratio are very healthy, with 2.53 and 1.29 respectively. As the reimbursement of their debt is almost terminated, their D/E ratio as of end of FY 2014 is 0.19. The fact that the company recovered its financial stability in the past three years helped them gaining access to almost \$1 billion worth of credit facility, which will help with capital

expenditures, among others.

Finally, PPC's free cash flows are increasing at an impressive rate. The company's FCF in FY 2011, 2012, 2013 and 2014 were respectively (265), 109, 762, and 895 million dollars.

Valuation

It is important to notice the aggressive short interest on PPC's shares. The short interest ratio is currently 11.28%, and 69% of the float. The dividend paid in January 2015, coupled with the surge in short interest, scared many investors away and led the stock to trade in the \$25-30 range, down from its \$36 levels.

There is noise among the analysts community that Steve Cohen-led hedge fund Point72 Asset Management, formerly SAC Capital, may be betting on a long/short play with Pilgrim's Pride Corp. and Tyson Foods. Indeed, the money management firm's latest 13-F filings (available [here](#)) show that during 2014, the company increased its position in Tyson Foods, Inc from \$92 Million to almost \$300 million. The table below shows a recap of Point72's position in TSN shares, and reveals that this position became the second largest long position in the company's portfolio:

Position in Tyson Foods	8/14/2014	11/14/2014	2/17/2015
Number of shares	2,447,600	7,422,400	5,176,100
Value	\$ 91,883,000	\$ 292,220,000	\$ 207,510,000
% of float	0.8%	2.5%	1.7%
% of long positions	0.59%	2.20%	1.46%
Position Size Ranking	#28	#2	#2

The theory is that with a huge bet on Tyson Foods, Point72 AM is betting on the company's product portfolio efficiency. Indeed, Tyson would be less impacted than PPC in a decrease in chicken prices, as the food giant also sells beef and pork. A decrease in currently record high chicken prices would more severely impact PPC, hence the Short PPC/Long Tyson play. Even if this theory revealed to be true, prices in chicken are expected to remain stable without suffering a big drop in price. Moreover, even if PPC is a chicken "pure player", its product mix is constituted such as that the company's sales are hedged against chicken prices fluctuations. It is important to note that there is no proof of the short

position, as the SEC does not require reporting them.

Investors who enter the position now could benefit from the short squeeze that will eventually happen. The whopping short interest on PPC may require these investors to hang on to their hats.

The image below shows trading multiples for PPC compared to its peers. It appears largely undervalued as the average discount based on the below multiples is 39%.

Name	Mkt Cap (USD)	NTM P/E	NTM EV/EBITDA	NTM EV/EBIT	NTM EV/Rev
2) PILGRIM'S PRIDE CORP	7.28B	9.4x	4.9x	5.7x	0.7x
Current Premium to Comps Mean		-43%	-44%	-52%	-17%
Mean (Including PPC US)	7.88B	16.6x	8.8x	12.0x	0.9x
Median	4.51B	16.9x	8.1x	12.4x	0.7x
Low	N.A.	8.6x	4.2x	5.3x	0.3x
High	29.86B	22.0x	12.5x	15.9x	1.5x

PPC's current P/E ratio is 9.88x, versus 26.13x for its peers and 17.6x for Tyson Foods. PPC's forward P/E shows investors are paying even cheaper for next year's earning, with 8.87x.

The next page of this report includes a screenshot of the valuation model for PPC. The assumptions used are very conservative. Even using negative growth for the next five year results in a 40% upside potential. Because of the high short interest, financial valuation is not taken into account in the current price of PPC.

As the saying goes, if you can't stand the heat, get out of the kitchen; meanwhile, more aggressive investors may want to look into this interesting play against the short sellers.

Sources:

10-K

Investor Presentations

Bloomberg

Capital IQ

US Department of Agriculture

SEC

CENTER FOR GLOBAL FINANCIAL STUDIES

Pilgrim's Pride Corporation		PPC	Analyst Etienne Lehideux	Current Price \$28.03	Intrinsic Value \$40.33	Target Value \$42.46	Divident Yield 0%	Target Return 51.48%	BULLISH
General Info			Peers		Market Cap.		Management		
Sector	Consumer Staples		Hormel Foods Corporation	\$15,277.82	Professional	Title	Comp. FY2012	Comp. FY2013	Comp. FY2014
Industry	Food Products		Sanderson Farms, Inc	\$1,941.52	Lovette, William	Chief Executive Officer, President, Director and Member of JBS Nominating	\$ 1,502,223.00	\$ 5,148,318.00	\$ -
Last Guidance	Feb-11-2015		Campbell Soup Company	\$14,510.91	Sandri, Fabio	Chief Financial Officer and Principal Accounting Officer	\$ 888,990.00	\$ 1,618,014.00	\$ -
Next earnings date	4/27/2015		Dean Foods Company	\$1,533.78	Penn, Jayson	Executive Vice President of Sales & Operations	\$ -	\$ -	\$ -
Market Data			Tyson Foods, Inc	\$16,839.73	Miner, James	Senior Vice President of Technical Services	\$ -	\$ -	\$ -
Enterprise value	\$6,710.40		The J. M. Smucker Company	\$11,625.36	Schult, Douglas	Head of Human Resources	\$ -	\$ -	\$ -
Market Capitalization	\$7,279.40				Snyder, William	Chief Restructuring Officer	\$ -	\$ -	\$ -
Daily volume	1.73		Historical Performance						
Shares outstanding	259.70		PPC						
Diluted shares outstanding	259.47		Peers						
% shares held by institutions	35.53%		Industry						
% shares held by insiders	0.15%		All U.S. firms						
Short interest	13.88%		Current Capital Structure						
Days to cover short interest	15.53		Total debt/market cap	0.06%	Growth	16.0%	3.8%	8.7%	6.0%
52-week high	\$38.64		Cost of Borrowing	18.94%	Retention Ratio	0.0%	42.9%	59.5%	61.6%
52-week low	\$17.73		Interest Coverage	1468.26%	ROIC		12.4%	13.5%	11.8%
5y Beta	0.88		Altman Z	9.05	EBITDA Margin	0.0%	6.7%	11.6%	13.7%
6-month volatility	64.46%		Debt Rating	BAA	Revenues/Invested capital	383.0%	223.3%	178.1%	202.3%
Past Earning Surprises			Levered Beta	0.73	Excess Cash/Revenue	#DIV/0!	3.3%	6.4%	18.5%
			WACC (based on market value weights)	6.82%	Unlevered Beta	0.76	0.50	0.64	0.95
					TEV/REV	0.4x	0.8x	1.5x	2.4x
					TEV/EBITDA	6.1x	9.3x	12.1x	11.3x
					TEV/EBITDA	8.8x	12.1x	15.3x	15.4x
					TEV/UFCF	7.9x	18.6x	28.3x	26.8x
					Non GAAP Adjustments				
					Operating Leases Capitalization	0%	N/A	N/A	N/A
					R&D Exp. Capitalization	100%	Straightline	10 years	10 years
					Expl./Drilling Exp. Capitalization	0%	N/A	N/A	N/A
					SG&A Capitalization	0%	N/A	N/A	N/A
					Forecasted Profitability				
					Revenue	NOPLAT	Invested capital	UFCF	
					\$8,583.37	\$917.63	\$1,718.90	\$917.63	
					\$8,669.44	\$508.80	\$1,701.23	\$526.43	
					\$8,756.13	\$489.51	\$1,701.45	\$489.28	
					\$8,843.70	\$538.26	\$1,709.89	\$529.82	
					\$8,932.13	\$536.45	\$1,721.71	\$524.64	
					\$9,021.45	\$594.41	\$1,734.46	\$581.66	
					\$9,111.67	\$598.08	\$1,746.91	\$585.63	
					\$9,202.78	\$659.91	\$1,758.96	\$647.86	
					\$9,294.81	\$665.43	\$1,770.20	\$654.19	
					\$9,387.76	\$729.44	\$1,780.24	\$719.40	
					Valuation				
					Enterprise Value	Total Debt	Other claims	Equity	Adjusted Price
					\$10,156.61	\$4.24	-\$496.39	\$10,648.76	\$41.29
					\$9,896.82	\$4.24	-\$1,155.77	\$11,048.34	\$43.21
					\$10,013.85	\$4.24	-\$1,817.00	\$11,826.61	\$46.19
					\$10,189.57	\$4.24	-\$2,576.36	\$12,761.69	\$49.79
					\$10,342.29	\$4.24	-\$3,351.35	\$13,689.41	\$53.45
					\$10,521.41	\$4.24	-\$4,235.19	\$14,752.37	\$57.69
					\$10,659.93	\$4.24	-\$5,142.13	\$15,797.82	\$61.64
					\$10,814.12	\$4.24	-\$6,166.66	\$16,976.54	\$66.17
					\$10,920.38	\$4.24	-\$7,221.22	\$18,137.36	\$70.73
					\$11,032.52	\$4.24	-\$8,402.35	\$19,430.63	\$74.82
					Monte Carlo Simulation Assumptions				
					Base	Stddev	Min	Max	Distribution
					0	10%	N/A	N/A	Normal
					0	10%	N/A	N/A	Normal
					6%	N/A	5%	7%	Triangular
					3%	N/A	3%	16%	Triangular
					0	0.1	N/A	N/A	Normal
					Monte Carlo Simulation Results				
					Intrinsic Value		1y-Target		
					Mean est.		\$41.29		\$43.21
					σ(e)		\$0.32		\$0.25
					3 σ(e) adjusted price		\$40.33		\$42.46
					Current Price		\$28.03		
					Analysts' median est.				\$32.00