

SMITHFIELD FOODS INC
Form 10-K
June 18, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the fiscal year ended May 2, 2010
Commission file number: 1-15321

SMITHFIELD FOODS, INC.
(Exact name of registrant as specified in its
charter)

Virginia		52-0845861
(State or other jurisdiction of incorporation or organization)		(I.R.S. Employer Identification No.)
200 Commerce Street		
Smithfield, Virginia	23430	
(Address of principal executive offices)		(Zip Code)
(757) 365-3000		
(Registrant's telephone number, including area code)		

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$.50 par value per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None

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Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of the shares of registrant's Common Stock held by non-affiliates as of November 1, 2009 was approximately \$1.5 billion. This figure was calculated by multiplying (i) the \$13.34 last sales price of registrant's Common Stock as reported on the New York Stock Exchange on the last business day of the registrant's most recently completed second fiscal quarter by (ii) the number of shares of registrant's Common Stock not held by any executive officer or director of the registrant or any person known to the registrant to own more than five percent of the outstanding Common Stock of the registrant. Such calculation does not constitute an admission or determination that any such executive officer, director or holder of more than five percent of the outstanding shares of Common Stock of the registrant is in fact an affiliate of the registrant.

At June 8, 2010, 166,013,232 shares of the registrant's Common Stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates certain information by reference from the registrant's definitive proxy statement to be filed with respect to its Annual Meeting of Shareholders to be held on September 1, 2010.

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PART I

ITEM 1. BUSINESS

GENERAL DEVELOPMENT OF BUSINESS

Smithfield Foods, Inc., together with its subsidiaries (the “Company,” “we,” “us” or “our”) began as a pork processing operation called The Smithfield Packing Company, founded in 1936 by Joseph W. Luter and his son, Joseph W. Luter, Jr. Through a series of acquisitions starting in 1981, we have become the largest pork processor and hog producer in the world.

We produce and market a wide variety of fresh meat and packaged meats products both domestically and internationally. We operate in a cyclical industry and our results are significantly affected by fluctuations in commodity prices for live hogs and grains. Additionally, some of the key factors influencing our business are customer preferences and demand for our products; our ability to maintain and grow relationships with customers; the introduction of new and innovative products to the marketplace; accessibility to international markets for our products including the effects of any trade barriers; and operating efficiencies of our facilities.

We conduct our operations through five reporting segments: Pork, International, Hog Production, Other and Corporate, each of which is comprised of a number of subsidiaries, joint ventures and other investments. The Pork segment consists mainly of our three wholly-owned U.S. fresh pork and packaged meats subsidiaries. The International segment is comprised mainly of our meat processing and distribution operations in Poland, Romania and the United Kingdom, as well as our interests in meat processing operations, mainly in Western Europe and Mexico. The Hog Production segment consists of our hog production operations located in the U.S., Poland and Romania as well as our interests in hog production operations in Mexico. The Other segment is comprised of our turkey production operations and our interest in Butterball, LLC (Butterball). Through the first quarter of fiscal 2010, this segment also included our live cattle operations. The Corporate segment provides management and administrative services to support our other segments.

Over the past few decades, we have completed numerous acquisitions. Recently, our overall focus has shifted from acquisitions to integration, driving operating efficiencies and growing our packaged meats business to fully leverage the benefits of our prior acquisitions. Additionally, we are currently focused on reducing our debt and eliminating non-core or under-performing businesses.

Fiscal 2010 Business Developments

The following business developments have occurred since the beginning of fiscal 2010:

Hog Production Cost Savings Initiative

In the fourth quarter of fiscal 2010, we announced a plan to improve the cost structure and profitability of our domestic hog production operations (the Cost Savings Initiative). The plan includes a number of undertakings designed to improve operating efficiencies and productivity. These consist of farm reconfigurations and conversions, termination of certain high cost, third-party hog grower contracts and breeding stock sourcing contracts, as well as a number of other cost reduction activities.

As a result of the Cost Savings Initiative, we recorded pre-tax charges totaling \$9.1 million in the fourth quarter of fiscal 2010, including impairment and accelerated depreciation charges of \$2.5 million and \$3.8 million, respectively, as well as contract termination costs of \$2.8 million. These charges were recorded in cost of sales in the Hog

Production segment.

Certain of the activities associated with the Cost Savings Initiative are expected to occur over a two to three-year period in order to allow for the successful transformation of farms while minimizing disruption of supply. We anticipate recording additional charges over this period in the range of \$30 million to \$35 million primarily associated with future contract terminations. We also anticipate capital expenditures totaling approximately \$86 million will be required in connection with the farm reconfigurations and other cost savings activities.

We do not believe the benefits of the Cost Savings Initiative will have any significant impact on our results of operations in fiscal 2011. Beginning in fiscal 2012, we expect a gradual improvement in profitability of our Hog Production segment. We expect that by fiscal 2014, the benefits of this initiative will be fully realized and we currently estimate profitability improvement of approximately \$2 per hundredweight.

Hog Farm Impairments

In fiscal 2008 and fiscal 2009, we announced that we would reduce the size of our U.S. sow herd by 10% in order to reduce the overall supply of hogs in the U.S. market.

In June 2009 (fiscal 2010), we decided to further reduce our domestic sow herd by 3%, or approximately 30,000 sows, which was accomplished by ceasing certain hog production operations and closing certain of our hog farms. In addition, in the first quarter of fiscal 2010, we began marketing certain other hog farms. As a result of these decisions, we recorded total impairment charges of \$34.1 million, including an allocation of goodwill, in the first quarter of fiscal 2010 to write-down the hog farm assets to their estimated fair values. The impairment charges were recorded in cost of sales in the Hog Production segment.

RMH Foods, LLC (RMH)

In October 2009 (fiscal 2010), we entered into an agreement to sell substantially all of the assets of RMH, a subsidiary within the Pork segment, for \$9.5 million, plus the assumption by the buyer of certain liabilities, subject to customary post-closing adjustments, including adjustments for differences in working capital at closing from agreed-upon targets. We recorded pre-tax charges totaling \$3.5 million, including \$0.5 million of goodwill impairment, in the Pork segment in the second quarter of fiscal 2010 to write-down the assets of RMH to their fair values. These charges were recorded in cost of sales. In December 2009 (fiscal 2010), we completed the sale of RMH for \$9.1 million, plus \$1.4 million of liabilities assumed by the buyer.

Farasia Corporation (Farasia)

In November 2009 (fiscal 2010), we completed the sale of our investment in Farasia, a 50/50 Chinese joint venture formed in 2001, for RMB 97.0 million (\$14.2 million at the time of the transaction). Farasia's wholly-owned subsidiary, Maverick Food Company Limited, focuses mainly on hot dogs and other sausages, whole and sliced ham, bacon, Chinese-style processed meat, and frozen and convenience food. We recorded, in selling, general and administrative expenses, a \$4.5 million pre-tax gain in the third quarter of fiscal 2010 on the sale of our investment in Farasia.

Premium Pet Health, LLC (PPH)

Prior to fiscal 2010, we held a 51% ownership interest in Premium Pet Health, LLC (PPH), a leading protein by-product processor that supplies many of the leading pet food processors in the United States. The partnership agreement afforded the noncontrolling interest holders an option to require us to redeem their ownership interests beginning in November 2009 (fiscal 2010). The redemption value was determinable from a specified formula based on the earnings of PPH.

In fiscal 2010, as a result of discussions with the noncontrolling interest holders, we determined that the noncontrolling interests were probable of becoming redeemable. As such, in fiscal 2010, we recorded an adjustment to increase the carrying amount of the redeemable noncontrolling interests by \$32.2 million with an offsetting decrease of \$19.4 million to additional paid-in capital and \$12.8 million to deferred tax assets.

In November 2009 (fiscal 2010), the noncontrolling interest holders exercised their put option. In December 2009 (fiscal 2010), we acquired the remaining 49% interest in PPH for \$38.9 million. Because PPH was previously consolidated into our financial statements, the acquisition of the remaining 49% interest in PPH was accounted for as an equity transaction.

Sioux City Plant Closure

In January 2010 (fiscal 2010), we announced that we would close our fresh pork processing plant located in Sioux City, Iowa. The Sioux City plant was one of our oldest and least efficient plants. The plant design severely limited our ability to produce value-added packaged meats products and maximize production throughput. A portion of the plant's production has been transferred to other nearby Smithfield plants. We closed the Sioux City plant in April 2010 (fiscal 2010).

As a result of the planned closure, we recorded charges of \$13.1 million in the third quarter of fiscal 2010. These charges consisted of \$3.6 million for the write-down of long-lived assets, \$2.5 million of unusable inventories and \$7.0 million for estimated severance benefits pursuant to contractual and ongoing benefit arrangements, of which \$5.5 million were paid-out during the fourth quarter of fiscal 2010. Substantially all of these charges were recorded in cost of sales in the Pork segment. We do not expect any significant future charges associated with the plant closure.

Pork Segment Restructuring

In February 2009 (fiscal 2009), we announced a plan to consolidate and streamline the corporate structure and manufacturing operations of our Pork segment (the Restructuring Plan). The plan included the closure of six plants, the last of which was closed in February 2010 (fiscal 2010). This restructuring is intended to make us more competitive by improving operating efficiencies and increasing plant utilization. For fiscal 2010, we achieved our targeted cost savings and improved pre-tax earnings, after applicable restructuring charges, of \$55 million in fiscal 2010. We expect the benefits of the Restructuring Plan will be fully reflected in our fiscal 2011 results.

DESCRIPTION OF SEGMENTS

Pork Segment

The Pork segment consists mainly of three wholly-owned U.S. fresh pork and packaged meats subsidiaries. The Pork segment produces a wide variety of fresh pork and packaged meats products in the U.S. and markets them nationwide and to numerous foreign markets, including China, Japan, Mexico, Russia and Canada. The Pork segment currently operates over 40 processing plants. We process hogs at eight plants (five in the Midwest and three in the Southeast), with an aggregate slaughter capacity of approximately 110,000 hogs per day.

The Pork segment sold approximately 4.0 billion pounds of fresh pork in fiscal 2010. A substantial portion of our fresh pork is sold to retail customers as unprocessed, trimmed cuts such as butts, loins (including roasts and chops), picnics and ribs.

The Pork segment also sold approximately 2.9 billion pounds of packaged meats products in fiscal 2010. We produce a wide variety of packaged meats, including smoked and boiled hams, bacon, sausage, hot dogs (pork, beef and chicken), deli and luncheon meats, specialty products such as pepperoni, dry meat products, and ready-to-eat, prepared foods such as pre-cooked entrees and pre-cooked bacon and sausage. We market our domestic packaged meats products under labels that include Smithfield, Farmland, John Morrell, Gwaltney, Great, Cumberland Gap, Armour, Eckrich, Margherita, LunchMakers, Dinner Bell, Carando, Kretschmar, Lean Generation, Lykes, Cook's, Esskay, Valleydale, Ember Farms, Rath, Roegelein, Ohse, Stefano's, Williamsburg, Tom & Ted's and Jamestown. We also sell a substantial quantity of packaged meats as private-label products.

Our product lines include leaner fresh pork products as well as lower-fat and lower-salt packaged meats. We also market a line of lower-fat value-priced luncheon meats, smoked sausage and hot dogs, as well as fat-free deli hams and 40% lower-fat bacon.

During the preceding three fiscal years, our main acquisition in the Pork segment was a vertically integrated hog producer and pork processor of mostly fresh pork products, Premium Standard Farms, Inc. (PSF), in fiscal 2008.

The following table shows the percentages of Pork segment revenues derived from packaged meats products and fresh pork for the fiscal years indicated.

	Fiscal Years					
	2010		2009		2008	
Packaged meats	55	%	53	%	58	%
Fresh pork	45		47		42	
	100	%	100	%	100	%

In fiscal 2010, export sales (including by-products and rendering) comprised approximately 15% of the Pork segment's volumes and approximately 12% of the segment's revenues.

Sources and availability of raw materials

Live hogs are the primary raw materials of the Pork segment. Historically, hog prices have been subject to substantial fluctuations. Hog supplies, and consequently prices, are affected by factors such as corn and soybean meal prices, weather and farmers' access to capital. Hog prices tend to rise seasonally as hog supplies decrease during the hot summer months and tend to decline as supplies increase during the fall. This tendency is due to lower farrowing performance during the winter months and slower animal growth rates during the hot summer months.

The Pork segment purchased 46% of its U.S. live hog requirements from the Hog Production segment in fiscal 2010. In addition, we have established multi-year agreements with Maxwell Foods, Inc. and Prestage Farms, Inc., which provide us with a stable supply of high-quality hogs at market-indexed prices. These producers supplied approximately 10% of hogs processed by the Pork segment in fiscal 2010. We also purchase hogs on a daily basis at our Southeastern and Midwestern processing plants and our company-owned buying stations in three Southeastern and five Midwestern states.

We also purchase fresh pork from other meat processors to supplement our processing requirements. Additional purchases include raw beef, poultry and other meat products that are added to sausages, hot dogs and luncheon meats. Those meat products and other materials and supplies, including seasonings, smoking and curing agents, sausage casings and packaging materials, are readily available from numerous sources at competitive prices.

International Segment

The International segment includes our international meat processing operations that produce a wide variety of fresh pork, beef, poultry and packaged meats products, including cooked hams, sausages, hot dogs, bacon and canned meats. We have controlling interests in international meat processing and distribution operations located mainly in Poland, Romania and the United Kingdom. In addition, we have noncontrolling interests in international meat processing operations, mainly in Western Europe and Mexico, including a 37% interest in the common stock of Campofrío Food Group, S.A. (CFG), a leading European packaged meats company headquartered in Madrid, Spain, and one of the largest worldwide with annual sales of approximately €1.8 billion (approximately \$2.4 billion as of May 2, 2010).

The following table shows the percentages of International segment revenues derived from packaged meats, fresh pork and other products for the fiscal years indicated.

	Fiscal Years					
	2010		2009		2008	
Packaged meats	35	%	34	%	41	%
Fresh pork	24		31		19	
Other products(1)	41		35		40	
	100	%	100	%	100	%

(1) Includes poultry, beef, by-products and rendering

The International segment has sales denominated in foreign currencies and, as a result, is subject to certain currency exchange risk. See “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Derivative Financial Instruments” for a discussion of our foreign currency hedging activities.

Sources and availability of raw materials

Like the Pork segment, live hogs are the primary raw materials of the International segment with the primary source of hogs being the Hog Production segment. The International segment purchased 87% of its live hog requirements from the Hog Production segment in fiscal 2010.

Hog Production Segment

As a complement to our Pork and International segments, we have vertically integrated into hog production and are the world’s largest hog producer. The Hog Production segment consists of our hog production operations located in the U.S., Poland and Romania, as well as our interests in hog production operations in Mexico. The Hog Production segment operates numerous hog production facilities with approximately 1.0 million sows producing about 19.3 million market hogs annually. In addition, through our Mexican joint ventures, we have approximately 90,000 sows producing about 1.7 million market hogs annually.

