EQUITY RESEARCH AMERICAS

Food Products

Brands Still Matter To Consumers - Do They To Investors?

Key Takeaway

Previously our sector thesis was that accelerating consolidation & cost cutting activity should drive earnings upside. We are adding a new element, related to brands that we believe will drive an inflection in sales growth and drive further earnings upside. The attached Brands Still Matter report, is the result of a collaborative project with Accenture & Barkley that we began 3 months ago, and forms the basis of this new "brand" element to our thesis.

Key takeaways from our Brands Still Matter report are outlined below.

Consumer preferences have not changed, and emerging brands are not tapping into newfound preferences. Taste and price remain top attributes for consumers. However, consumers have more leverage and are demanding that brands do more – i.e. meeting needs of a "holistic experience" that includes attributes such as health, trust and sustainability.

Contrary to popular belief, leading brands have maintained their ground & it is important to be a leader. 60% of leading brands are growing sales and 53% are growing share. Mid-tier brands and the long "tail" is struggling. Loyalty to Leading Brands remains very high and relatively stable. Leading Brands are incredibly productive at retail.

Consumer insights, brand activation and operating model agility are key to succeeding. Companies that build next-generation capabilities in consumer insights and category development, brand activation and operating model agility are likely to succeed.

Cost-savings opportunity is significant and can fund next-gen capability investments. We estimate the industry can reduce supply chain costs by $18-$30B or ~300-500 bps of sales. Emerging technologies (AI, Blockchain, etc.) could unlock incremental savings and at a faster rate.

We expect strength of brands to be reflected in improved organic sales growth trends. Large food companies' sales growth has underperformed overall food consumption growth. We believe most of the factors driving the underperformance are transitory while the street assumes the issues are more structural. The street assumes big brands (and by association big food companies) are dying because consumer needs have fundamentally changed, and only small/emerging brands are able to meet these needs. Our evidenced based research dispels these beliefs. Moreover, we believe transitory factors such as strategy transition, pantry de-loading, consolidation and channel blurring are the main causes.

Industry valuations are attractive especially considering our non-consensus view on industry's growth prospects. LT, we believe large packaged food companies on average can grow sales organically at ~2% and EBIT 5-8%, generally in-line with the historical growth algorithms but higher than street expectations (~5% EBIT growth).

HRL & PF are the two companies that skew most to Brands Still Matter thesis element but we are making several other adjustments to our stock picks & rankings. After incorporating findings from our BSM study into our comprehensive stock picking framework, our stock picking rankings have changed quite a bit and we are upgrading GIS and HRL to Buys. Our top picks are now PF, KHC, HRL and MKC.

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^Prior trading day's closing price unless otherwise noted.

Company Name	Ticker	Mkt. Cap (MM)	Rating	Price^	Price Target	Cons. Next FY	Current EPS Estimates 2017	2018	2019	Previous Est. 2018	2019
Flowers Foods	FLO	$4,361.4	HOLD	$20.67	$19.00	1.04	$0.89	$1.07	$1.14	$0.93	$1.02
General Mills	GIS	$31,778.2	BUY▲	$54.79	$63.00▲	$3.12	$3.08	$3.19	$3.55	$3.08	$3.23
Hormel Foods	HRL	$17,797.0	BUY▲	$33.08	$38.00▲	$1.69	$1.57	$1.86	$2.00	$1.60	$1.72
Tyson Foods	TSN	$27,724.8	BUY	$74.73	$85.00	$6.44	$5.31	$6.75	$7.40	$5.76	$6.19

Investment Summary

Challenging but attractive industry. Empowered, challenging consumer: Increasing complexity, changing behaviors and demands. Increasing competition: Disruptive new business models and decreased barriers to entry. Macroeconomic concerns: Mature US market and continued price pressure. However, the US CPG market is still a must-win – big, profitable market - $820B in sales and $120B-$160B in profits.

Consumer preferences have not changed, and emerging brands are not tapping into newfound preferences. Taste and price remain top attributes for consumers while choosing what food to buy, yet consumers are demanding brands do more, meeting needs of a "holistic experience" that include attributes such as health, trust and sustainability. Brands can resonate with consumers by providing a "reliable" experience that consumers can trust will align with their ideals.

Contrary to popular belief, leading brands have maintained their ground – and it's important to be leading (#1/#2). 60% of leading brands are growing sales and 53% of leading brands are growing share; mid-tier brands are struggling. Consumers continue to purchase – and repurchase – leading brands (high loyalty). Leading brands are incredibly productive at retail.

Consumer insights, brand activation and operating model agility are key to succeeding. It's not about being a big or small brand, but instead having the right kind of brand for a specific need. Large companies need to rigorously manage a portfolio of brands, with different types of brands (and levels of investment) for different categories/ consumer need states. Companies that build next-generation capabilities in consumer insights and category development, brand activation and operating model agility are likely to succeed.

Cost savings opportunity is significant and can fund next-gen capabilities that will drive profitable growth. We estimate the industry can reduce supply chain costs by $18-$30B or 300-500 bps of sales. Emerging technologies (AI, Blockchain, etc) could unlock incremental savings and at a faster rate.

Market is pricing in a significant structural slowdown in CPG EBIT growth. The underperformance of large CPG relative to overall food consumption (~300 bps gap in growth) does not signal the death of big brands but is more a function of several transitory factors that we believe are likely to reverse. LT, we believe large CPG's on average can grow sales organically at ~2% and EBIT 5-8%, generally in-line with the historical growth algorithm's but higher than street expectation – street is expecting ~5% EBIT growth.

We have incorporated findings from our BSM study into our comprehensive stock picking framework – upgrading GIS and HRL to Buy; Our top picks are now PF, KHC, HRL and MKC. GIS and HRL are both high quality names that are beaten down with under-appreciated brand portfolio strength and competitive advantages in the faster growing unmeasured channels - perimeter of store (HRL) and Ecommerce (GIS).

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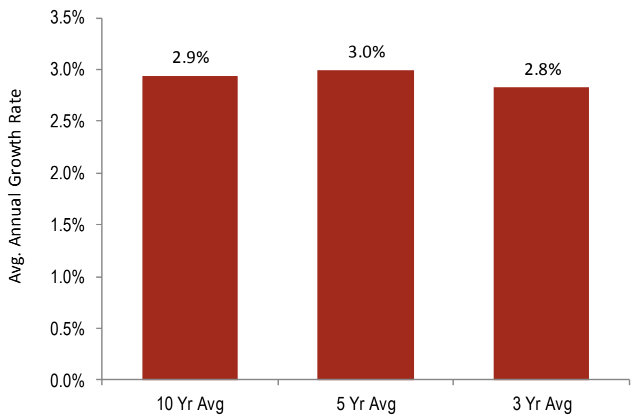
U.S. Food Sales Growth Has Slowed Down But Not For Reasons Many Believe...

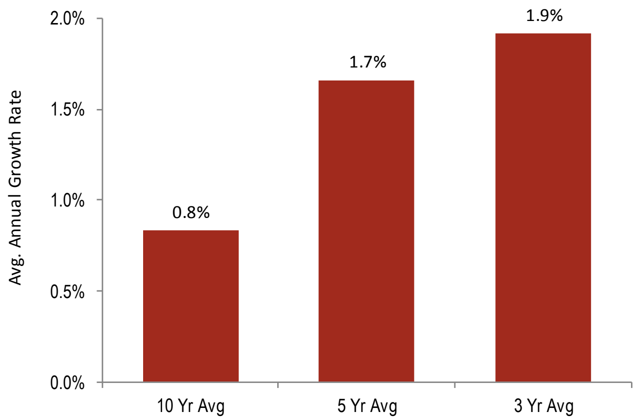
Food industry sales growth has been relatively stable; volume growth seems to be accelerating. According to the Bureau of Economic Analysis (BEA), growth in total U.S. food expenditures has been relatively stable over the last 10 years. Specifically, the data suggests that in dollar terms, total spending on food (At-Home and Away From Home) has grown at a ~2.9% CAGR over the last ten years, ~3.0% over the last five years and ~2.8% over the last three years. Interestingly, however, volume growth has been accelerating over the aforementioned period – total food volumes have grown at ~0.8%, ~1.7% and ~1.9% over the last ten, five and three-year periods, respectively.

Chart 1: Total U.S. Food Sales Growth (At-Home + AFH) Has Been Relatively Stable Over The Past Decade



Source: Bureau of Economic Analysis (BEA), Jefferies estimates

Chart 2: ...While Volume Growth Seems To Be Accelerating



Source: BEA, Jefferies estimates

Population growth and per capita caloric consumption seem to be driving the acceleration in volume growth. Historically (last 50 years), the U.S. population has grown at ~1% per year, while calories consumed per capita have grown at ~0.5% annually. In combination, we estimate these two factors have driven ~1.5% annual growth in total U.S. caloric consumption, however both population growth and per capita caloric consumption have slowed more recently. Although per capita caloric consumption has declined on an absolute basis over the last 10 years, it appears to have re-accelerated in more recent years (see Chart 4). This combined with positive population growth (albeit slightly lower relative to historical levels) seems to be driving the recent upward trend in food volume growth.

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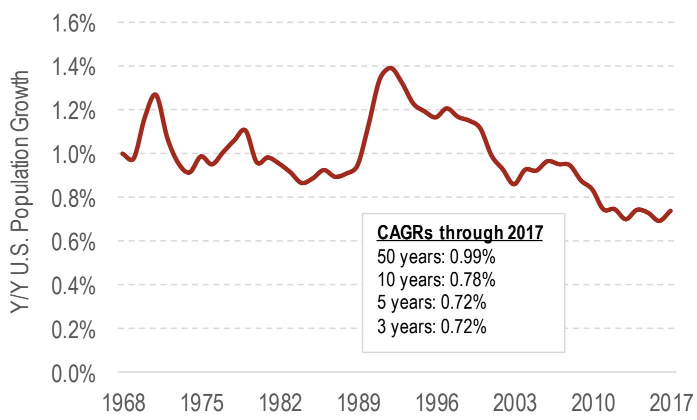
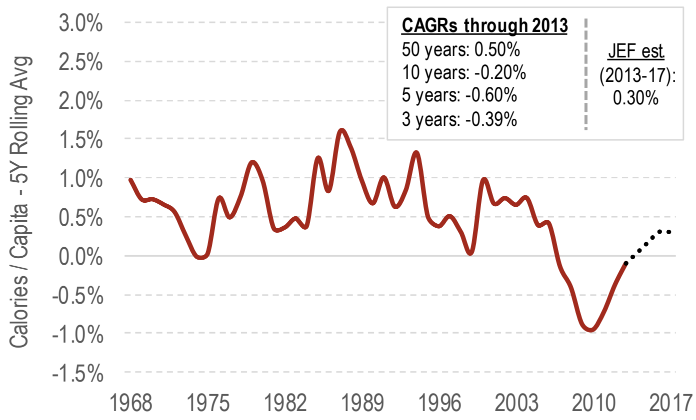
Chart 3: US Pop. Growth Has Stabilized & Is Accelerating In Recent Years



Source: The World Bank, Jefferies estimates

Chart 4: Per Capita Caloric Consumption Has Also Accelerated Recently

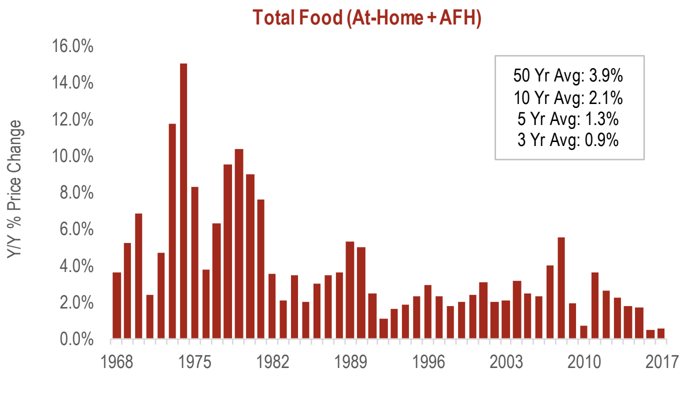


Source: FAOSTAT, Jefferies estimates

**Caloric consumption data beyond 2013 are Jefferies estimates (actuals not available post-2013)*

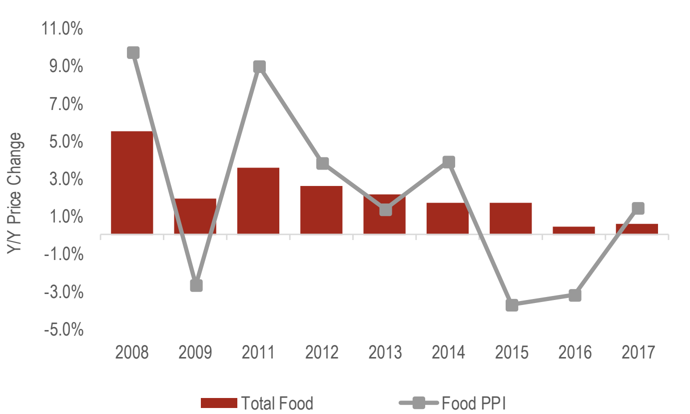
The food industry's ability to take pricing has diminished, but that has been true for at least the last 10 years – pricing pressure is not materially increasing. We acknowledge that food companies' ability to take pricing has diminished relative to the industry's long-term history, however this has been the case for a long time now (driven to a large degree by Walmart's expansion in the grocery space) and has impacted other CPG manufacturers, not just food producers. As such, we do not believe that pricing pressure in the food industry is increasing materially as some investors contend.

Chart 5: The Industry's Ability To Increase Pricing Has Diminished…



Source: BEA, Jefferies estimates

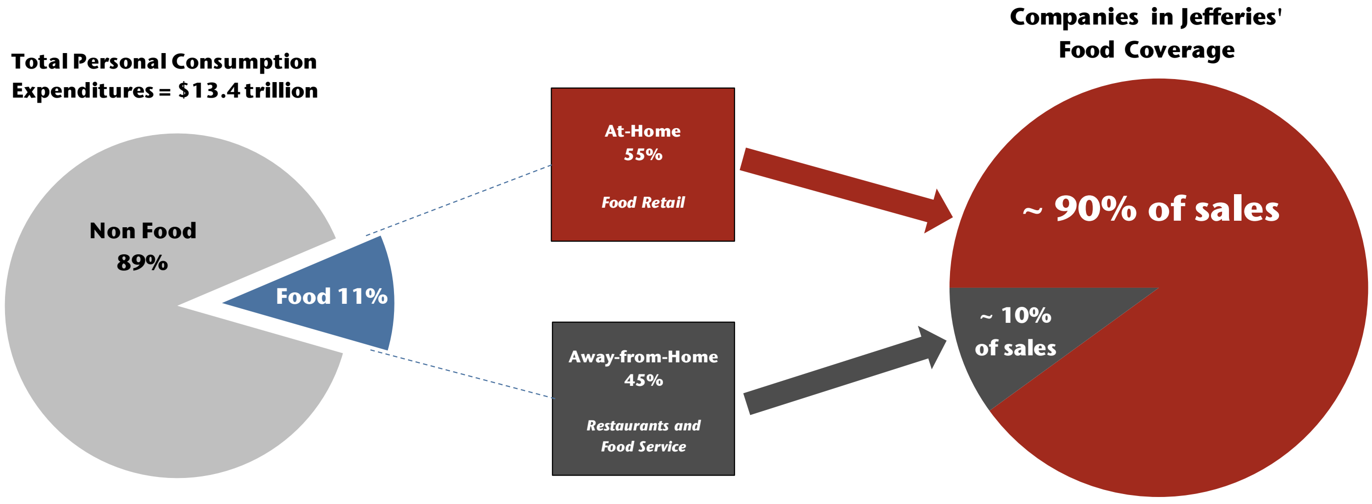
Chart 6: …However Decelerating Food PPI Growth Partially Explains Some Of The More Recent Pricing Slowdown



Source: BEA, BLS, Jefferies estimates

At-Home channel is more representative of our coverage universe. The previously described industry trends pertain to both food consumed at home (food retail) and food consumed away from home (at foodservice locations such as restaurants, for example). The remainder of this report focuses primarily on the at-home channel, which is more representative of our coverage universe. For perspective, according to the BEA, food makes up ~11% of total personal consumption expenditures (~$1.4 trillion annually), of which ~55% is At-Home consumption and ~45% is Away From Home. On average, food companies within our coverage space generate ~90% of their total sales from the At-Home (retail) market while the remaining ~10% comes from Away From Home (foodservice).

Chart 7: At-Home Channel (Food Retail) Trends Are Most Relevant To Our Coverage Universe



Source: BEA, Company data, Jefferies estimate

At-Home food sales growth has lagged overall food sales growth owing to consumers eating out more (especially true since the 2008-09 recession). BEA data indicates that growth in At-Home food sales has decelerated meaningfully relative to long-term averages (from >5% over the last fifty years to ~3% more recently). Moreover, At-Home food sales have decelerated at a faster pace than overall food primarily as a result of consumers eating out more (see Chart 8 below – growth in Away From Home has outpaced At-Home by >200 bps over the last 50 years) and, interestingly, the gap has widened since the 2008-09 recession.

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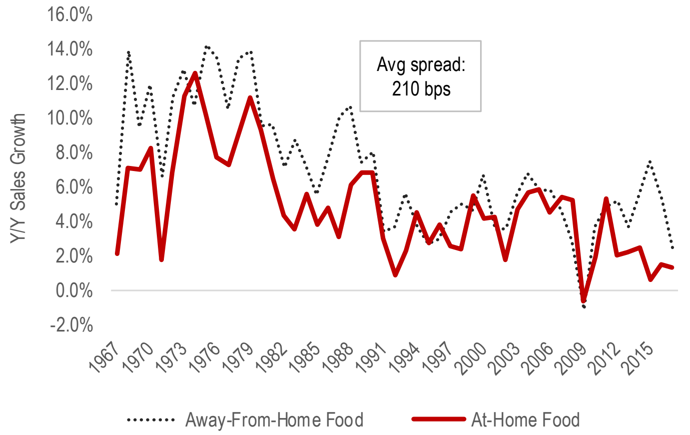
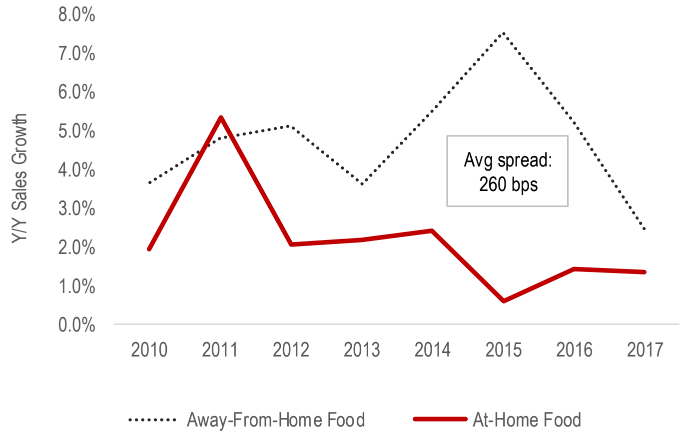
Chart 8: At-Home Food Sales Growth Has Lagged Away-From Home by ~210 bps on Average Over Last 50 Years



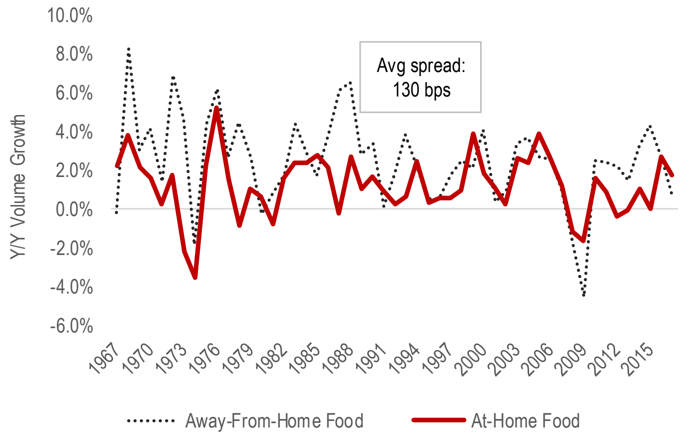
Source: Company data, BEA

Chart 9: ...And This Growth Gap Widened Since The Recession to ~260 bps



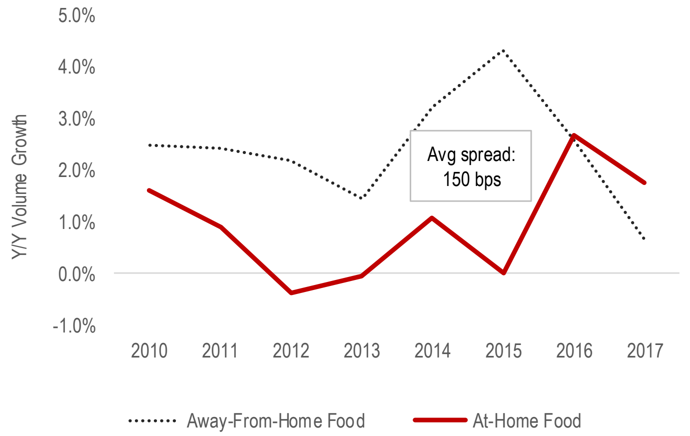
Source: Company data, BEA

Chart 10: At-Home Food Volume Growth Has Lagged Away-From Home by ~130 bps on Average Over Last 50 Years



Source: Company data, BEA

Chart 11: ...Volume Growth Trends Have Reversed In Favor of AH Food Over Last Two Years



Source: Company data, BEA

Encouragingly, share trends have seemingly reversed in favor of At-Home over the last 2 years (first time since 2009). Interestingly, At-Home food volume growth has been accelerating in recent years, which is likely contrary to what many investors believe given the lackluster earnings results from many food companies in recent years. Moreover, At-Home volume growth has exceeded Away From Home in each of the last two years after consistently trailing Away From Home since 2009.

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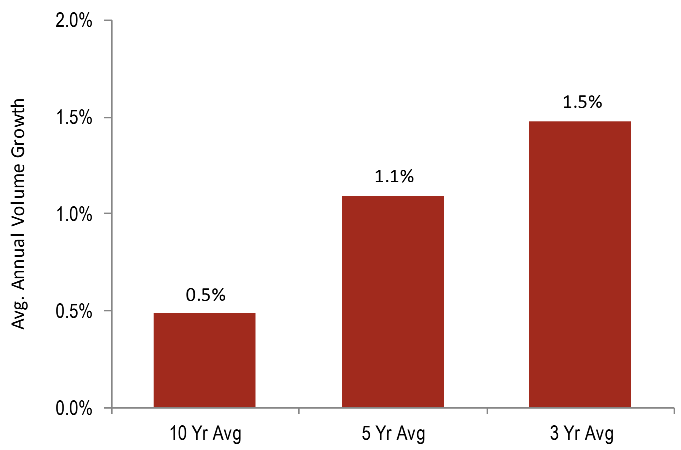
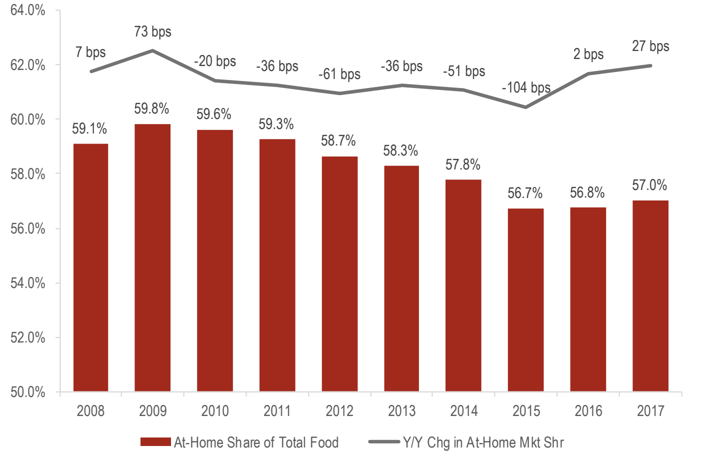
Chart 12: At-Home Food Volume Growth Has Been Accelerating Over The Past Several Years



Source: BEA, Jefferies estimates

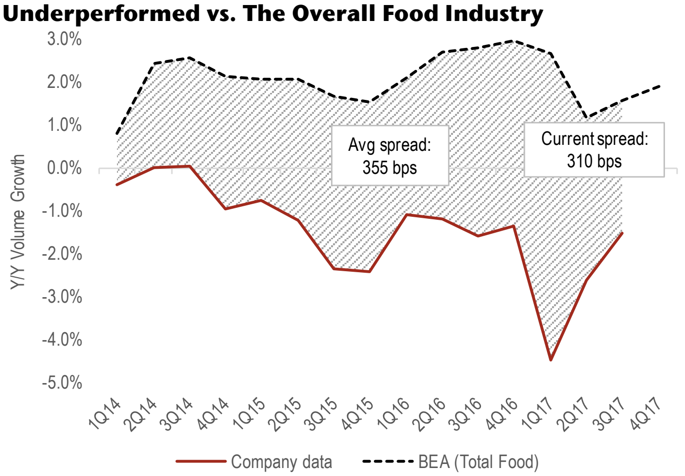
Chart 13: At-Home Grew At A Faster Pace Than AFH In 2016 and 2017 (First Time Since 2009)



Source: BEA, Jefferies estimates

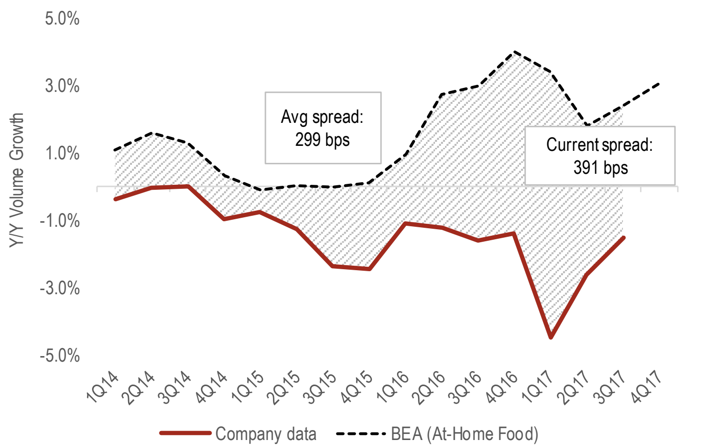
However, public company results and measured channel data (AC Nielsen) have lagged overall food growth. Reported data for ten large-cap U.S. packaged food companies we track indicates that, on average, volumes for these companies have declined at an annual rate of -1.5% since 2013 and even worse (-2.0%) over the last two years. This reported data has consistently underperformed the overall food and At-Home markets (as reported by the BEA) by a relatively wide margin and has also underperformed relative to total food growth as implied by Nielsen measured channel data (we note that Nielsen measured channels have mostly underperformed the overall market as well since 2013; see Charts 14-17 below).

Chart 14: Food Companies' Reported Volume Growth Has Underperformed vs. The Overall Food Industry



Source: Company data, BEA

Chart 15: …Similarly, Reported Volumes Have Also Lagged 'At-Home' Food Volume Growth



Source: Company data, BEA

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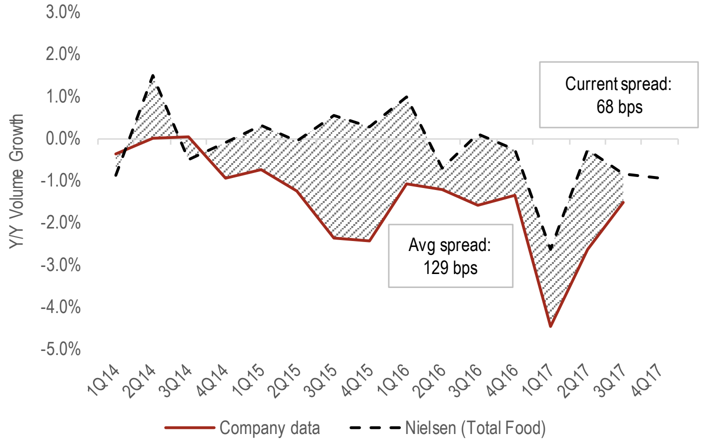
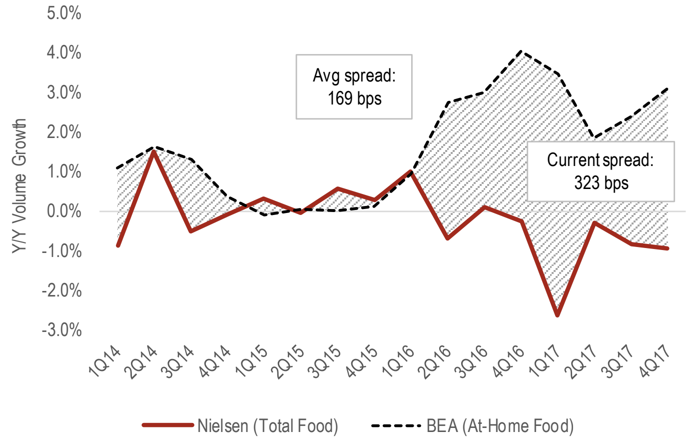
Chart 16: Company Results Have Even Trailed Growth In Nielsen Measured Channels



Source: Company data, Nielsen

Chart 17: …Measured Channel Growth Has Also Lagged The Broader 'At-Home' Food Market, Particularly Since 2016



Source: Nielsen, BEA

"To a large degree, the underlying basis of investors' negative sentiment is the perception that large food brands are "dying", increasingly losing share to private label and steadily losing their pricing power, which is expected to erode margins over time and stifle earnings growth."

Investors are extrapolating / assuming the underperformance in company results & measured channel data relative to overall food growth is structural and will persist. Investors' focus has primarily been on reported company results and measured channel data (Nielsen/IRI) and the market is extrapolating that the previously described gap relative to the broader market (At-Home food) will continue. The relatively pessimistic market outlook on food industry earnings growth is predicated on the belief that the string of disappointing sales and earnings results over the past few years is likely to persist for the foreseeable future. To a large degree, the underlying basis of this negative sentiment is the perception that large food brands are "dying", increasingly losing share to private label and steadily losing their pricing power, which is expected to erode margins over time and stifle earnings growth. Although we acknowledge that the industry's ability to take pricing has diminished relative to its long-term history (also true in other sectors beyond the food space), we disagree with the notions that large brands are dying or likely to lose to private label. We acknowledge that industry dynamics for food manufacturers have been challenging for the past few years, but we do not believe the industry is facing a severe / long-term, structural issue which the market seems to be pricing in. Said differently, we believe current market expectations are too low.

We believe much of the disappointing results among public US food companies have been driven by transitory factors which should abate over time. With the food industry transitioning from a growth to a mature stage, several large manufacturers have faced challenges in adapting their strategies accordingly. While top-line growth was relatively easy to come by historically (owing to the industry's historical ability to take pricing), food companies today need to be more diligent in terms of margin management and analyzing returns on reinvestment activities in order to drive sustainable earnings growth. We believe recent reported data from several of the large, publicly-traded food manufacturers contains a lot of "noise" related to this strategic "transition" that the industry is going through. For example, several companies are in the process of reshaping their portfolios through SKU rationalization and M&A (which increases executional risk), reassessing and in many cases pulling back on promotional spending (which could negatively impact volumes in the short-term but should benefit profitability longer-term), and are also contending with inventory adjustments at the retailer and consumer levels. In addition, retail square footage has been declining and other non-traditional channels (e.g. eCommerce) have gained a foothold (which some companies have been slower to adapt to than others). In some cases, smaller emerging

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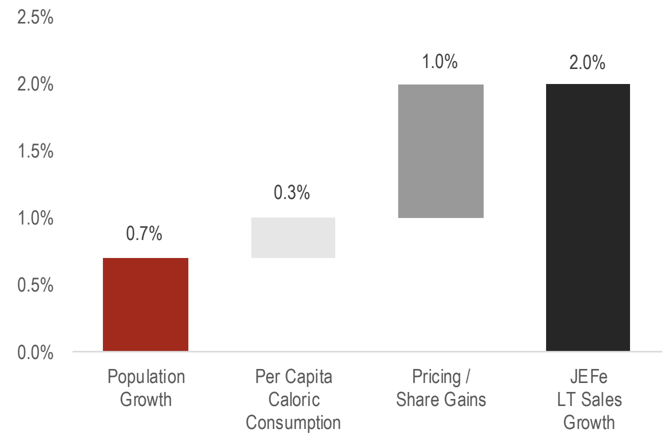
brands have taken share from the larger players, but these instances are relatively few and far between, and frequently these emerging brands eventually get acquired by the larger companies. Over time, we would expect the level of disruption from all these factors to abate and for food company results to converge towards the broader At-Home market trends.

Longer term, we expect At-Home sales growth to average ~2% driven by population growth and increases in per capita consumption. Over the long term, we expect At-Home food sales to grow ~2% per year driven by pricing (~1 pt), population growth (~70 bps), and increases in per capita consumption (~30 bps). For perspective, At-Home food sales have grown between 1.5-2.6% per year over each of the last 3, 5 and 10-year periods. Of the aforementioned growth in At-Home sales, we estimate pricing contributed anywhere from ~0-2%. We believe food companies that can manage their portfolios reasonably well should be able to drive organic top-line growth in line with the ~2% long-term rate we are projecting for At-Home food, while best-in-class managers should be able to exceed that.

Chart 18: We Expect At-Home Food Sales To Grow ~2% Long-Term



Source: Jefferies estimates

Our expectations for At Home Food are likely significantly higher than what the market is pricing in. Given the relatively lackluster growth implied by recent measured channel data and company earnings, we believe our outlook for At-Home food sales growth is likely much higher than what most investors expect. We believe our views on the ongoing relevance of brands as well as the transitory nature of recent industry headwinds are differentiated and largely explain our more optimistic outlook relative to the market. Although we expect many of the headwinds to continue to impact food company results in the short-term, we note that some of the most recent measured channel data and company reports are pointing to improving trends (albeit still down y/y).

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Cost-Savings Opportunity & Thereby Profit Growth Is Underestimated

For our projected food industry earnings growth algorithm to work, companies need to increase margins by ~80-100 bps/year. EBIT margins for the food group on average are 15%. To grow EBIT at 8% (HSD's) with 2% sales growth would imply that margins would need to improve by ~90 bps/year.

Historically the food group on average has delivered 30-40 bps/year of margin expansion, implying that the industry would have to significantly accelerate its margin expansion. Our analysis of a broad group of publicly traded food companies indicates that on average over the last 5 years the industry has managed to expand margins by 30-40 bps/year. Best-in-class (top quartile) performers expanded margins anywhere from 75-350bps/year.

Chart 19: On Average, Food Companies Have Expanded Margins By ~30-40 bps/year Over The Past 5 Years – However, Top Quartile Performers Have Significantly Outperformed The Group Average

U.S. Packaged Food EBITDA Margin Trends (Last 5 Years; Sorted By Annual Avg. Expansion)

		EBITDA Margin (FY)						Margin Expansion (Last 5 Years)*	
Company Name	Ticker	Last FY-5	Last FY-4	Last FY-3	Last FY-2	Last FY-1	Last FY	Cumulative	Annual Avg
Kraft Heinz Company	KHC	-	-	-	22.4%	24.6%	29.4%	696bp	348bp
Lamb Weston Holdings, Inc.	LW	-	-	17.8%	18.0%	19.8%	22.3%	447bp	149bp
Tyson Foods, Inc. Class A	TSN	5.3%	5.5%	5.8%	7.2%	9.6%	11.0%	562bp	112bp
Hormel Foods Corporation	HRL	10.2%	10.5%	11.2%	13.0%	14.9%	15.0%	476bp	95bp
Pinnacle Foods, Inc.	PF	-	17.1%	18.4%	19.5%	20.0%	20.6%	352bp	88bp
Conagra Brands, Inc.	CAG	-	17.8%	16.6%	17.0%	18.0%	21.1%	334bp	83bp
Campbell Soup Company	CPB	19.2%	20.3%	19.1%	18.8%	22.3%	22.9%	370bp	74bp
Lancaster Colony Corporation	LANC	14.5%	14.9%	16.7%	15.9%	17.5%	18.1%	358bp	72bp
Snyder's-Lance, Inc.	LNCE	10.3%	12.1%	12.8%	11.8%	11.5%	13.0%	264bp	53bp
Mondelez International, Inc.	MDLZ	16.0%	15.2%	15.1%	15.3%	17.8%	18.4%	241bp	48bp
Hershey Company	HSY	21.4%	21.7%	22.2%	22.3%	23.3%	23.8%	234bp	47bp
J. M. Smucker Company	SJM	20.6%	20.7%	21.7%	19.8%	21.9%	22.9%	226bp	45bp
SodaStream International Ltd.	SODA	13.5%	13.8%	12.9%	9.1%	8.6%	15.7%	220bp	44bp
General Mills, Inc.	GIS	19.9%	19.6%	19.5%	19.3%	20.5%	22.0%	208bp	42bp
Kellogg Company	K	17.8%	17.6%	18.1%	17.8%	18.1%	19.1%	133bp	27bp
SunOpta, Inc.	STKL	4.9%	6.2%	5.2%	5.4%	5.4%	6.1%	120bp	24bp
J & J Snack Foods Corp.	JJSF	13.4%	14.5%	15.1%	14.7%	14.8%	14.4%	104bp	21bp
Flowers Foods, Inc.	FLO	10.6%	10.8%	11.2%	11.4%	11.7%	11.4%	74bp	15bp
Amira Nature Foods Ltd.	ANFI	12.2%	12.6%	13.3%	14.1%	13.3%	12.8%	62bp	12bp
McCormick & Company, Incorporated	MKC	17.6%	17.5%	17.4%	17.2%	17.2%	17.9%	31bp	6bp
B&G Foods, Inc.	BGS	23.8%	26.7%	25.4%	22.9%	22.5%	23.1%	-70bp	-14bp
Hain Celestial Group, Inc.	HAIN	12.6%	13.6%	14.1%	13.8%	13.1%	9.7%	-300bp	-60bp
Post Holdings, Inc.	POST	22.4%	21.0%	14.3%	14.1%	18.6%	18.9%	-345bp	-69bp
TreeHouse Foods, Inc.	THS	14.6%	14.1%	14.6%	13.3%	12.3%	10.7%	-393bp	-79bp
Inventure Foods, Inc.	SNAK	6.1%	8.7%	8.2%	8.7%	3.4%	1.9%	-418bp	-84bp
Amplify Snack Brands Inc	BETR	-	42.5%	44.4%	43.3%	40.7%	31.4%	-1114bp	-278bp
Group Average		**14.6%**	**16.4%**	**16.4%**	**16.4%**	**17.0%**	**17.4%**	**110 bp**	**32 bp**
Group Median		**14.5%**	**15.1%**	**15.1%**	**15.6%**	**17.7%**	**18.2%**	**214 bp**	**43 bp**

Source: Company data, Jefferies estimates

**Where 5-year history is not available, "Annual Avg" reflects annual margin expansion for longest time period available*

Cost savings efforts post 3G's emergence have accelerated – savings now averaging 3% of sales compared to 1.5% before. We estimate that historically food companies' cost-savings programs averaged ~1.5% of annual sales, however following the successful margin transformation at H.J. Heinz and Kraft Foods Group by 3G Capital, there has been increased pressure for food companies to deliver more, especially in light

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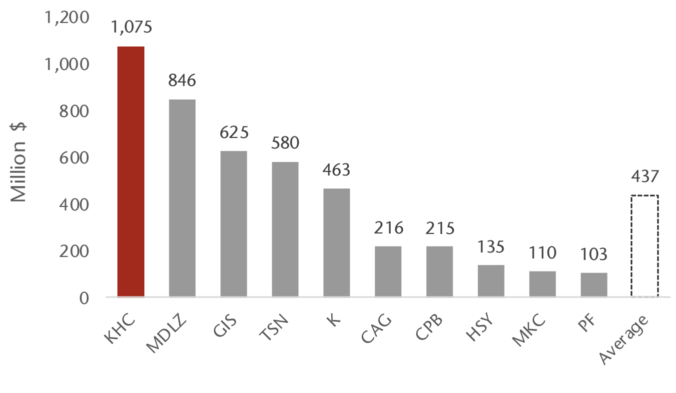
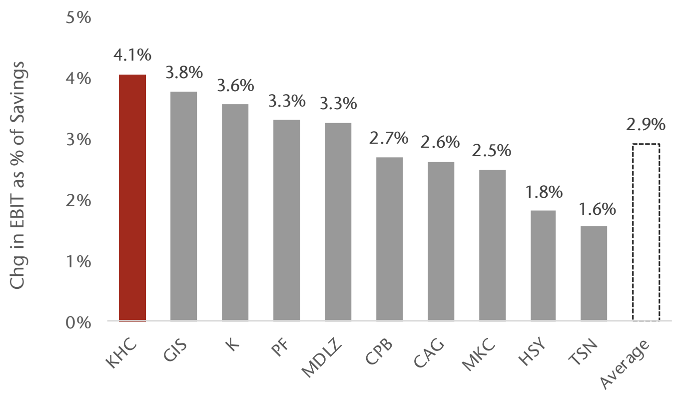
of a weak sales growth environment for the food industry. Following 3G's success several food companies have announced new, aggressive cost-savings programs of their own and we believe the increased focus on cost savings delivery has already started to bear fruit – we estimate that, on average, realized cost savings across numerous food companies averaged ~3% of sales, roughly twice the historical average.

Chart 20: 2016 Actual Cost Savings / Synergies Captured



Source: Company data, Jefferies estimates

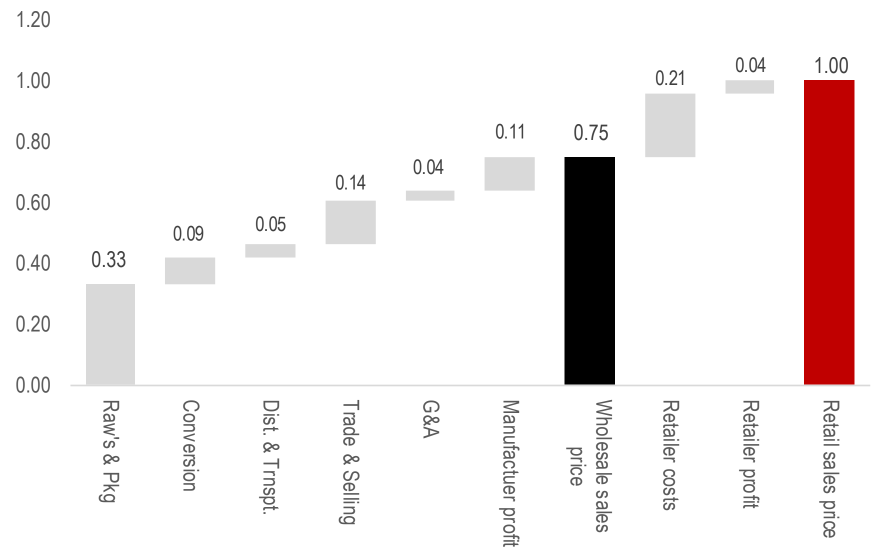
Chart 21: 2016 Actual Cost Savings / Synergies As A Percentage Of Sales



Source: Company data, Jefferies estimates

Looking at the combined value of $1.00 spent on food reveals some interesting findings. We estimate that for every dollar spent on food/beverage items at retail, ~64c represents manufacturers' costs while retailers bear another ~21c of the overall cost. In other words, a majority of food and beverage supply chain costs are in the control of the manufacturer.

Chart 22: Majority of food & beverage supply chain costs are in the control of the manufacturer



Source: Accenture, Jefferies estimates

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We believe supply chain costs can be reduced to the tune of 3-5% of sales, which could be a source of incremental savings for the industry. We believe 50% of the 65c in costs per $1.00 spent at retail by consumer on food are compressible and can be broken down into 4 buckets – manufacturing (conversion costs), distribution/transportation, trade marketing and selling and G&A. In total, we believe the opportunity exists to lower these costs by 3-5% of revenues.

Chart 23: Food Industry - Cost Savings Opportunity

	Food Manufacturer	Adressable Cost Buckets	Cost savings potential in % Low	Cost savings potential in % High	Cost savings potential in cents Low	Cost savings potential in cents High
Raw material & packaging	0.330					
Manufacturing	0.090	0.090	5%	10%	0.005	0.009
Distribution & transporation	0.045	0.045	4%	8%	0.002	0.004
Trade marketing and selling	0.140	0.140	10%	15%	0.014	0.021
Store Operations						
G&A	0.035	0.035	10%	15%	0.004	0.005
Profit	0.110					
Wholesale price	**0.750**					
Retail price						
Total cost savings opp		**0.310**	**8%**	**163%**	**0.024**	**0.039**
% of revenue						
Raw material & packaging	44.0%					
Manufacturing	12.0%	12.0%	6.7%	13.3%	0.6%	1.2%
Distribution & transporation	6.0%	6.0%	5.3%	10.7%	0.2%	0.5%
Trade marketing and selling	18.7%	18.7%	13.3%	20.0%	1.9%	2.8%
Store Operations	0.0%					
G&A	4.7%	4.7%	13.3%	20.0%	0.5%	0.7%
Profit	14.7%					
Total cost savings opp'ty % of sales					**3.2%**	**5.2%**

Source: Company data, Jefferies estimates

Over the last two years, companies in the food space have dropped down ~60% of their cost savings down to the bottom-line (EBITDA). We compared y/y dollar change in EBIT to the amount of absolute cost-savings / synergy capture for several food companies in 2016 (latest year for which we have complete data). We believe this ratio serves as a rough proxy for each company's level of success in terms of dropping cost-savings to the bottom line. Our analysis suggests that the group averages ~ 57% net pass through of cost savings.

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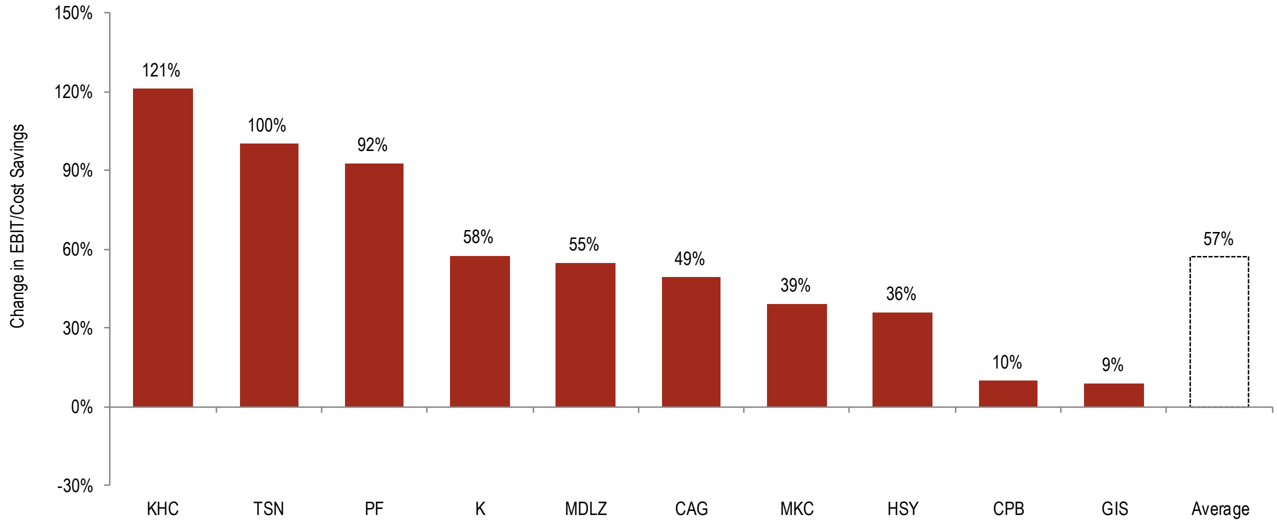
Chart 24: On average, food companies have dropped ~60% of their gross cost-savings to the bottom line – 2016 Data



Source: Company data, Jefferies estimates

We have line of sight to ~180-300 bps margin expansion for the industry, which should be enough to deliver HSD EBIT growth for at least the next 2-3 years (90 bps/year). Assuming the industry can achieve ~60% net pass through of cost savings, we believe there is visibility into 180-300 bps margin expansion for the industry. Consolidation and emerging technology could unlock even more savings and at a faster pace.

In order to drive sustainable margin improvement, companies need to reinvest cost-savings into 3 types of next-generation capabilities. Based on our extensive BSM deep-dive including executive interviews, we posit that the companies that have had greater success in dropping cost-savings to the bottom line are those that have selectively invested capital into next generation capabilities. At a high-level, our deep-dive project work found that there are 3 main types of capabilities that successful food companies have disproportionately invested in: 1) Consumer Insights & Strategy Formulation; 2) Brand Activation; and 3) Operating Model Agility.

Chart 25: To Extract Growth, Brand Owners Need To Focus On Three Types Of Next-Generation Capabilities

Source: BSM Executive Interviews, Accenture Research, Jefferies Research

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Chart 26: Capability Components & Specific Examples

	Capability Components	Examples
CONSUMER INSIGHT & STRATEGY	**Continually Renewing Market and Consumer Awareness:** Holistic, data-driven external outlook that continually scans the market and identifies disruptive opportunities	• Experimentations with evolving technologies (blockchain, AI, etc) • Real-time and predictive insights (consumer, market and technology, etc.) • Data-driven decisions
CONSUMER INSIGHT & STRATEGY	**Compelling, Balanced Portfolio:** Clear and disciplined brand portfolio strategy	• Clearly defined roles, investments and performance metrics by brand • Balanced brand portfolio driving financial goals while renewing new growth options
BRAND ACTIVATION	**Agile Innovation:** Deep consumer insight drives rapid product/ service/ business model innovation	• Open innovation, tapping into extended ecosystem • Consumer-centric design • Corporate garage: rapid prototyping, nimble teams, "minimum viable product"
BRAND ACTIVATION	**Consumer Intimacy:** Hyper-relevant consumer engagement creates authentic brand stories and meaningful relationships	• Consumer intimacy through diverse data sources (consumer, consumption, channel, social) • 'Living' marketing: dynamically adapting to individual consumer occasions and portfolio role
BRAND ACTIVATION	**Consumer-Centric Omnichannel**: Brand alignment across a proliferating array of business models based on consumer occasions	• Category management now aligned around holistic consumer needs rather than products • Omnichannel trade spend management • eCommerce platform partnerships
OPERATING MODEL AGILITY	**Market-Adapting Supply Chain:** Demand-sensing manufacturing/supply chain balances flexibility and efficiency	• Personalization and customization • Rapid commercialization from sourcing to shelf
OPERATING MODEL AGILITY	**Living Organization:** Nimble and modular organization supporting multiple business models with diverse strategic objectives	• Data-driven organization: predictive insights driving decision-making at all levels • Plug-and-play capabilities and infrastructure supporting multiple business models; liquid workforce and assets • Self-organizing project teams and intrapreneurial culture
OPERATING MODEL AGILITY	**Ecosystem Mastery:** Design, form and manage ecosystems for value creation	• Encompassing data, innovation, capabilities, consumer solutions • Define partners, roles and own core competencies

Source: BSM Executive Interviews, Accenture Research, Jefferies Research

Chart 27: Large Brands Require The Greatest Investment In Capabilities

	Capability	Required Mastery by Brand Type		
		Leading	Retailer	Emerging
CONSUMER INSIGHT & STRATEGY	**Continually Renewing Market and Consumer Awareness:** Holistic, data-driven external outlook that continually scans the market and identifies disruptive opportunities	✓		✓
CONSUMER INSIGHT & STRATEGY	**Compelling, Balanced Portfolio:** Clear and disciplined brand portfolio strategy	✓	✓	
BRAND ACTIVATION	**Agile Innovation:** Deep consumer insight drives rapid product/ service/ business model innovation	✓		✓
BRAND ACTIVATION	**Consumer Intimacy:** Hyper-relevant consumer engagement creates authentic brand stories and meaningful relationships	✓		✓
BRAND ACTIVATION	**Consumer-Centric Omnichannel**: Brand alignment across a proliferating array of business models based on consumer occasions	✓	✓	
OPERATING MODEL AGILITY	**Market-Adapting Supply Chain:** Demand-sensing manufacturing and supply chain balances flexibility and efficiency	✓		
OPERATING MODEL AGILITY	**Living Organization:** Nimble and modular organization that supports multiple business models with diverse strategic objectives	✓		
OPERATING MODEL AGILITY	**Ecosystem Mastery:** Design, form and manage ecosystems for value creation	✓	✓	✓

Source: BSM Executive Interviews, Accenture Research, Jefferies Research

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Chart 28: Evolving Digital Technology Presents Disruptive Opportunities For Brand Owners

Technology	Capability	Value	Use Case by Maturity-Level			P&L Impact		
			Foundational	Emerging	Pioneering	Sales	COGS	SG&A
Internet of Things (IOT)		Enabling data sharing across value chain and among ecosystem partners	Quality management; fleet management; digital stores; real-time omnichannel marketing; beacons/ geolocation; wearables	Automated replenishment in consumer homes; remote diagnostics; predictive maintenance	IoT sensors feeding real-time consumer/ market/ supplier data to inform the entire value chain	✓	✓	✓✓
Autonomous Vehicles		Advancements continue to open possibilities in distribution efficiency	Self-driving commercial trucks; last mile delivery; self-driving drones	Self-driving personal automobiles; self-driving public transportation	Drone consumer intelligence; "dronevertising"; from last mile to last feet	✓	✓	✓✓
Artificial Intelligence (AI)		New models for 'Human+Machine' augmentation emerging, extending from operations to consumer	Trend and volume forecasting; descriptive analytics; chatbots; robotics process automation; automate dev ops	Predictive recommendations; Intelligent S&OP; AI-assisted merchandising; dynamic pricing	Scenario-driven prescriptive analytics; brain-simulation ideation; DNA workforce profiling	✓✓	✓✓	✓✓
Robotics		Robotics lowers costs and enables repatriation of manufacturing to bring production closer to the end-consumer	Robotics-enabled prototyping; robotic manufacturing; robotic picking	Automated warehouse; automated sales assistants; automated customer support; robotic shopping carts	Co-bots; perceptive robotics; "dark manufacturing" without human intervention	✓	✓	✓✓

Technology	Capability	Value	Use Case by Maturity-Level			P&L Impact		
			Foundational	Emerging	Pioneering	Sales	COGS	SG&A
Digital Traceability		Consumer demand for trust and transparency continue to increase	Product source tracking; inventory replenishment; supply chain management; product authenticity	End-to-end transparency (farm to fork)	Real-time data across the end-to-end supply chain supports vast data ecosystems	✓	✓✓	✓
3D Printing		R&D, prototyping and manufacturing converge, enabling repatriation of manufacturing, shrinking the supply chain	Prototyping; in-store product printing; real-time manufacturing	In-store 'point-of-sale marketing' printing; in-store customization	Real-time inventory production; 3D printed fashion; custom promotional material; custom workplace	✓	✓✓	✓
Augmented Reality / Virtual Reality (AR/VR)		Growing applications for training workforce and facilitating Human + Machine collaboration	Virtual planogramming; product design; virtual retail locations; AR/VR engagement	Virtual changing rooms; immersive campaigns; virtual training environments	Virtual market research, virtual sourcing; virtual customer service; virtual hiring	✓✓	✓	✓✓
Blockchain		New applications emphasize trusted verification of individually held information	Authenticity verification; supply-chain verification; online wallet; transaction verification; shared ledgers	Employee data verification; verify formal transcripts/ professional credentials	Legal services; "consumer data passport" whereby individuals monetize personal data	✓	✓	✓

Source: BSM Executive Interviews, Accenture Research, Jefferies Research

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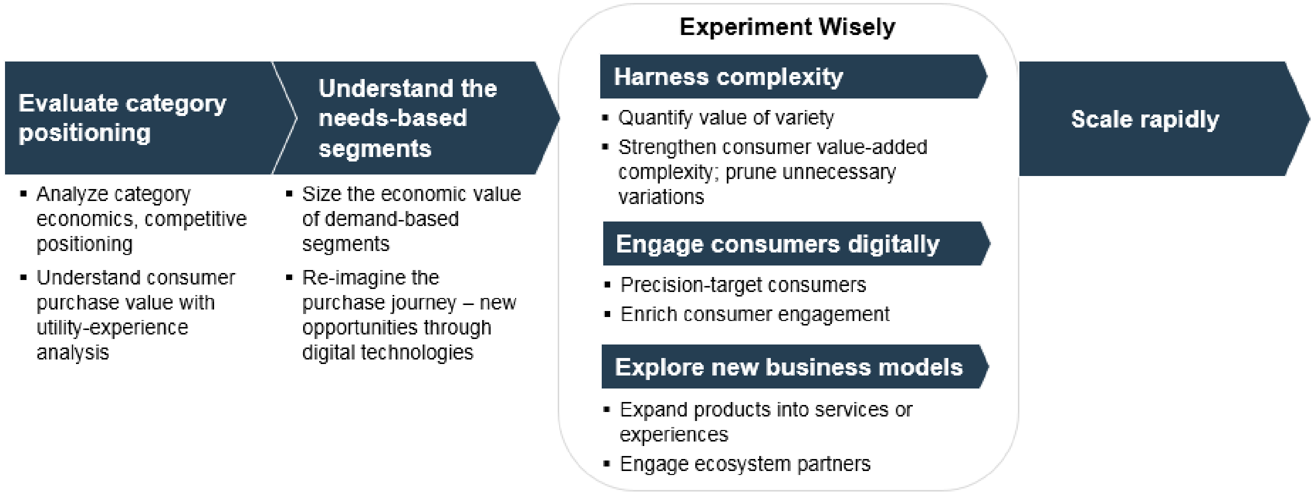
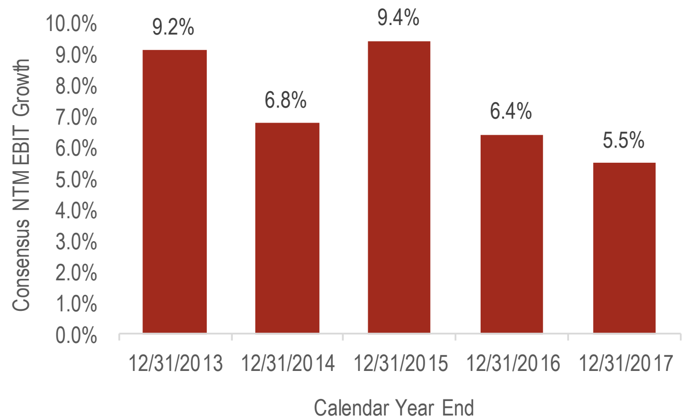
Chart 29: CPG "Playbook" To Ensure That Brands Still Matter



Source: Accenture Research, Jefferies Research

The market is pricing in a significant slowdown in food industry EBIT growth. We believe the market is pricing in a fair amount of sales growth deceleration and, additionally, investors are concerned about potential long-term margin compression in the food industry owing to retailers increasingly squeezing their suppliers to lower prices. In aggregate, we estimate the market is factoring in a ~200 bps slowdown in sales and another ~150 bps slowdown in EBIT growth related to margin compression from pricing concessions.

Chart 30: 'JEF Large Cap Food Index' Projected NTM EBIT Growth – The Market Is Pricing In Further Deceleration In Food Industry EBIT Growth



Source: FactSet, Jefferies estimates

**Note: 'JEF Large Cap Food Index' consists of CPB, CAG, GIS, HSY, HRL, K, KHC, MKC, MDLZ, SJM, TSN*

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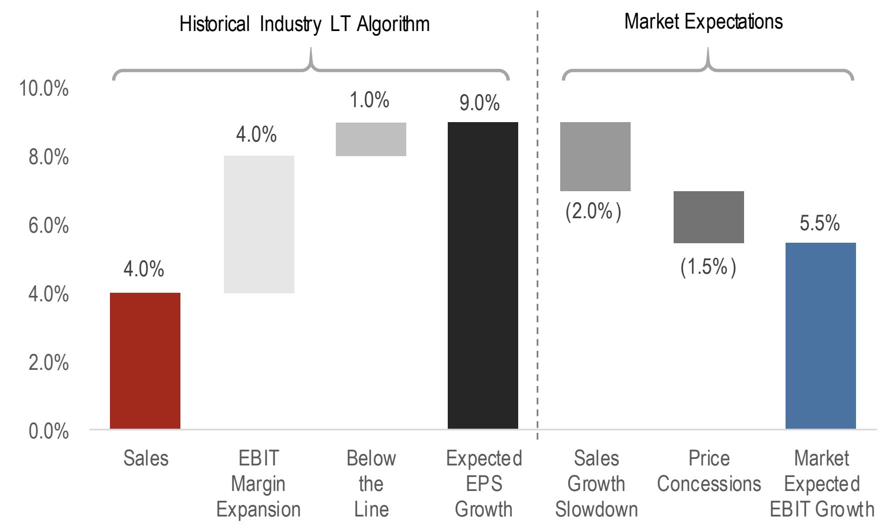
Chart 31: Market Expectations For Industry Earnings Growth Are Pretty Negative

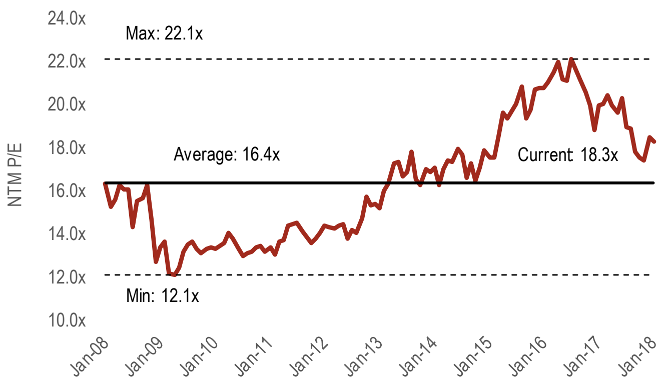


Source: Company data, Jefferies estimates

Sector Valuation Reflects Investor Expectations for a Slowdown In Earnings Growth

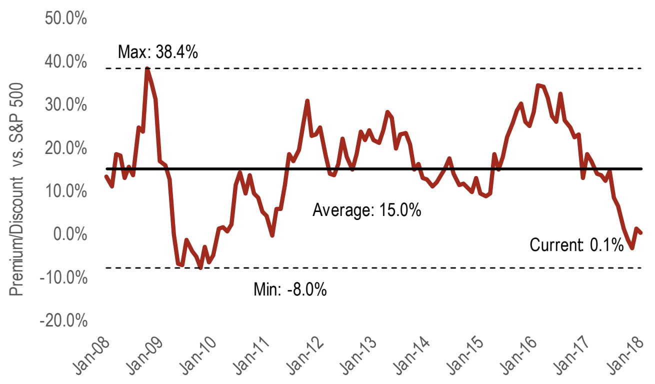
The negative sentiment has driven down food company valuations significantly, especially on a relative basis. P/E valuations for large-cap food stocks reached their most recent peak of ~22x in July 2016 but have come down considerably (~18%) since then. Although the group's absolute P/E valuation remains ~10% above its 10-year average of 16.6x, the group is currently trading at its lowest level relative to the S&P 500 since early 2010 (see Charts 32-34).

Chart 32: JEF Large Cap Index NTM P/E – Valuations Have Come In Significantly Since Their Summer 2016 Peak



Source: FactSet, Jefferies estimates

Chart 33: On A Relative Basis, The Food Group Now Trades At Its Lowest Level Since January 2010



Source: FactSet, Jefferies estimates

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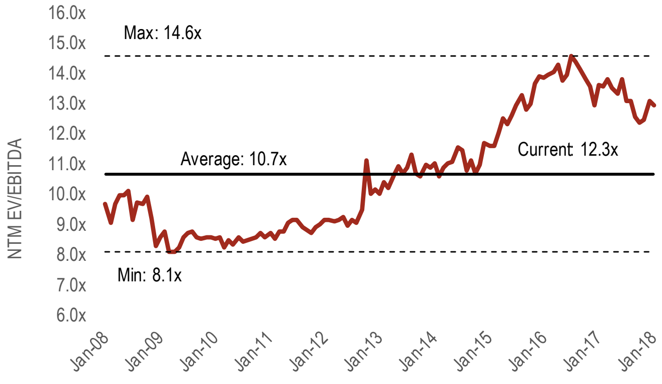
Chart 34: JEF Large Cap Index NTM EV/EBITDA



Source: FactSet, Jefferies estimates

Incorporating Findings From BSM Project Into Our Stock Picking Framework

Key takeaways from our collaborative BSM project. Overall, our extensive BSM project work with Accenture and Barkley solidified our view that brands do still indeed matter. In particular, large 'Leading Brands' have shown that they can succeed in a challenging environment and resonate with consumers, despite relatively widespread perception to the contrary. Other key takeaways are summarized below:

- Consumer preferences have not significantly changed, but their leverage and generational expectations have increased
- Leading Brands are not dying and are still highly valued by consumers; they are able to win due to superior size and capabilities
- Consumers are seeking experiences more than ever, and Food & Beverage brands that can maximize consumer engagement will be poised for success
- Brand owners can meet these category-specific needs by focusing on consumer insight & strategy formulation, brand activation, and operating model agility
- These companies will need to take advantage of the evolving disruptive opportunities presented by evolving technologies and refresh the category management "playbook" to prosper

How we incorporated BSM research findings into our stock picking framework. Companies that build next-generation capabilities in consumer insights and category development, brand activation and operating model agility are likely to succeed. The table below summarizes the way in which we incorporated some of the key findings from our BSM research project into our stock picking framework.

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Jefferies

Chart 35: How we incorporated our BSM findings into our stock picking framework

Capability Drivers	Tools Used	Top 5 Ranked Companies
Brand Portfolio Strength	• Jefferies brand health tracker • BSM Executive Interviews • Jefferies organic growth potential ranking	LW, TSN, HRL, PF, HAIN
Investing in Next-Gen Capabilities & Getting Good Returns	• BSM Executive Interviews • Jefferies management quality - qualitative rankings • Jefferies capital allocation & M&A potential analysis	KHC, HRL, PF, MKC, TSN
Agile & Effective Operating Model	• BSM Executive Interviews • Jefferies management quality - qualitative rankings • Jefferies historical sales, share & margin performance analysis	KHC, HRL, PF, MKC, TSN
Fuel for Growth	• Jefferies cost savings database • Jefferies cost savings conversion analysis • Jefferies cost synergy database	KHC, MKC, PF, HAIN, CAG

Source: Company data, Jefferies estimates

After incorporating BSM findings into our stock picking framework, we are upgrading HRL and GIS to Buys (from Hold). Our deep-dive 'BSM' work reaffirmed our view that HRL is one of the best managed companies in our universe and its brand-building capabilities are best-in-class. Moreover, the company's strong balance sheet and cash flow generation make it a solid platform for accretive acquisitions, and our less pessimistic view on pork processor margins now make us believe that potential downside risk in the Refrigerated Foods business is adequately priced into the stock already. As for GIS, although the company has faced several challenges over the past few years (especially as it relates to top-line growth), we believe the company has significantly enhanced its capabilities and refined its strategy such that it can unlock meaningful value from its underappreciated portfolio of leading brands, especially in the emerging e-Commerce channel. In addition, we expect M&A to play a greater role in GIS' growth in the near to mid-term and we show that even a hypothetical buyout of the company by KHC (which is widely expected to do another large acquisition sometime in the near future) at $70/share (~30% premium) would be significantly (double-digits) accretive to KHC's earnings. We outline our company-specific views on HRL and GIS in greater detail below.

Our Top 5 picks now are PF, KHC, HRL, MKC and TSN. In light of our view that the industry is currently going through a transitional phase (from a growth to a mature stage), we expect near-term results to continue to reflect some "noise" related to the ongoing strategic shifts. Well-managed portfolios, coupled with "healthy" brands and strong enterprise capabilities, should fare better than the group average while less well-equipped companies face a greater risk of running into execution issues and potential share losses in the interim. As such, we continue to recommend selective stock-picking and have updated our proprietary stock-picking screen to incorporate learnings from our 'BSM' project – specifically, we attempt to quantify and objectively compare those characteristics that distinguish stronger, successful portfolios from the more challenged ones across our coverage space. Our stock-picking screen evaluates companies across 15 different metrics within five broader buckets – we look for stocks with above-average organic growth potential, identifiable margin improvement opportunities, M&A optionality, solid historical returns and reasonable valuations. Chart 36 below summarizes our coverage universe rankings (excluding agribusiness names) while Charts 37-39 summarize our rankings within three of the previously mentioned high-level buckets.

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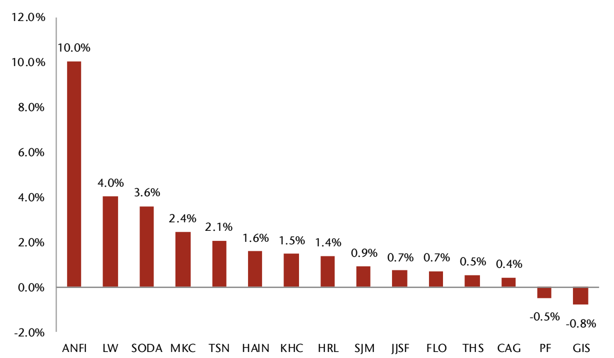
Chart 36: Jefferies Proprietary Stock - Picking Screen

			Organic Growth Potential				Margin Potential			M&A Optionality		Mgmt Quality & Historical Returns			Valuation	
Rank	Company Name	Ticker	Wtd Avg Category Growth (Last 4 Years)	Change in Market Share (L52W)	Next 3 Years Projected Organic Sales Growth (%)	Last 2 Years Innovation % of Sales	Net Cost Savings as % of Sales	JEF Proj. EBIT Margins (Next 3 Yrs)	JEF Margin Potential Rank	Potential Buyout Candidate	Accretive Acquisitions	EPS CAGR (L5Y)	ROIC (Last FY)	Invested Capital (L3Y CAGR)	Premium / Discount vs. Historical Avg EV/EBITDA	Premium / Discount vs. Food Group EV/EBITDA
1	Pinnacle Foods	PF	14	3	10	1	2	3	5	2	5	4	7	9	13	12
2	Kraft Heinz	KHC	7	12	12	6	1	2	4	10	1	3	11	1	9	13
3	Hormel Foods Corporation	HRL	8	6	7	3	11	7	7	10	7	5	4	7	6	9
4	McCormick & Company	MKC	4	14	4	9	4	1	3	10	6	8	8	2	8	15
5	Tyson Foods, Inc.	TSN	5	2	8	7	9	11	9	10	2	2	10	8	12	3
6	Hain Celestial Group, Inc.	HAIN	6	9	3	8	8	5	1	1	9	10	14	12	3	8
7	ConAgra Brands, Inc.	CAG	13	10	14	4	3	9	8	6	3	14	6	15	2	6
8	J. M. Smucker Company	SJM	9	11	11	2	7	15	10	7	8	7	9	4	5	4
9	Lamb Weston Holdings, Inc.	LW	2	1	6	10	11	4	14	4	13	13	1	10	14	10
10	General Mills	GIS	15	13	13	5	10	10	6	3	4	12	3	14	4	7
11	Amira Nature Foods	ANFI	1	15	1	13	11	12	15	10	12	1	12	5	7	1
12	TreeHouse Foods, Inc.	THS	12	7	15	12	6	6	2	10	15	15	15	3	1	2
13	Flowers Foods, Inc.	FLO	11	4	9	11	5	8	11	9	10	9	13	11	10	5
14	J & J Snack Foods Corp.	JJSF	10	8	5	13	11	14	12	8	11	6	5	6	11	11
15	SodaStream International Ltd.	SODA	3	5	2	13	11	13	13	5	14	11	2	13	15	14

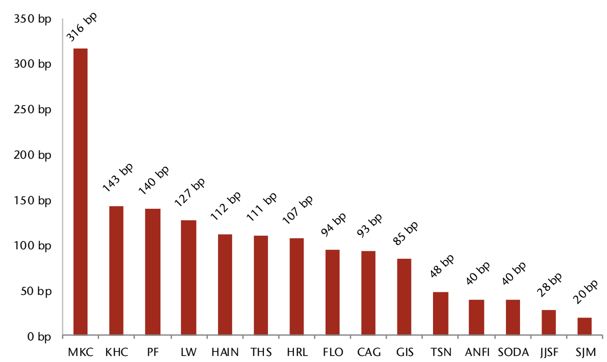
Source: Jefferies estimates

Chart 37: Weighted Average Category Growth



Source: Jefferies estimates, Nielsen xAOC+C

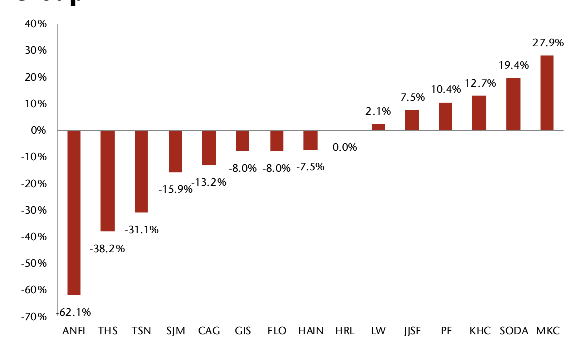
Chart 38: EBIT Margins (Change over Next 3 years)[1]



Source: Jefferies estimates

[1]Forecasted period includes Fiscal Years 2018-2020

Chart 39: EV/EBITDA - Premium/Discount vs. Food Group



Source: Jefferies estimates, FactSet

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Hormel Foods (HRL)
Upgrading to Buy & Raising PT to $38

Key Takeaway

We are upgrading the stock based on the work we did as part of the BSM report and a materially less pessimistic view on pork processor margins. Our deep-dive 'BSM' work reaffirmed our view that HRL is one of the best managed companies in our universe and its brand building capabilities are best-in-class, which combined with its strong BS & CF generation, make it a solid platform for accretive acquisitions.

BSM project supports our upgrade. We worked in collaboration with Accenture's Strategy group and an independent ad agency, Barkley, over a three-month period to assess the importance of brands in the CPG industry. Our work included an exhaustive analysis of 52 Nielsen categories (~60% of overall market), a consumer survey and multiple executive interviews. Overall, we came away feeling that large food brands are significantly underappreciated and undervalued by investors.

Where we are differentiated. We believe our framework for modelling Refrig. Foods EBIT margin based on historical and projected spreads over the commodity pork packer margin is differentiated. Our analysis indicates that HRL has been able to widen this spread over time with its increasing mix of value-added sales and we believe the market may be underestimating the extent to which the company's latest Refrig. Foods acquisitions (Fontanini and Columbus) should be additive to the premium over the commodity packer margin.

Materially less pessimistic view on pork packer margins significantly limits downside risk. We now expect less of a compression in packer margins relative to our estimate a few months ago owing to: 1) greater availability of hogs; and 2) slower ramp up of new plant capacity. As such, we have revised our estimates for the remainder of the year for capacity utilization and processing spreads. We are now projecting pork processing margins will come down by ~$14/head y/y to $20/head in 2018 (vs. our previous estimate of ~$12/head). Accounting for the recent acquisitions, we estimate HRL should earn ~$30/head above the commodity margin (our model assumes a ~$29/head premium in FY18). Our previous estimates implied ~12% potential downside to our Ref. Foods estimates, which we no longer think is the case.

Valuation/Risks

HRL trades at 12.3x our NTM EBITDA estimate, or a ~3% premium to its large-cap food peers. Our new $38 PT values the stock at 13.1x (in line with 3-year average) our FY19 EBITDA estimate of 1.543B.

Risks include: 1) unexpected, material increases in grain prices; 2) competition in the grocery aisle; 3) animal disease; and 4) acquisition-related execution risk.

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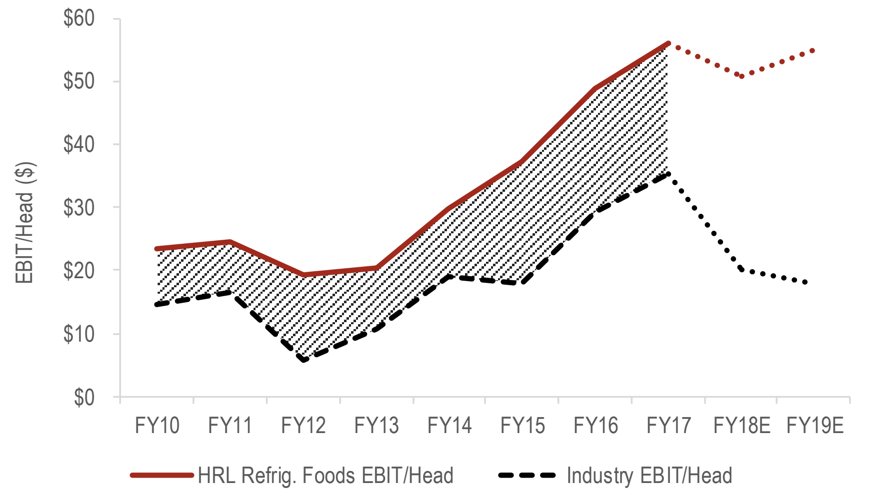
Investment Summary

We believe our framework for modelling Refrig. Foods EBIT margin is differentiated. We believe our framework for modelling Refrig. Foods EBIT margin based on historical and projected spreads over the commodity pork packer margin is differentiated. Our analysis indicates that HRL has been able to widen this spread over time (see Chart 40) with its increasing mix of value-added sales and we believe the market may be underestimating the extent to which the company's latest Refrig. Foods acquisitions (Fontanini and Columbus) should be additive to the premium over the commodity packer margin.

Chart 40: HRL's Refrig. Foods' EBIT/Head Premium Relative To The Industry Has Widened Over The Last Several Years, Which We Expect To Continue



Source: USDA, Company data, Jefferies estimates

Our outlook for pork packer margins has improved materially – we now expect $20/head vs. $12/head previously. We still expect commodity packer margins to compress in 2018 owing to a reduction in industry capacity utilization rates driven by capacity expansion, which we expect to outpace hog supply growth. However, we now expect less of a compression relative to our estimate a few months ago owing to: 1) greater availability of hogs – we expect 1.2 pts greater hog supply than our previous estimates supported by USDA's latest projections; 2) slower ramp up of new plant capacity, which combined with greater availability of hogs, should equate to lower hog prices than we previously assumed. New plants started to come online in October and since then hog prices have rallied significantly while the cutout has not kept pace, resulting in significant margin compression. The margin compression so far in 1Q18 has been lower than we were expecting owing to the aforementioned dynamics. As such, we have revised our estimates for the remainder of the year for capacity utilization and processing spreads. We are now projecting an 11% increase in hog prices (down from 20% previously), which combined with a 1% increase in the cutout price, implies that commodity pork processing margins will come down ~$14/head y/y to $20/head in 2018 (vs. our previous estimate of ~$12/head).

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Chart 41: We Now Expect Capacity Utilization Could Be Down ~200 bps In 2018 (vs. ~300 bps before)

	2015	2016	1Q17	2Q17	3Q17	4Q17	2017	1Q18e	2Q18e	3Q18e	4Q18e	2018e	1Q19e	2Q19e	3Q19e	4Q19e	2019e
Slaughter capacity Heads/day period av	450,611	450,865	450,640	452,703	458,136	473,721	458,800	481,757	485,000	500,000	502,000	492,189	502,000	502,000	502,000	502,000	502,000
y/y ch		0.1%	0.1%	0.6%	1.8%	5.3%	1.8%	6.9%	7.1%	9.1%	6.0%	7.3%	4.2%	3.5%	0.4%	0.0%	2.0%
Hog Slaughter y/y % ch			3.1%	3.7%	2.9%	3.2%		4.0%	5.0%	5.0%	6.0%		2.0%	2.0%	0.0%	0.0%	
Hog Slaughter Heads/day period averag	403,585	413,297	422,041	407,876	419,050	447,636	424,151	438,922	428,269	440,003	474,495	445,422	447,701	436,835	440,003	474,495	449,758
y/y ch		2.4%	3.1%	3.7%	2.2%	1.6%	2.6%	4.0%	5.0%	5.0%	6.0%	5.0%	2.0%	2.0%	0.0%	0.0%	1.0%
Capacity Utilization	**89.6%**	**91.7%**	**93.7%**	**90.1%**	**91.5%**	**94.5%**	**92.4%**	**91.1%**	**88.3%**	**88.0%**	**94.5%**	**90.5%**	**89.2%**	**87.0%**	**87.6%**	**94.5%**	**89.6%**
y/y ch			2.7%	2.7%	0.4%	-3.5%	0.8%	-2.5%	-1.8%	-3.5%	0.0%	-1.9%	-1.9%	-1.3%	-0.4%	0.0%	-0.9%

Source: Jefferies estimates

Chart 42: Quarterly Pork Processing Spreads Projections

	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18e	2Q18e	3Q18e	4Q18e	1Q19e	2Q19e	3Q19e	4Q19e
Spot Prices																
Hog $/cwt	59.82	72.94	63.47	47.20	66.27	70.15	69.75	58.84	68.09	76.33	81.50	67.00	66.00	74.67	79.72	65.54
Pork $/cwt	74.69	83.00	80.35	75.20	81.60	86.33	89.82	78.64	80.78	85.63	89.35	77.79	82.42	86.70	91.41	77.34
Drop Value $/cwt	3.19	3.78	3.99	3.79	3.96	3.99	4.01	3.86	3.81	3.86	3.86	3.86	3.86	3.86	3.86	3.86
Margin Calc																
Profit $/head	**25.31**	**17.32**	**31.49**	**53.19**	**28.33**	**30.10**	**37.92**	**36.99**	**22.62**	**16.00**	**18.00**	**23.00**	**21.00**	**14.00**	**16.00**	**21.00**
(+) Pork	149.22	165.84	160.53	150.26	163.04	172.48	179.46	157.13	161.39	171.09	178.53	155.43	164.68	173.22	182.64	154.52
(+) Drop Value	8.61	10.21	10.77	10.23	10.69	10.77	10.82	10.42	10.29	10.42	10.42	10.42	10.42	10.42	10.42	10.42
(-) Hog	119.52	145.73	126.81	94.30	132.40	140.15	139.36	117.56	136.05	152.51	162.84	133.87	131.87	149.18	159.28	130.94
(-) Fixed Cost	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00

Source: Bloomberg, USDA, Jefferies estimates

Chart 43: Annual Pork Processing Spreads Projections

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018E	2019E
(+) Pork $/head	107.32	117.48	147.09	139.54	134.90	134.83	137.56	116.43	162.53	187.69	168.60	183.09	220.61	156.81	156.46	168.03	169.37	168.76
(+) Drop Value $/cwt	6.70	7.46	9.33	9.14	8.77	10.21	12.39	11.18	12.31	14.27	14.80	15.19	16.08	9.71	9.95	10.67	10.42	10.42
(-) Hog $/head	90.71	104.05	138.86	132.98	124.79	124.85	126.81	110.88	144.86	173.90	165.48	172.48	205.42	132.19	121.59	132.37	146.79	148.19
(-) Fixed Cost	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00
Profit $/head	**10.30**	**7.88**	**4.56**	**2.70**	**5.89**	**7.18**	**10.14**	**3.73**	**16.98**	**15.06**	**4.92**	**12.79**	**18.27**	**21.32**	**31.83**	**33.33**	**20.00**	**18.00**
Profit c/lb live	3.8	2.9	1.7	1.0	2.2	2.7	3.8	1.4	6.3	5.6	1.8	4.7	6.8	7.9	11.4	11.9	7.1	6.4
EBIT margin	**9.6%**	**6.7%**	**3.1%**	**1.9%**	**4.4%**	**5.3%**	**7.4%**	**3.2%**	**10.4%**	**8.0%**	**2.9%**	**7.0%**	**8.3%**	**13.6%**	**20.3%**	**19.8%**	**11.8%**	**10.7%**
y/y change																		
(+) Pork		9%	25%	-5%	-3%	0%	2%	-15%	40%	15%	-10%	9%	20%	-29%	0%	7%	1%	0%
(+) Drop Value		11%	25%	-2%	-4%	16%	21%	-10%	10%	16%	4%	3%	6%	-40%	3%	7%	-2%	0%
(-) Hog		15%	33%	-4%	-6%	0%	2%	-13%	31%	20%	-5%	4%	19%	-36%	-8%	9%	11%	1%
Capacity/Utilization																		
Capacity - daily max slaughter					425,645	432,720	442,038	442,676	442,676	442,676	442,676	442,676	442,676	450,611	450,865	458,800	492,189	502,000
Production - dail actual slaughter					366,212	381,719	407,175	397,266	385,524	387,623	395,676	391,877	373,692	403,585	413,297	424,151	445,422	449,758
Utilization Rate					86%	88%	92%	90%	87%	88%	89%	89%	84%	90%	92%	92%	90%	90%
y/y change																		
Capacity - daily max slaughter						2%	2%	0%	0%	0%	0%	0%	0%	2%	0%	2%	7%	2%
Production - dail actual slaughter						4%	7%	-2%	-3%	1%	2%	-1%	-5%	8%	2%	3%	5%	1%
Utilization Rate						3%	4%	-3%	-3%	1%	2%	-1%	-5%	6%	2%	1%	-2%	-1%

Source: Bloomberg, USDA, Jefferies estimates

We are increasing our estimates for HRL's Refrigerated Foods segment EBIT and our estimates now look somewhat conservative. Management is guiding to a LSD increase in Refrigerated Foods EBIT in FY18. We estimate that the recent acquisitions of Fontanini & Columbus acquisitions should be ~18% (incl. synergies) additive to Ref. Foods EBIT growth in FY18, which implies that management is expecting base business to decline by ~16%. We now believe the 16% decline in base business EBIT is appropriately

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conservative given our view on commodity packer margins. HRL is expecting a LSD increase in hog prices in 2018 and commented that forecasts range from MSD-HSD increases. We are expecting a ~11% increase (down from 20% before). If hog prices increase more than management is expecting, there could be downside to their Refrigerated Foods EBIT guidance. Also, the composition of the cutout has implications on HRL's guidance – lower belly and trim prices are good for the company. Although there are quite a few variables that make it hard to model segment EBIT, we continue to believe our "commodity margin plus" framework makes the most sense. Accounting for the recent acquisitions, we estimate HRL should earn ~$30/head ($18 prior to Fontanini & Columbus acquisitions) above the commodity margin. Our new estimates assume HRL will earn ~$29/head above commodity packer margin in FY18. Every $1/head change in our margin assumption implies $0.016/share to EPS.

Updating estimates. We are increasing our FY18 EPS estimate from $1.60 to $1.86, primarily reflecting a lower tax rate ($0.24 benefit) and higher Refrigerated Foods segment EBIT ($0.02). We note that our revised estimates are well above consensus and mgmt's guidance given that our estimates reflect the US tax legislation while consensus and mgmt. guidance does not. As for FY19, our EPS estimate is going up to $2.00 from $1.72 primarily driven by our lower tax rate assumption.

1Q18 earnings preview. HRL is scheduled to report 1Q18 earnings on 2/22/18, however we note that despite the proximity of our upgrade to earnings, we are not making a specific call (positive or negative) into the quarter. We expect the company to meet or beat our 1Q EPS estimate of $0.49, which takes into account our estimate for the expected positive impact from US tax reform. We note that consensus' 1Q EPS estimate currently stands at $0.43 but we believe most estimates on the Street do not yet reflect the impact from tax reform (for perspective, our consolidated 1Q18 EBIT estimate of $334M is roughly in line with consensus). Our 1Q estimates assume ~8% y/y sales growth (~6% driven by Fontanini and Columbus acquisitions) and a ~2% y/y decline in adj. EBIT driven (driven mainly by Refrig. Foods, albeit to a lesser extent than our previous estimates).

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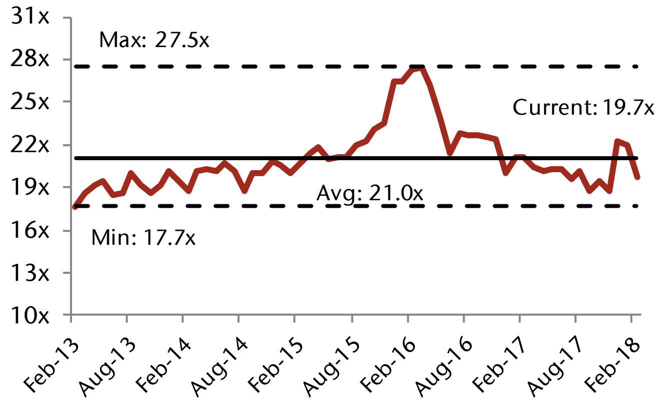
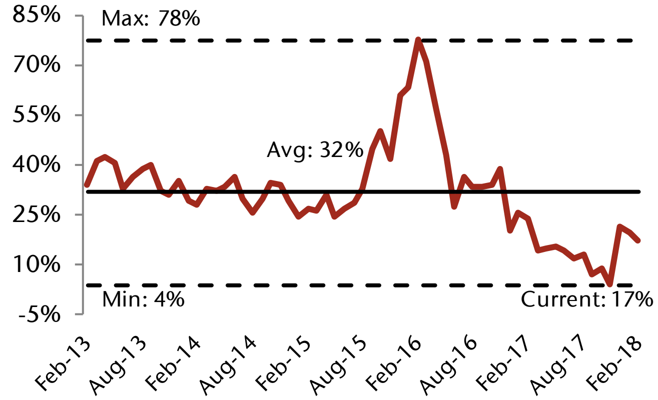
Chart 44: Historical P/E



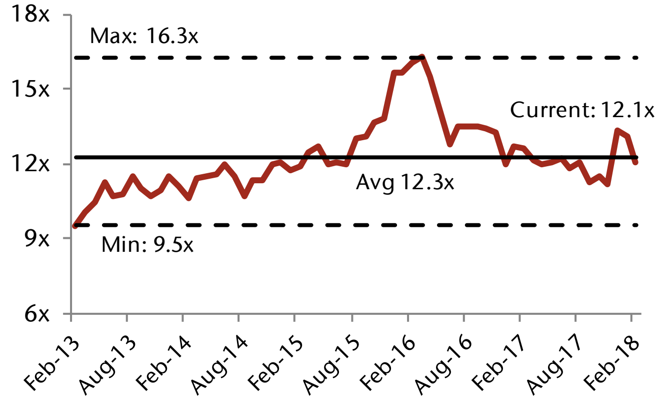
Source: FactSet

Chart 45: P/E Premium/Discount Relative to S&P 500



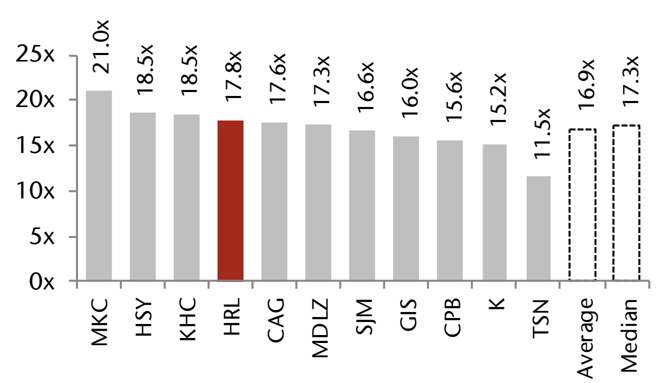
Source: FactSet

Chart 46: Historical EV/EBITDA



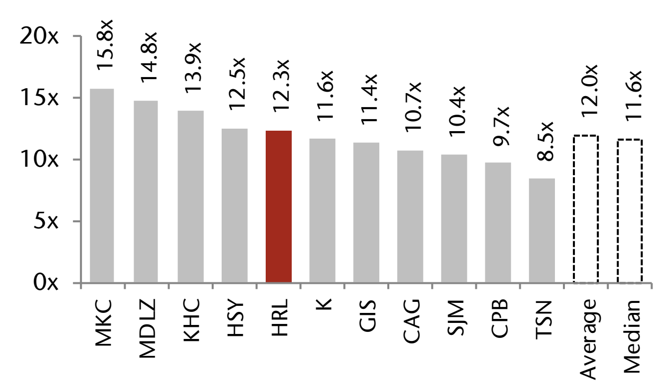
Source: FactSet

Chart 47: NTM P/E vs. Peers



Source: FactSet, Jefferies estimates

Chart 48: EV/EBITDA vs. Peers



Source: FactSet, Jefferies estimates

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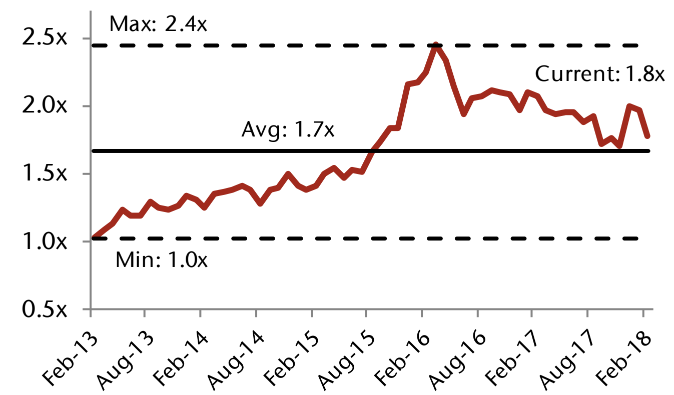
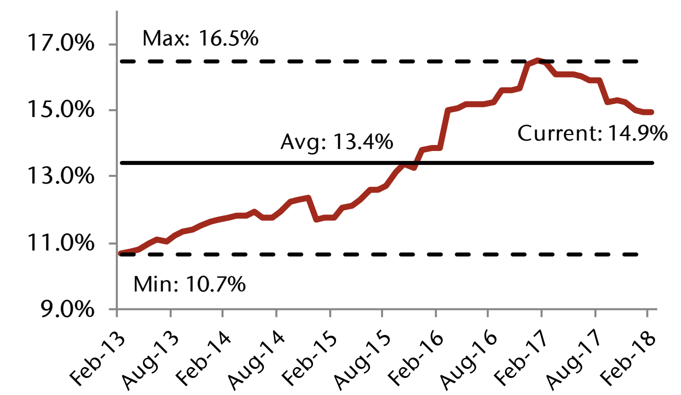
Chart 49: EV/Sales



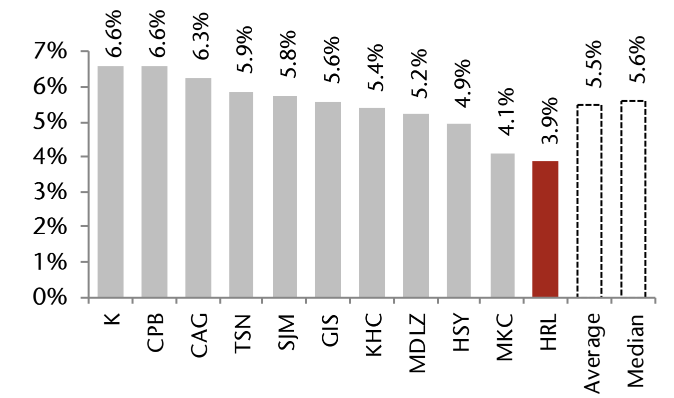
Source: FactSet

Chart 50: EBITDA/Sales



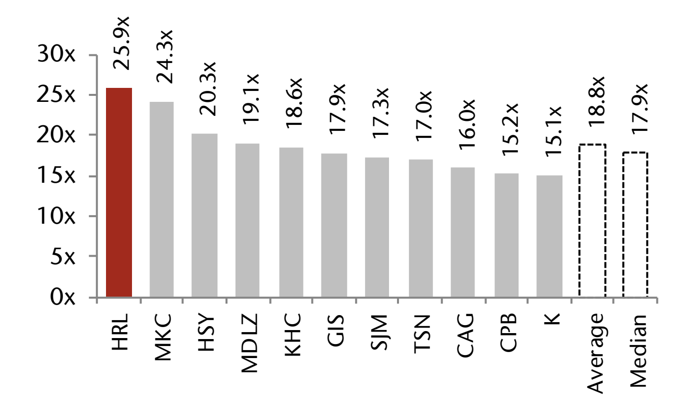
Source: FactSet

Chart 51: Free Cash Flow Yield vs. Peers



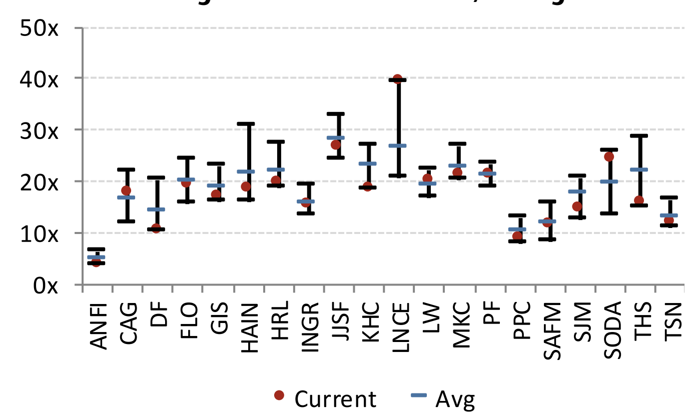
Source: FactSet, Jefferies estimates

Chart 52: Free Cash Flow Multiple vs. Peers



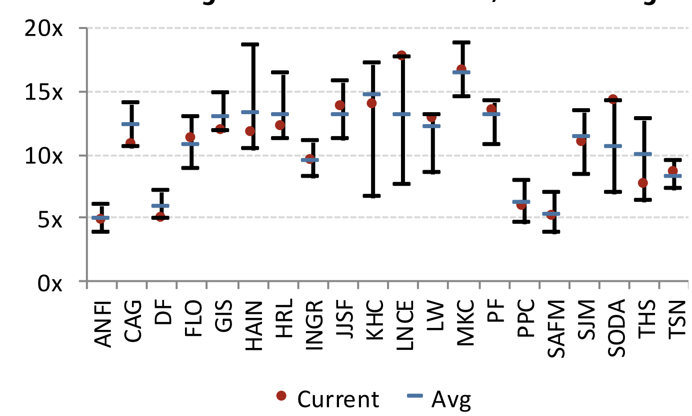
Source: FactSet, Jefferies estimates

Chart 53: Coverage Universe Historical P/E Range



Source: FactSet

Chart 54: Coverage Universe Historical EV/EBITDA Range



Source: FactSet

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Chart 55: HRL - Financial Summary

Financial Summary	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18E	2Q18E	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
($ in millions)	Oct-14	Oct-15	Oct-16	Jan-17	Apr-17	Jul-17	Oct-17	Oct-17	Jan-18	Apr-18	Jul-18	Oct-18	Oct-18	Oct-19	Oct-20	Oct-21
Total Revenues	**9,316**	**9,264**	**9,523**	**2,280**	**2,187**	**2,207**	**2,493**	**9,168**	**2,459**	**2,384**	**2,428**	**2,635**	**9,906**	**10,295**	**10,674**	**11,068**
% change	6%	-1%	3%	-1%	-5%	-4%	-5%	-4%	8%	9%	10%	6%	8%	4%	4%	4%
Cost of Sales	7,751	7,455	7,365	1,728	1,700	1,755	1,981	7,164	1,891	1,865	1,934	2,088	7,777	8,002	8,201	8,407
Adjusted Gross Profit	**1,565**	**1,809**	**2,158**	**552**	**487**	**452**	**512**	**2,003**	**568**	**519**	**495**	**547**	**2,129**	**2,293**	**2,473**	**2,662**
SG&A	654	734	872	210	181	177	195	763	234	204	202	213	853	918	984	1,053
Adj. EBIT (ex. Equity Earnings)	**911**	**1,075**	**1,286**	**342**	**306**	**276**	**317**	**1,241**	**334**	**315**	**293**	**334**	**1,276**	**1,375**	**1,489**	**1,609**
% change	16%	14%	23%	-2%	-3%	3%	-10%	-4%	-2%	3%	6%	5%	3%	8%	8%	8%
Net Interest Expense	13	13	13	3	3	3	4	13	5	8	8	8	29	33	33	33
Adjusted EBITDA	1,041	1,208	1,418	373	338	308	352	1,371	365	352	332	376	1,426	1,543	1,669	1,801
Adjusted Net Income	606	687	892	235	211	183	218	847	266	246	224	263	999	1,075	1,166	1,261
Adjusted EPS	**$1.12**	**$1.32**	**$1.64**	**$0.44**	**$0.39**	**$0.34**	**$0.41**	**$1.57**	**$0.49**	**$0.46**	**$0.42**	**$0.49**	**$1.86**	**$2.00**	**$2.17**	**$2.34**
% change	15%	18%	24%	1%	-2%	-6%	-10%	-4%	14%	17%	23%	20%	18%	8%	8%	8%
Operating cash flow	746.9	992.0	992.8	177.6	83.5	250.3	498.7	1,010.2	151.5	148.6	258.9	555.9	1,114.8	1,220.0	1,321.6	1,427.9
Capex	(159.1)	(144.1)	(255.5)	(37.9)	(39.1)	(41.5)	(102.8)	(221.3)	(108.2)	(102.5)	(104.4)	(113.3)	(428.4)	(257.4)	(266.8)	(276.7)
Free cash flow	587.7	847.9	737.3	139.7	44.5	208.8	395.9	788.9	43.3	46.1	154.4	442.6	686.4	962.6	1,054.8	1,151.2
Net debt	(84.2)	87.8	(165.1)	(359.8)	(298.9)	(383.3)	(194.1)	(194.1)	624.7	679.5	625.9	284.2	284.2	(274.9)	(926.3)	(1,674.0)
Equity	3,612.1	4,001.4	4,451.4	4,575.3	4,686.4	4,753.2	4,939.7	4,939.7	5,093.5	5,238.5	5,361.8	5,523.6	5,523.6	6,195.1	6,957.5	7,814.8
# of diluted shares	540.4	541.0	542.5	540.1	539.6	538.8	538.0	539.1	538.0	538.0	538.0	538.0	538.0	538.0	538.0	538.0
Gross Margin (adjusted)	16.8%	19.5%	22.7%	24.2%	22.3%	20.5%	20.5%	21.9%	23.1%	21.8%	20.4%	20.8%	21.5%	22.3%	23.2%	24.0%
SG&A/sales	7.0%	7.9%	9.2%	9.2%	8.3%	8.0%	7.8%	8.3%	9.5%	8.6%	8.3%	8.1%	8.6%	8.9%	9.2%	9.5%
EBIT Margin (adjusted)	9.8%	11.6%	13.5%	15.0%	14.0%	12.5%	12.7%	13.5%	13.6%	13.2%	12.1%	12.7%	12.9%	13.4%	14.0%	14.5%
EBITDA Margin (adjusted)	11.2%	13.0%	14.9%	16.4%	15.5%	14.0%	14.1%	15.0%	14.9%	14.8%	13.7%	14.3%	14.4%	15.0%	15.6%	16.3%
FCF Margin	6.3%	9.2%	7.7%	6.1%	2.0%	9.5%	15.9%	8.6%	1.8%	1.9%	6.4%	16.8%	6.9%	9.4%	9.9%	10.4%
Tax rate	34.3%	35.0%	32.3%	33.7%	33.2%	34.3%	33.8%	33.7%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%	23.0%
Net debt/TTM EBITDA	-0.1x	0.1x	-0.1x	-0.3x	-0.2x	-0.3x	-0.1x	-0.1x	0.5x	0.5x	0.4x	0.2x	0.2x	-0.2x	-0.6x	-0.9x
Net debt/cap	-2%	2%	-4%	-9%	-7%	-9%	-4%	-4%	11%	11%	10%	5%	5%	-5%	-15%	-27%
ROIC	14.8%	14.9%	17.4%	17.2%	16.2%	16.1%	15.4%	15.4%	14.6%	14.8%	15.4%	15.8%	15.8%	14.7%	14.5%	14.2%

Source: Jefferies estimates, company data

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Jefferies

Chart 56: HRL - Segment Summary

Segment Summary	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18E	2Q18E	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
Revenues																
Grocery Products	1,558.3	1,617.7	1,684.8	417.7	432.2	422.0	489.2	1,761.1	432.4	447.3	436.8	499.0	1,815.4	1,869.9	1,926.0	1,983.7
% change	2.7%	3.8%	4.1%	6.5%	7.7%	5.7%	-0.5%	4.5%	3.5%	3.5%	3.5%	2.0%	3.1%	3.0%	3.0%	3.0%
Refrigerated Foods	4,644.2	4,372.3	4,647.2	1,123.0	1,027.5	1,086.5	1,166.7	4,403.7	1,281.0	1,186.0	1,257.1	1,263.8	4,988.0	5,162.6	5,317.5	5,477.0
% change	9.2%	-5.9%	6.3%	-3.4%	-5.9%	-6.0%	-5.7%	-5.2%	14.1%	15.4%	15.7%	8.3%	13.3%	3.5%	3.0%	3.0%
Jenny-O Turkey Store	1,672.5	1,635.8	1,741.0	421.0	388.2	369.1	484.9	1,663.2	404.1	388.2	372.8	499.4	1,664.6	1,731.1	1,800.4	1,872.4
% change	4.4%	-2.2%	6.4%	13.1%	-8.3%	-8.6%	-10.4%	-4.5%	-4.0%	0.0%	1.0%	3.0%	0.1%	4.0%	4.0%	4.0%
Specialty Foods	907.1	1,103.4	939.1	192.6	208.2	196.9	196.8	794.5	183.0	206.1	198.8	198.8	786.7	833.9	884.0	937.0
% change	-2.7%	21.6%	-14.9%	-19.0%	-23.6%	-7.2%	-9.2%	-15.4%	-5.0%	-1.0%	1.0%	1.0%	-1.0%	6.0%	6.0%	6.0%
International & Other	534.2	534.7	511.2	125.8	131.2	132.9	155.1	545.0	158.3	156.0	163.0	174.3	651.6	697.2	746.0	798.2
% change	19.2%	0.1%	-4.4%	-2.1%	19.0%	1.0%	10.1%	6.6%	25.8%	18.9%	22.6%	12.4%	19.6%	7.0%	7.0%	7.0%
Total Revenues	**9,316.3**	**9,263.9**	**9,523.2**	**2,280.2**	**2,187.3**	**2,207.4**	**2,492.6**	**9,167.5**	**2,458.8**	**2,383.7**	**2,428.5**	**2,635.2**	**9,906.3**	**10,294.8**	**10,673.8**	**11,068.4**
% of Total																
Grocery Products	16.7%	17.5%	17.7%	18.3%	19.8%	19.1%	19.6%	19.2%	17.6%	18.8%	18.0%	18.9%	18.3%	18.2%	18.0%	17.9%
Refrigerated Foods	49.9%	47.2%	48.8%	49.3%	47.0%	49.2%	46.8%	48.0%	52.1%	49.8%	51.8%	48.0%	50.4%	50.1%	49.8%	49.5%
Jenny-O Turkey Store	18.0%	17.7%	18.3%	18.5%	17.7%	16.7%	19.5%	18.1%	16.4%	16.3%	15.3%	19.0%	16.8%	16.8%	16.9%	16.9%
Specialty Foods	9.7%	11.9%	9.9%	8.4%	9.5%	8.9%	7.9%	8.7%	7.4%	8.6%	8.2%	7.5%	7.9%	8.1%	8.3%	8.5%
International & Other	5.7%	5.8%	5.4%	5.5%	6.0%	6.0%	6.2%	5.9%	6.4%	6.5%	6.7%	6.6%	6.6%	6.8%	7.0%	7.2%
EBIT																
Grocery Products	195.1	239.1	268.5	65.6	77.5	58.8	88.9	290.8	71.2	83.6	65.2	95.7	315.6	325.1	334.8	344.9
EBIT margin	12.5%	14.8%	15.9%	15.7%	17.9%	13.9%	18.2%	16.5%	16.5%	18.7%	14.9%	19.2%	17.4%	17.4%	17.4%	17.4%
% change	-8.7%	22.6%	12.3%	0.5%	15.5%	10.2%	7.5%	8.3%	8.4%	7.8%	10.9%	7.6%	8.5%	3.0%	3.0%	3.0%
bps change	-156 bp	226 bp	115 bp	-93 bp	121 bp	57 bp	135 bp	58 bp	75 bp	75 bp	100 bp	100 bp	87 bp	0 bp	0 bp	0 bp
Refrigerated Foods	338.0	425.0	585.7	173.8	130.2	138.3	145.6	587.9	162.3	133.1	147.1	153.3	595.8	660.8	724.9	791.3
EBIT margin	7.3%	9.7%	12.6%	15.5%	12.7%	12.7%	12.5%	13.4%	12.7%	11.2%	11.7%	12.1%	11.9%	12.8%	13.6%	14.4%
% change	45.3%	25.7%	37.8%	4.1%	0.1%	14.6%	-13.3%	0.4%	-6.6%	2.2%	6.4%	5.3%	1.3%	10.9%	9.7%	9.2%
bps change	181 bp	244 bp	288 bp	111 bp	77 bp	228 bp	-110 bp	75 bp	-280 bp	-145 bp	-103 bp	-35 bp	-141 bp	85 bp	83 bp	82 bp
Jenny-O Turkey Store	272.4	276.2	329.4	68.2	63.8	45.0	70.4	247.3	60.5	59.1	43.9	72.3	235.6	255.2	285.0	316.5
EBIT margin	16.3%	16.9%	18.9%	16.2%	16.4%	12.2%	14.5%	14.9%	15.0%	15.2%	11.8%	14.5%	14.2%	14.7%	15.8%	16.9%
% change	22.6%	1.4%	19.3%	-25.3%	-28.9%	-19.9%	-23.8%	-24.9%	-11.3%	-7.4%	-2.5%	2.7%	-4.7%	8.3%	11.7%	11.1%
bps change	242 bp	60 bp	204 bp	-834 bp	-474 bp	-171 bp	-253 bp	-405 bp	-124 bp	-122 bp	-42 bp	-4 bp	-71 bp	58 bp	109 bp	107 bp
Specialty Foods	71.5	105.9	110.9	26.7	30.8	23.3	15.9	96.8	28.2	33.6	26.6	19.1	107.4	113.8	120.6	127.9
EBIT margin	7.9%	9.6%	11.8%	13.9%	14.8%	11.9%	8.1%	12.2%	15.4%	16.3%	13.4%	9.6%	13.6%	13.6%	13.6%	13.6%
% change	-19.5%	48.1%	4.7%	-0.2%	-16.4%	-13.9%	-21.1%	-12.7%	5.3%	9.0%	13.8%	19.7%	10.9%	6.0%	6.0%	6.0%
bps change	-165 bp	172 bp	221 bp	262 bp	127 bp	-91 bp	-122 bp	38 bp	150 bp	150 bp	150 bp	150 bp	146 bp	0 bp	0 bp	0 bp
International & Other	84.7	87.9	78.4	25.5	19.6	17.1	23.1	85.3	31.3	22.5	20.2	25.1	99.1	107.4	116.4	126.2
EBIT margin	15.9%	16.4%	15.3%	20.2%	15.0%	12.9%	14.9%	15.7%	19.7%	14.5%	12.4%	14.4%	15.2%	15.4%	15.6%	15.8%
% change	18.5%	3.7%	-10.8%	4.8%	37.7%	-15.7%	18.1%	8.8%	22.7%	14.9%	17.9%	8.6%	16.1%	8.4%	8.4%	8.4%
bps change	-9 bp	57 bp	-109 bp	133 bp	204 bp	-256 bp	101 bp	31 bp	-50 bp	-50 bp	-50 bp	-50 bp	-45 bp	20 bp	20 bp	20 bp
Corporate and other expenses	(33.4)	(35.2)	(48.4)	(4.6)	(5.8)	(2.9)	(14.8)	(28.1)	(5.0)	(6.3)	(5.6)	(18.3)	(35.2)	(41.2)	(42.7)	(44.3)
As % of revenues	0.4%	0.4%	0.5%	0.2%	0.3%	0.1%	0.6%	0.3%	0.2%	0.3%	0.2%	0.7%	0.4%	0.4%	0.4%	0.4%
Total Adj. EBIT (incl. Equity	**961.7**	**1,134.1**	**1,372.9**	**359.8**	**321.9**	**282.5**	**343.9**	**1,308.2**	**353.4**	**331.8**	**302.9**	**365.5**	**1,353.5**	**1,462.3**	**1,581.7**	**1,706.6**
% of Total																
Grocery Products	20.3%	21.1%	19.6%	18.2%	24.1%	20.8%	25.9%	22.2%	20.1%	25.2%	21.5%	26.2%	23.3%	22.2%	21.2%	20.2%
Refrigerated Foods	35.1%	37.5%	42.7%	48.3%	40.4%	49.0%	42.3%	44.9%	45.9%	40.1%	48.6%	42.0%	44.0%	45.2%	45.8%	46.4%
Jenny-O Turkey Store	28.3%	24.4%	24.0%	18.9%	19.8%	15.9%	20.5%	18.9%	17.1%	17.8%	14.5%	19.8%	17.4%	17.5%	18.0%	18.5%
Specialty Foods	7.4%	9.3%	8.1%	7.4%	9.6%	8.3%	4.6%	7.4%	8.0%	10.1%	8.8%	5.2%	7.9%	7.8%	7.6%	7.5%
International & Other	8.8%	7.7%	5.7%	7.1%	6.1%	6.1%	6.7%	6.5%	8.8%	6.8%	6.7%	6.9%	7.3%	7.3%	7.4%	7.4%

Source: Jefferies estimates, company data

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General Mills (GIS)
Upgrading to Buy & Raising PT to $63

Key Takeaway

We are upgrading to a Buy with a $63 PT based on our extensive work as part of our 'BSM' report. Although GIS has faced several challenges over the past few years (especially related to top-line growth), we believe the company has significantly enhanced its capabilities (people & process) and refined its strategy such that it can unlock meaningful value from its underappreciated portfolio of leading brands, especially in the emerging e-Commerce channel.

BSM project supports our upgrade. Following our deep-dive collaborative project with Accenture and Barkley, we feel better about large food brands' potential to remain relevant and succeed in the marketplace (with the right investments). As it relates to GIS specifically, although the company has faced meaningful challenges over the last few years (mainly related to share loss and weak top-line growth), we believe the company has significantly enhanced its capabilities (people & processes) and refined its strategy such that it can unlock substantial value from its underappreciated portfolio of leading brands. We are particularly optimistic about GIS's growth prospects in the e-Commerce channel, where we believe its category management knowledge, combined with a portfolio of well-recognized brands, will result in industry-leading penetration.

Margin upside could be significant if recent sales inflection sustains. Investors are skeptical about GIS' margin targets given recent underperformance & extended period of gross margin declines (down 330 bps over 6 years). We believe the decline in sales has masked strong performance & momentum on net productivity & lowering SG&A costs. If the recent sales growth inflection can be sustained (turned positive in 2Q18 for the first time in 10 qtrs), we think margins could surprise to the upside, however we acknowledge that mgmt's FY18 guidance implies a meaningful improvement in back half earnings growth, potentially representing a NT risk. We believe most of the downside risk is already priced into the stock and note that our upgrade to Buy is not predicated on NT earnings growth inflection.

Current valuation looks attractive. Consensus EPS contains some noise related to the recent US tax law changes (included in some estimates, but not others). As such, we prefer to look at the valuation on an EV/EBITDA basis. On this metric, the stock currently trades ~8% below its 5-year average and at a 5% discount to its large cap packaged food peers (compared to an average discount of 1% over the last 5 years). Our $63 PT simply assumes a reversion to the mean in terms of EV/EBITDA multiple and does not account for any future M&A, which could represent further upside to our estimate. Our EBIT projections are generally ahead of consensus which we believe is mainly attributable to our slightly more optimistic outlook on sales growth potential.

We view M&A as a "free" option. We believe GIS is well-positioned for a transformative deal. As an illustrative example, we show that a hypothetical acquisition of HAIN (at $60/shr) would not only make strategic sense but would be ~10% (39c/share) accretive to EPS by year 3. Conversely, if GIS' execution issues persist, we see the possibility of a buyout increasing & we show that a hypothetical buyout by KHC (at~$70/shr or 28% premium) would be significantly (DD) accretive to KHC's earnings.

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Valuation/Risks

GIS currently trades at 11.4x our NTM EBITDA estimate, or a ~5% discount to its large-cap packaged food peers. Our $63 PT assumes an EV/EBITDA multiple of 12.4x our FY19 estimates, in line with the stock's 5-year average and at a ~4% premium to its large-cap food peers.

Risks include: 1) High exposure to some secularly challenged categories; 2) execution missteps related to new growth initiatives; & 3) increases in competition.

Investment Summary

Significant Cost-Cutting Initiatives Are Already Underway & Seem To Be Tracking Ahead Of Expectations

Management expects to achieve $700M in gross annual savings (~4.5% of sales) by FY18. At the beginning of FY15, management originally announced a goal to generate $350M in gross annual savings by the end of FY17. Since then, cost savings delivery has come in faster than expected and the company has raised its total cost-savings target numerous times. Currently, management expects to generate ~$700M (cumulative) in gross annual savings by the end of FY18. The cost-savings initiative is comprised of 3 sub-projects:

- *Project Century* – special projects to streamline GIS' North American supply chain and reduce overhead costs
- *Project Catalyst* – includes the elimination of at least 700-800 positions across the US and lowering other SG&A expenses
- *Project Compass* – initiative to streamline GIS' international organization structure

On an absolute basis, GIS' gross cost-savings delivery compares favorably to its packaged food peers. We looked at 12 packaged food companies with notable cost-savings programs / near-term synergy opportunities and compared their cost-savings delivery over their most recent fiscal years. GIS ranked fifth (above-average) in terms of absolute cost savings generated over the past fiscal year and third on a percentage of sales basis. In other words, the company's cost-cutting efforts compare favorably to its packaged food peers, which we would expect to continue going forward.

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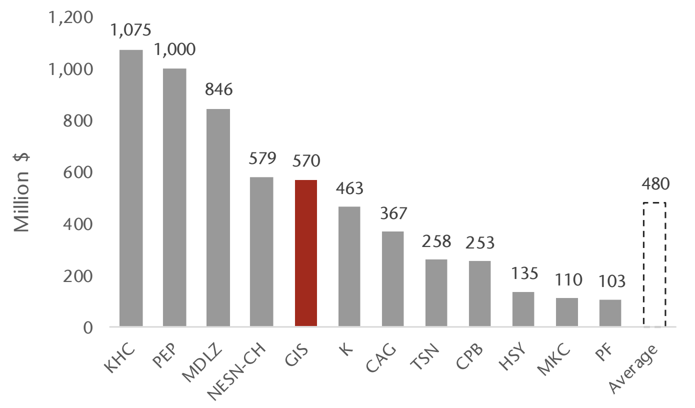
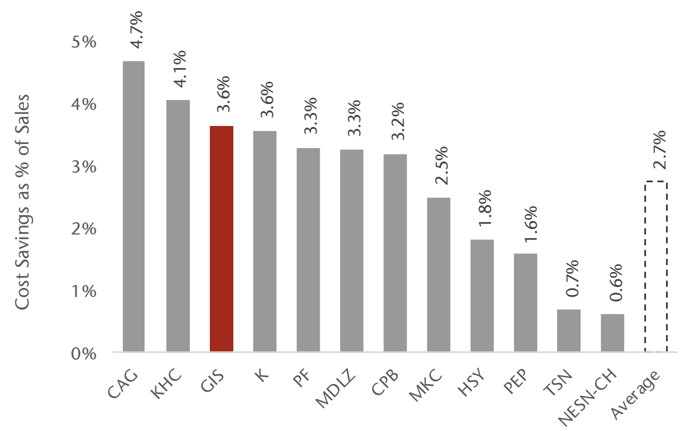
Chart 57: Cost Savings / Synergies Captured – Last FY



Source: Company data, Jefferies estimates

Note: Cost-savings shown above Include cost-cutting programs as well as ongoing productivity initiatives

Chart 58: Cost Savings / Synergies as % of sales – Last FY



Source: Company data, Jefferies estimates

However, dropping realized cost-savings to the bottom line has been more of a challenge for the company. While GIS' absolute cost savings are comfortably above-average relative to the 12-company group we analyzed, the company has had a tougher time converting those savings into actual profit growth. To measure this, we looked at the ratio of the year-over-year change in EBIT (in absolute dollars) to the absolute amount of (gross) cost-savings generated during the past fiscal year. We believe this approach serves as a reasonable (and less subjective) proxy for each company's recent success at dropping cost savings to the bottom line. On this metric, GIS actually ranked lowest out of our 12-company group suggesting that cost-savings flow-through has been a challenge. We attribute GIS' lower cost-savings conversion primarily to its significant top-line growth headwinds, which have been more severe than many of its large-cap peers. The volume de-leveraging impact of GIS' weak sales growth seems to have offset most if not all of the company's cost-savings benefit. As such, we believe GIS will need to drive better sales growth trends in order to grow absolute EBIT dollars. In the next section of this report, we outline some of the initiatives management currently has underway to address the company's sales growth struggles.

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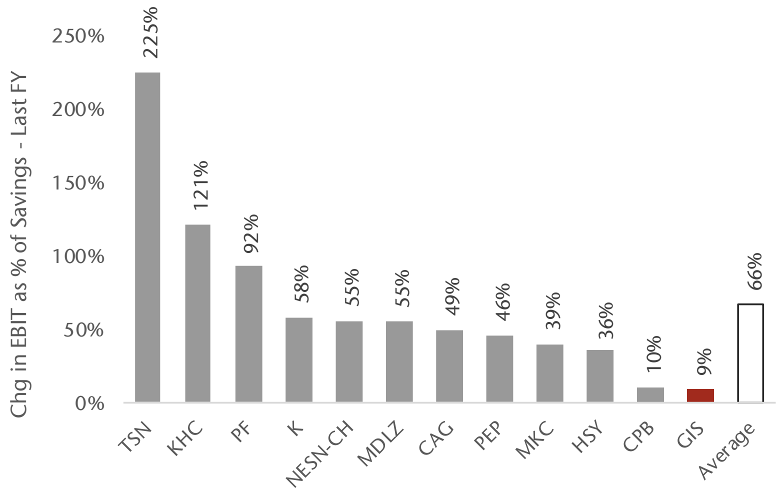
Chart 59: GIS has lagged most of its peers in terms of converting cost-savings into absolute profit growth



Source: Company data, Jefferies estimates

Despite generating robust productivity savings (net of inflation) gross margins have been on a downward trend. Productivity from the company's HMM program (mainly captured in COGS and not including incremental savings announced since FY15) has averaged ~2.3% of sales or cumulative ~900 bps over the last 4 years (period over which data was readily available). The goal of the program is to offset commodity inflation and it has more than achieved that goal as productivity has exceeded commodity inflation which has averaged 1.5% of sales or cumulative ~600 bps over the last 4 years. In other words, net productivity has been additive to margins by ~80 bps/year over each of the last 4 years. However, gross margins over that period are down ~5 bps/year implying a ~80 bps headwind from other factors (mix and volume being the main ones).

Company has done an outstanding job of lowering SG&A costs. In addition to the productivity initiatives outlined above GIS has reduced costs by another ~1% of sales each year since FY15. We don't know precisely how much of these savings come from the SG&A line but it is fair to assume that at least a portion of it is focused on reducing SG&A. Since FY12, SG&A costs are down ~$570M (or 17%) driven $290M (or 32%) by lower advertising, $253M (or 11%) by lower SG&A ex advertising & R&D and $27M (or 11% CAGR) by lower R&D costs. We point out that the reductions in SG&A ex-advertising & R&D have gained steam in recent years - down 8.5% in FY17, down 5% in FY16 compared to 2% CAGR over last 5 years.

Comparing GIS' cost structure to industry peers suggests the opportunity to lower costs further is still significant. Relative to nine other large-cap packaged food stocks we compared, GIS's SG&A/sales ratio lies fairly close to the group average. We do not view the cost structure as being "bloated" in any way and the company has already eliminated a fair amount of costs over the past several years. However, when compared to KHC, which is commonly seen as the benchmark in terms of running a large packaged food company with a lean cost structure, GIS seems to have plenty of room for further cost reduction. In particular, we note that GIS' total SG&A/sales of ~18% is some ~600 bps higher than KHC's and SG&A (excluding advertising & promotions) / sales is about 500 bps higher. We do not expect GIS' cost structure to mimic KHC's anytime soon;

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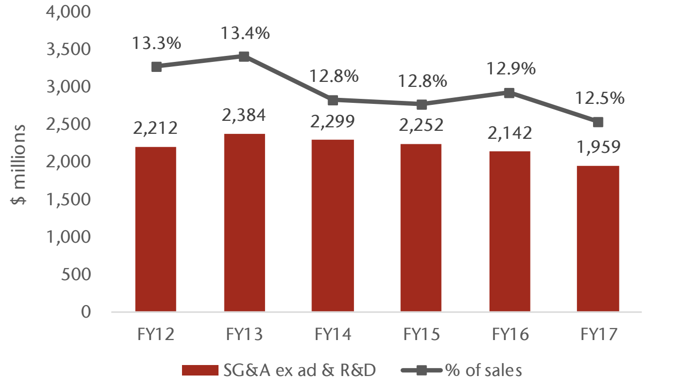
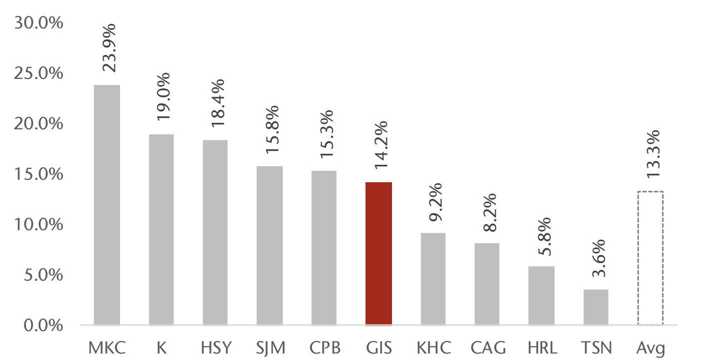
however, our analysis does at least give us some confidence that a sizable opportunity to lower SG&A expenses further still exists.

Chart 60: GIS' SG&A (ex A&P & R&D)/Sales Has Come Down



Source: Company data, Jefferies estimates

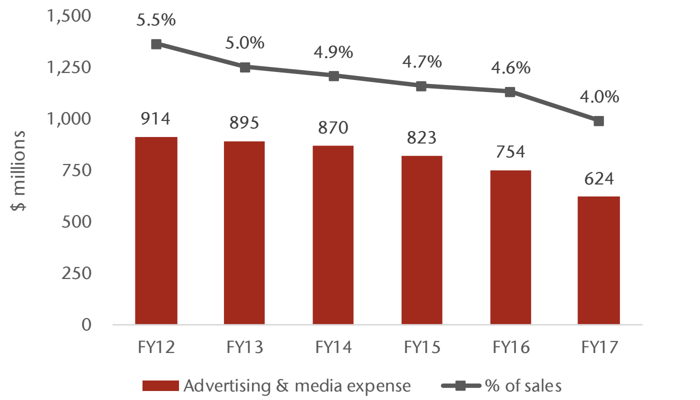
Chart 61: ..But There Is More Room To Lower Costs (SG&A(ex. A&P)/Sales Comparison - Last FY)



Source: Company data, Jefferies estimates

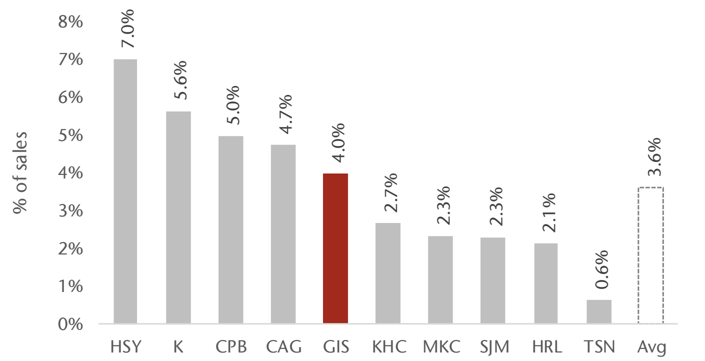
Advertising expense has been a major source of savings in the past. GIS' advertising and media expense has already been on a downward trajectory for at least five years – the company has lowered its total advertising spending by ~$290M or 32% since FY12. At the same time, the company's sales over that period are only down ~6%, which would seemingly imply that the company's advertising spending has become more efficient. When compared against a group including nine other large-cap food companies, GIS's advertising spending rate is slightly above average (4.0% of sales vs. 3.6% for the group; see Chart 16). Meanwhile the company's sales growth has largely underperformed the aforementioned group owing to its greater exposure to certain disadvantaged categories. As such, we would expect management to continue to focus on improving its advertising efficiency, which could be a key contributor to GIS' long-term margin expansion.

Chart 62: GIS Has Reduced Its Advertising Spending By ~$290M (32%) Over the Last 5 Years



Source: Company data

Chart 63: ...However, Advertising/Sales Remains Slightly Above Average Relative To Other Large-Cap Food Peers



Source: Company data, Jefferies estimates

All in, we conservatively model 120 bps of EBIT margin expansion over the next 5 years (FY17-22e). Our model assumes ~120 bps of EBIT margin expansion over

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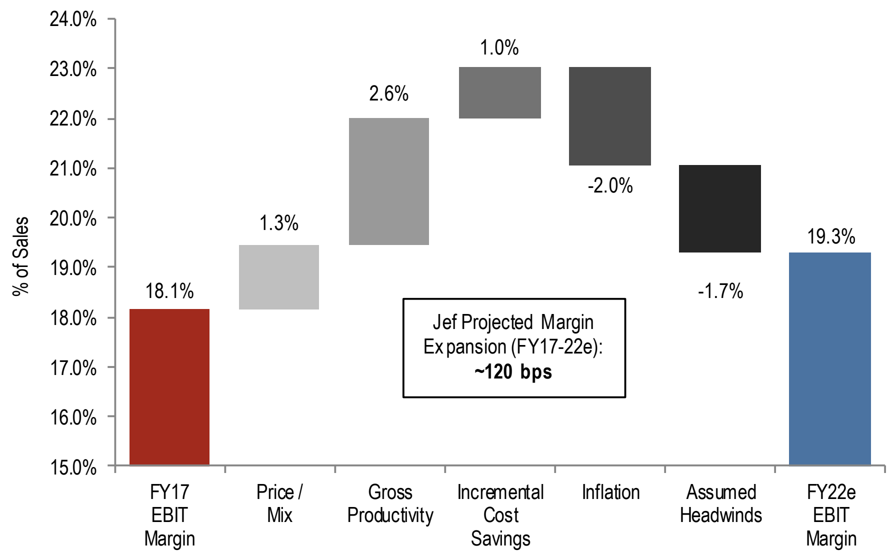
the next five years, from 18.1% in FY17 to 19.3% by the end of FY22. We expect margin expansion to be driven by continued price/mix gains, productivity gains net of inflation (via the company's HMM program) and incremental cost-saving initiatives that have already been announced (see Chart 17). We believe our assumptions will likely end up being conservative given that our margin expansion drivers do not assume any mix benefit from future M&A or any incremental cost-saving initiatives beyond what has already been announced/realized.

Chart 64: Jefferies' Projected EBIT Margin Expansion (FY17-22e)



Source: Jefferies estimates

We believe weak top-line growth trends have been the main reason why GIS has struggled to convert cost-savings into profit growth. GIS' recent organic sales growth trends have been significantly challenged, driven largely by share losses in yogurt and, to a lesser extent, RTE cereal. We believe the resulting volume deleverage and inefficient trade / advertising spend have masked most of the positive progress the company has already made on cutting costs.

Sales growth trends are improving – if GIS can sustain positive growth, we believe margin performance will improve meaningfully. Nielsen data suggests that the company's revenue management initiatives in the US may be starting to pay off. The data indicates that GIS' baseline velocity has improved meaningfully over the last ~8-9 months – specifically, after having been in negative territory for a good part of four years, baseline velocities in the US have shown positive y/y growth in each of the last nine Nielsen scanner periods and have mostly shown an accelerating trend (see Chart 66). At the same time, the company's y/y TDP (total distribution points) growth has seen fairly consistent sequential improvement since February 2017, which combined with better baseline velocities, may suggest that the company's US organic sales growth trends should continue to improve over the coming quarters.

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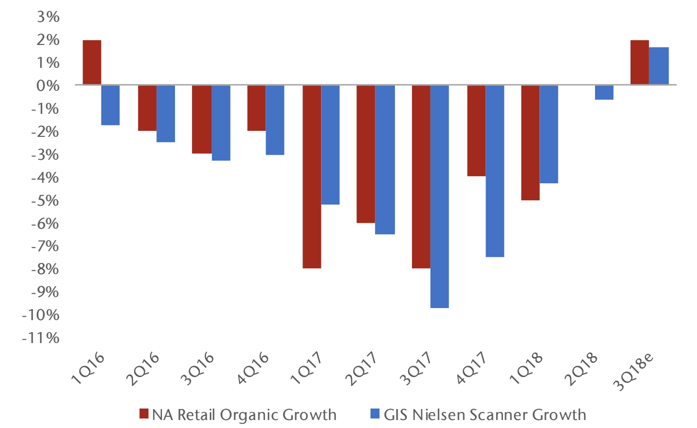
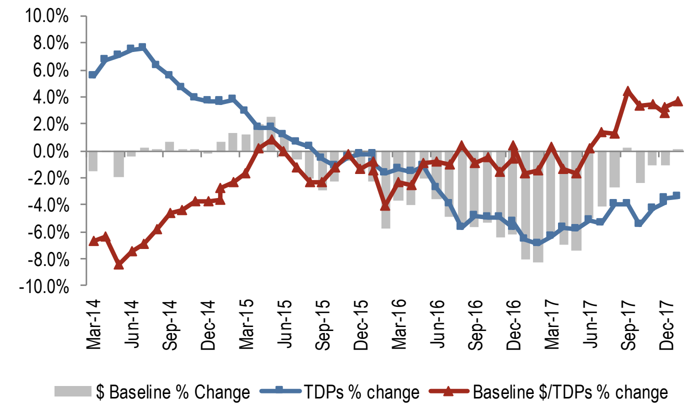
Chart 65: Scanner Data Showing Signs of Inflection



Source: Company data, Nielsen xAOC+C

Chart 66: Baseline velocity has improved in recent months



Source: Nielsen xAOC+C

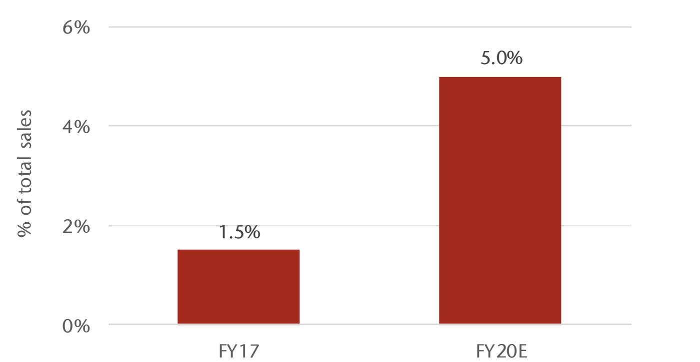
Ecommerce is A Meaningful Opportunity LT & We Expect GIS to Lead Industry Growth

Longer-term, we see eCommerce being a meaningful opportunity and expect GIS to lead the food industry in terms of penetrating the online channel. Of the large, publicly traded food companies, we believe GIS is likely the furthest along in terms of developing / implementing a comprehensive online growth strategy. The company already has a strategic partnership in place with Amazon and, encouragingly, GIS' online market share is substantially higher than its market share in brick and mortar, suggesting that the company has a healthy head start on its peers. Tech companies like Amazon have to rely heavily on the category management expertise of companies like GIS to tailor their technology to entice consumers to buy more online. Overall, GIS expects to grow its eCommerce business from ~1.5% of sales today to ~5% by FY20, which we estimate points to online sales of ~$750-800M in FY20 and implies a ~25-30% CAGR in eCommerce sales over the next three years (for perspective, the company reported that its US Retail e-commerce business was up 82% y/y in 1H18).

Chart 67: GIS Market Share Comparison – In-Store vs. Online

Source: Company presentation

Chart 68: GIS Projected eCommerce Sales As % Of Total



Source: Company presentation

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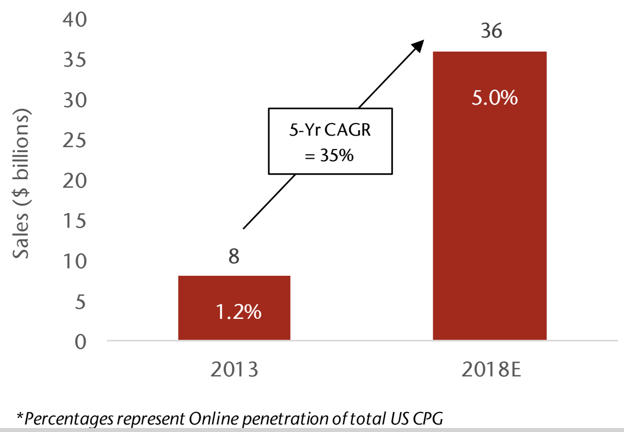
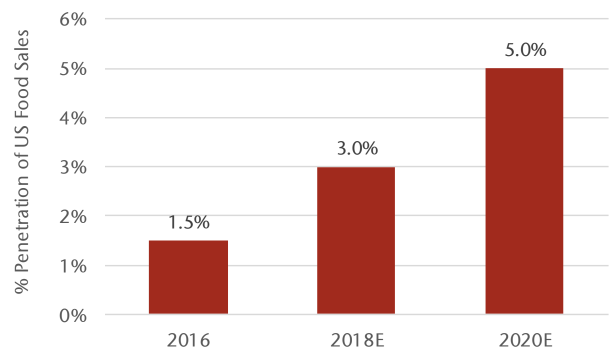
Chart 69: US CPG eCommerce Projected Sales Growth & Penetration



Source: GMA/BCG/Google/IRI Report – The Digital Future: A Game Plan For Consumer Packaged Goods (2014)

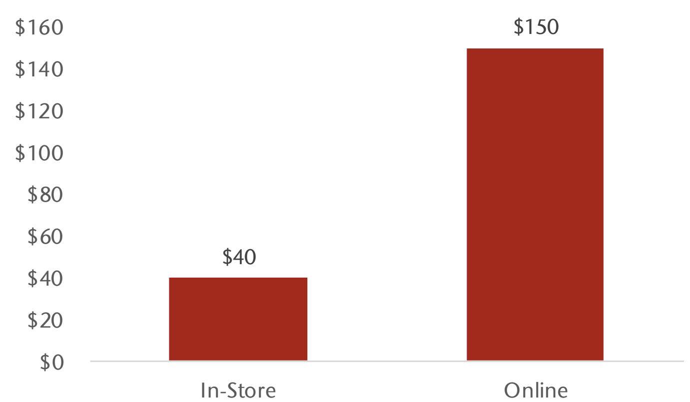
Chart 70: eCommerce Projected Share of US Food Sales



Source: Company presentation

GIS's differentiated eCommerce strategy focuses more on full basket sales rather than the "spear-fishing" approach most food companies currently employ. Our meetings with the new head of GIS's online business reaffirmed our belief that the company is an undisputed leader in e-commerce solutions in the food industry today. Most online food sales today occur in a "spear-fishing" manner, wherein consumers purchase single items (usually difficult to find in stores) and the basket size is small. However, GIS expects most of the growth in online food sales to come from consumers shifting their "stock-up" trips to online. On average, consumers' basket size online is much larger than offline ($150 vs. $40 in-store) because of the 'stock-up' nature. These stock-up trips favor large national brands because consumers typically go in knowing exactly what they want to buy and they usually gravitate towards the brands they know and trust. GIS's market shares on these stock-up online trips are much higher than offline.

Chart 71: US Average Grocery Purchase Size – In-Store vs. Online



Source: Company presentation

Contrary to what some may think, the gross margin profile for GIS' online business will likely be comparable to offline. Regarding margins on products sold

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through eCommerce, it is generally assumed that margins are lower than offline because prices are lower and distribution costs are much higher. For example, some industry observers have noted that the breakeven cost for CPG companies is $20/box while a study focused on distribution costs in the U.K. showed distribution costs as a percentage of sales to be anywhere from 10-30%, compared to 6-7% for offline product. According to GIS, its prices online are the same as offline (not allowed by law apparently to offer different prices by retailer) and although it is investing for future growth (infrastructure investments), gross margins are comparable, or at least will be, once the business achieves appropriate scale.

Significant M&A Optionality Remains & Is Not Adequately Priced In

Conservative acquisition strategy underpinned by desire to accelerate top-line growth. GIS has had a fairly acquisitive history but the company has not completed a sizable transaction for several years now. The last noteworthy transaction was Annie's Inc. back in October 2014 but the company has not completed a "transformational" deal since the Pillsbury deal in 2000. According to management, the company's M&A filter takes into account several considerations, including (but not limited to): 1) the deal's potential to take GIS deeper into global categories it's already in; 2) extendibility of acquired brands; 3) the acquired business' growth prospects in emerging markets; and 4) natural/organic positioning in the United States. Each of these considerations is aimed at accelerating GIS' top-line growth profile, which is a key priority for management. In the US, we would expect acquisitions to mainly target the natural/organic segment of the market where top-line growth remains robust. According to management, the company is well-positioned in the flow of information around the natural/organic space and it would be extremely unlikely for any deal to occur in that area without GIS having had prior knowledge that the asset was for sale. We note that management has set a target of achieving $1B in natural/organic sales by FY19, which implies a ~10% CAGR for the company's natural/organic business over the next two years.

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Chart 72: GIS Acquisition History – Last 20 Years

Announced Date	Completion Date	Acquired/ Sold Company	Product Category	EV ($MM)	Transaction Multiples (LTM Financials) EV/Sales	EV/EBITDA
6-Jan-16	6-Jan-16	Epic Provisions LLC	Natural and organic meat snacks, including meat, fruit and nut bars, jerky bites, pork skins, snack strips, hunt & harvest mix and bacon/chicken bits. EPIC's portfolio has also expanded to include bone broth and animal oils	na		
23-Dec-15	23-Dec-15	Carolina Administracao E Participaçoes Societarias Ltda.	Brazilian-based dairy products producer, including yogurt brands Carolina, Very Gurt and Gluck. The company markets more than 20 different dairy product lines in Brazil.	na		
19-Dec-14	19-Dec-14	Pinedale Holdings Pte. Ltd.	Singapore-based producer and distributor of ice-creams and other dairy products	11		
8-Sep-14	21-Oct-14	Annie's, Inc.	Natural and organic foods across several, large packaged food categories including meals, snacks, dressings, condiments and other	789	3.8x	35.2x
31-Dec-12	31-Dec-12	Immaculate Baking Co.	Ready-to-bake cookie dough made with all natural and organic ingredients and other wholesome treats including sweet rolls, biscuits and pie crusts	na		
24-May-12	1-Aug-12	Yoki Alimentos SA	Products include ready mixes, popcorn, condiments, snacks, teas, cake mixtures, desserts, soups, juice mixes, cereals, and flours.	990	1.9x	
9-May-12	9-May-12	Parampara Foods Pvt. Ltd.	India-based food manufacturer primarily engaged in the manufacturing and distribution of ready-to-cook spice and sauce mixes	na		
29-Feb-12	29-Feb-12	FoodShouldTasteGood, Inc.	Producer and marketer of cookies and related bakery products	na		
18-May-11	1-Jul-11	Yoplait SAS	Milk and dairy products including butter, cheese and yogurt. Yoplait SAS also sells products under the brand names Petit Yoplait, Petits Filous, Calin, Yop, Parle de Laitt, Frutos, Crème Fraîche, and Yaourt Nature Sucré	1,136	2.3x	
12-Dec-10	30-Apr-11	The Pasta Master Pty Ltd.	Chilled Italian meals, pasta and sauces	na		
21-Nov-10	22-Feb-11	Mountain High Yoghurt	All-natural yogurt	na		
30-Jun-08	31-Dec-08	HD Distributors (Thailand) Co. Ltd.	Thailand-based marketer of Haagen-Dazs ice creams	1		
10-Jun-08	31 May '09	Humm Foods, Inc.	Producer of Larabar natural and organic fruit and nut bars	na		
11-Jan-07	11-Jan-07	Saxby Bros Ltd.	UK-based producer of branded and own-label chilled pastry ingredients	21		
31-Oct-05	31-Oct-05	Majority stake in Pinedale Holdings P	Singapore-based producer and distributor of ice-creams and other dairy products	3		
24-Jul-03	24-Jul-03	Haagen-Dazs Taiwan Ltd.	Taiwan-based subsidiary of Haagen-Dazs ice cream	7		
17-Jul-00	31-Oct-01	Pillsbury Co. LLC	Baked goods, biscuits, breads, cookies, crescents, pie crusts, pizza crusts and snacks	10,473	1.7x	11.4x
14-Aug-96	31-Jan-97	Ralcorp Cereal and Snack Division	Cereal and snack products	360		
Average				**1,379**	**2.4x**	**23.3x**

Source: Company data, FactSet

How much dry powder does GIS have and what would a transformative deal look like? Given that the company's leverage currently sits at a very manageable level of ~2.3x and the business continues to generate a significant amount of FCF, we expect M&A to play an important role in GIS' growth going forward. Although management has not stated a specific "maximum leverage" amount, we believe the company has the balance sheet to consummate a sizable deal. Specifically, we think the company can lever up to 4-4.5x net debt/proforma EBITDA to fund a transformative deal and still maintain its investment grade rating. Knowing that GIS is interested in assets within the natural/organic space in the US, we present a hypothetical scenario below wherein GIS acquires HAIN (HAIN has recently been more open to exploring all strategic options that might maximize shareholder value). We think this hypothetical deal would make strategic sense and our analysis below shows that it works financially as well. We assume a purchase price of $60/share or ~$6.9B in EV funded entirely by debt, resulting in proforma leverage of 3.7x. Other important assumptions include a 3.5% incremental cost of debt, $55M in deal-related amortization and $297M in synergies (10% of acquired company sales). We estimate the deal would be ~10% accretive to EPS by year 3.

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Chart 73: GIS Hypothetical Acquisition of HAIN – An Illustrative Example

Transaction Terms	
Trans. Equity Value	$60.00
x HAIN Share Count	104.4
= Equity Value	$6,266
+ Net Debt	$603
= Enterprise Value	$6,869
EV/NTM EBITDA	18.4x

Deal Funding			
Sources		**Uses**	
Enterprise Value	$6,869	HAIN Debt	$603
Cash On Hand	$0	HAIN Equity Value	$6,266
Incremental Debt	$6,869		
Equity	$0		

Assumptions			
Incremental Debt cost	3.50%	Current GIS Shares	580.3
Book Equity GIS	$5,383	New Shares Issued	0.0
Run Rate Synergies	$297	Pro-Forma Shares	580.3
Synergies % of target sales	10.0%	Pro-Forma Tax Rate	24.0%
Dividend/share	$1.96	Deal Amort % of EV	0.8%

General Mills Financials (Year ending May 31)				
Last Price	$54.79			
Fully Diluted Shares	580			
Equity Value	$31,795			
Balance Sheet	**Last Q**			
Cash and Investments	$962			
Long-Term Debt	$8,228			
Net Debt	$7,467			
Enterprise Value	$39,261			
Income Statement	**2017A**	**2018E**	**2019E**	**2020E**
Total Revenues[1]	$15,620	$15,704	$15,862	$16,095
Revenue Growth	-5.7%	0.5%	1.0%	1.5%
Non-GAAP Operating Profit	$2,834	$2,787	$2,893	$2,992
Operating Profit Margin	*18.1%*	*17.7%*	*18.2%*	*18.6%*
Adjusted EPS	$3.08	$3.19	$3.55	$3.82
D&A	$604	$593	$619	$547
EBITDA	$3,438	$3,379	$3,512	$3,539
EBITDA Margin	*22.0%*	*21.5%*	*22.1%*	*22.0%*
Less Net Interest Expense	$295	$300	$294	$255
Less Tax	$1,124	$1,078	$749	$747
Less CapEx	$684	$620	$714	$624
Free Cash Flow	$1,629	$1,681	$2,049	$2,169
Free Cash Flow/Share	$2.81	$2.90	$3.53	$3.74
Free Cash Flow Yield	*8.4%*	*8.7%*	*10.6%*	*11.2%*
Cash EPS	3.97	4.19	4.61	4.67
Valuation and Leverage	**2017A**	**2018E**	**2019E**	**2020E**
Price / Earnings	17.8x	17.2x	15.4x	14.4x
EV / EBITDA	11.4x	11.6x	11.2x	11.1x
Gross Debt / EBITDA	2.4x	2.4x	2.3x	2.3x

Hain Celestial Financials (Year ending June 30)				
Last Price	$33.27			
Fully Diluted Shares	104			
Equity Value	$3,475			
Balance Sheet	**Last Q**			
Cash and Investments	$139			
Long-Term Debt	$742			
Net Debt	$603			
Enterprise Value	$4,078			
Income Statement	**2018E**	**2019E**	**2020E**	**2021E**
Total Revenues[2]	$2,972	$3,090	$3,237	$3,393
Revenue Growth	4.2%	4.0%	4.8%	4.8%
Non-GAAP Operating Profit	$264	$291	$324	$359
Operating Profit Margin	*8.9%*	*9.4%*	*10.0%*	*10.6%*
Adjusted EPS	$1.70	$1.94	$2.24	$2.60
D&A	$80	$82	$85	$88
EBITDA	$344	$373	$409	$448
EBITDA Margin	*11.6%*	*12.1%*	*12.6%*	*13.2%*
Less Net Interest Expense	$26	$21	$17	$7
Less Tax	$126	$109	$120	$123
Less CapEx	$75	$77	$81	$85
Free Cash Flow	$143	$186	$208	$240
Free Cash Flow/Share	$1.37	$1.78	$2.00	$2.30
Free Cash Flow Yield	*4.1%*	*5.4%*	*6.0%*	*6.9%*
Valutation and Leverage	**2018E**	**2019E**	**2020E**	**2021E**
Price / Earnings	19.6x	17.1x	14.8x	12.8x
EV / EBITDA	11.8x	10.9x	10.0x	9.1x
Gross Debt / EBITDA	1.8x	2.0x	1.8x	1.7x

GIS/HAIN FY 2018-2020 Pro-Forma Financials			
GIS Share Price	$54.79		
Pro-Forma Shares	580		
Equity Value	$31,795		
Pro-Forma Balance Sheet	**Last Q**		
Cash and Investments			
GIS legacy Debt	$7,467		
Incremental Debt	$6,869		
Net Debt	$14,336		
Enterprise Value	$46,131		
Pro-Forma Income Statement	**2018E**	**2019E**	**2020E**
Revenues	$18,794	$19,100	$19,488
Revenue Growth		1.6%	2.0%
Non-GAAP Operating Profit	$3,078	$3,217	$3,351
(+) Cost Synergies	$89	$196	$297
(-) Deal-Related Amortization	$55	$55	$55
Operating Profit post Synergies	$3,112	$3,358	$3,594
Operating Profit Margin	16.6%	17.6%	18.4%
D&A	$729	$758	$690
GIS Net Interest	$300		
Interest on Incremental Debt	$240		
Total Pro-Forma Interest	$541	$489	$445
Pre Tax	$2,571	$2,870	$3,149
Pro-Forma Tax Rate	24.0%	24.0%	24.0%
Tax	$617	$689	$756
JV income & Min Int	$47	$47	$47
Net Income	$2,001	$2,228	$2,440
GIS Pro-Forma Non-GAAP EPS	**$3.45**	**$3.84**	**$4.21**
Accretion	**8.0%**	**8.2%**	**10.2%**

EBITDA/Cash Flow/Cash EPS	2018E	2019E	2020E
EBITDA post Synergies	$3,841	$4,117	$4,284
EBITDA Margin	20.4%	21.6%	22.0%
Free Cash Flow	$1,981	$2,206	$2,416
Free Cash Flow/Share	$3.41	$3.80	$4.16
Cash EPS	$4.40	$4.83	$5.11

Pro-Forma Valuation and Leverage	2018E	2019E	2020E
Price / Earnings	15.9x	14.3x	13.0x
EV / EBITDA	12.0x	11.2x	10.8x
Net Debt / EBITDA	3.7x	3.0x	2.6x
EBITDA ROC	19.5%	20.9%	21.7%

Source: Company data, Jefferies estimates

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What is the hypothetical value in a buyout scenario? We continue to view the food space as event-driven and believe M&A activity in the space will continue to pick up. With the success 3G Capital has had in consolidating the food industry, most large-cap food companies are considered potential targets for 3G's next deal. GIS is no exception. In fact, if GIS performance fails to improve in the near term, we see increased pressure in the board room for the CEO to consider strategic options. To evaluate the likelihood of a sale and potential value unlock, we present a hypothetical scenario in which KHC buys GIS. We assume a purchase price of $70/share (~28% premium to current stock price) or ~$48.1B in EV, funded 73% by debt and resulting in proforma leverage of 5.0x (we believe KHC can flex its balance sheet more than that but prefer to be conservative). Other important assumptions include a 4.5% incremental cost of debt, $481M in deal-related amortization and $1.3B in synergies (8.2% of acquired company sales). In such a scenario, we estimate the deal would be neutral to KHC's EPS in year 1 but ~11% accretive by year 3. We note that GIS' CPW and Häagen-Dazs Japan JVs each have a 'change of control' provision wherein the JV partners would have the option to buy out the remaining 50% portion of the JV that they don't already own in the event that GIS gets acquired. If this scenario plays out (i.e., GIS gets acquired and the JV partners exercise their option) then GIS' acquirer would receive cash for the sale of GIS's JV interest, but would lose the EBITDA associated with GIS' JV share (which we estimate at ~$60-70M annually). Net-net, we don't think the implications of such a scenario would have a material impact on the buyout analysis we present below.

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Chart 74: Kraft Heinz Hypothetical Acquisition of GIS – An Illustrative Example

Transaction Terms			
Trans. Equity Value	$70.00	Percent Cash	73%
x GIS Share Count	580.3	Cash Per Share	$10.13
= Equity Value	$40,621	Percent Stock	27%
+ Net Debt	$7,467	Stock Per Share	$2.76
= Enterprise Value	$48,088		
EV/TTM EBITDA	13.9x		

Deal Funding			
Sources		**Uses**	
Enterprise Value	$48,088	GIS Debt	$7,467
Cash On Hand	$0	GIS Equity Value	$40,621
Incremental Debt	$35,000		
Equity	$13,088		

Assumptions			
Incremental Debt cost	4.50%	Current KHC Shares	1,228.0
Book Equity KHC	$58,971	New Shares Issued	182.5
Run Rate Synergies	$1,300.0	Pro-Forma Shares	1,410.5
Synergies % of target sales	8.2%	Pro-Forma Tax Rate	30.0%
Dividend/share	$2.91	Deal Amort % of EV	1.0%

Kraft Heinz Financials (Year ending Dec)				
Last Price	$71.71			
Fully Diluted Shares	1,228			
Equity Value	$88,060			
Balance Sheet	**Last Q**			
Cash and Investments	$1,441			
Long-Term Debt	$28,299			
Net Debt	$30,068			
Enterprise Value	$118,128			
Income Statement	**2018E**	**2019E**	**2020E**	**2021E**
Total Revenues [1]	$26,821	$27,357	$28,053	$28,772
Revenue Growth	2.2%	2.0%	2.5%	2.6%
Non-GAAP Operating Profit	$7,935	$8,306	$8,702	$9,056
Operating Profit Margin	*29.6%*	*30.4%*	*31.0%*	*31.5%*
Adjusted EPS	$3.98	$4.23	$4.52	$4.78
D&A	$676	$649	$609	$624
EBITDA	$8,612	$8,955	$9,311	$9,680
EBITDA Margin	*32.1%*	*32.7%*	*33.2%*	*33.6%*
Less Net Interest Expense	$1,145	$1,070	$984	$885
Less Tax	$1,901	$2,026	$2,161	$2,288
Less CapEx	$738	$752	$771	$791
Free Cash Flow	$4,814	$5,088	$5,375	$5,697
Free Cash Flow/Share	$3.92	$4.14	$4.38	$4.64
Free Cash Flow Yield	*5.5%*	*5.8%*	*6.1%*	*6.5%*
Cash EPS	4.49	4.72	4.97	5.25
Valuation and Leverage	**2018E**	**2019E**	**2020E**	**2021E**
Price / Earnings	18.0x	16.9x	15.9x	15.0x
EV / EBITDA	13.7x	13.2x	12.7x	12.2x
Gross Debt / EBITDA	3.3x	3.2x	3.0x	2.9x

General Mills Financials (Calendarized)				
Last Price	$54.79			
Fully Diluted Shares	580			
Equity Value	$31,795			
Balance Sheet	**Last Q**			
Cash and Investments	$962			
Long-Term Debt	$8,228			
Net Debt	$7,467			
Enterprise Value	$39,261			
Income Statement	**2018E**	**2019E**	**2020E**	**2021E**
Total Revenues [2]	$15,783	$15,980	$16,241	$16,533
Revenue Growth	0.5%	1.2%	1.6%	1.8%
Non-GAAP Operating Profit	$2,840	$2,942	$3,048	$3,163
Operating Profit Margin	*18.0%*	*18.4%*	*18.8%*	*19.1%*
Adjusted EPS	$3.42	$3.68	$3.97	$4.28
D&A	$616	$582	$552	$562
EBITDA	$3,456	$3,525	$3,601	$3,725
EBITDA Margin	*21.9%*	*22.1%*	*22.2%*	*22.5%*
Less Net Interest Expense	$301	$275	$234	$189
Less Tax	$571	$593	$628	$667
Less CapEx	$722	$678	$630	$641
Free Cash Flow	$1,780	$2,102	$2,229	$2,349
Free Cash Flow/Share	$3.07	$3.62	$3.84	$4.05
Free Cash Flow Yield	*5.6%*	*6.6%*	*7.0%*	*7.4%*
Valutation and Leverage	**2018E**	**2019E**	**2020E**	**2021E**
Price / Earnings	16.0x	14.9x	13.8x	12.8x
EV / EBITDA	11.4x	11.1x	10.9x	10.5x
Gross Debt / EBITDA	2.2x	2.3x	2.3x	2.2x

KHC/GIS FY 2019-2021 Pro-Forma Financials			
KHC Share Price	$71.71		
Pro-Forma Shares	1,411		
Equity Value	$101,148		
Pro-Forma Balance Sheet	**Last Q**		
Cash and Investments			
KHC brands legacy debt	$30,068		
Incremental Debt	$35,000		
Net Debt	$65,068		
Enterprise Value	$166,216		
Pro-Forma Income Statement	**2019E**	**2020E**	**2021E**
Revenues	$43,337	$44,294	$45,304
Revenue Growth		2.2%	2.3%
Non-GAAP Operating Profit	$11,248	$11,750	$12,219
(+) Cost Synergies	$429	$858	$1,300
(-) Deal-Related Amortization	$481	$481	$481
Operating Profit post Synergies	$11,196	$12,127	$13,038
Operating Profit Margin	25.8%	27.4%	28.8%
Proforma D&A (incl. deal-related amort)	$1,712	$1,642	$1,667
KHC legacy net interest	$1,070		
Interest on Incremental Debt	$1,575		
Total Pro-Forma Interest	$2,645	$2,498	$2,367
Pre Tax	$8,551	$9,629	$10,671
Pro-Forma Tax Rate	30.0%	30.0%	30.0%
Tax	$2,565	$2,889	$3,201
Minority interest (after tax)	-$4	-$10	-$10
Net Income	$5,982	$6,730	$7,460
KHC Pro-Forma Non-GAAP EPS	**$4.24**	**$4.77**	**$5.29**
Accretion	**0%**	**6%**	**11%**

EBITDA/Cash Flow/Cash EPS	2019E	2020E	2021E
EBITDA post Synergies	$12,908	$13,769	$14,706
EBITDA Margin	29.8%	31.1%	32.5%
Free Cash Flow	$6,267	$6,981	$7,705
Free Cash Flow/Share	$4.44	$4.95	$5.46
Cash EPS	$5.09	$5.59	$6.12

Pro-Forma Valuation and Leverage	2019E	2020E	2021E
Price / Earnings	16.9x	15.0x	13.6x
EV / EBITDA	12.9x	12.1x	11.3x
Net Debt / EBITDA	5.0x	4.4x	3.8x
EBITDA ROC	10.4%	11.1%	11.9%

Source: Company data, Jefferies estimate

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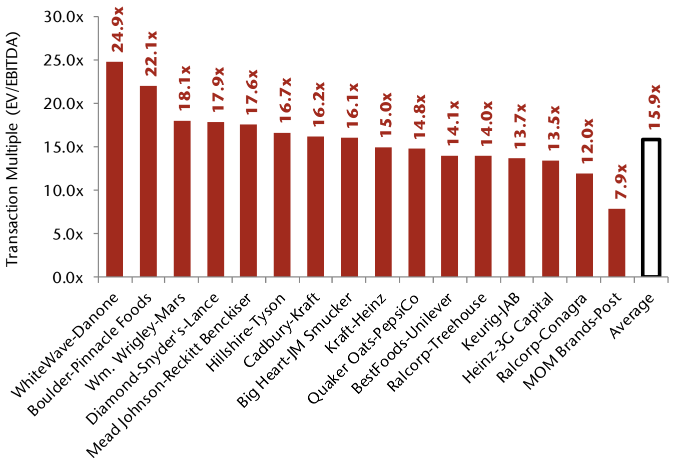
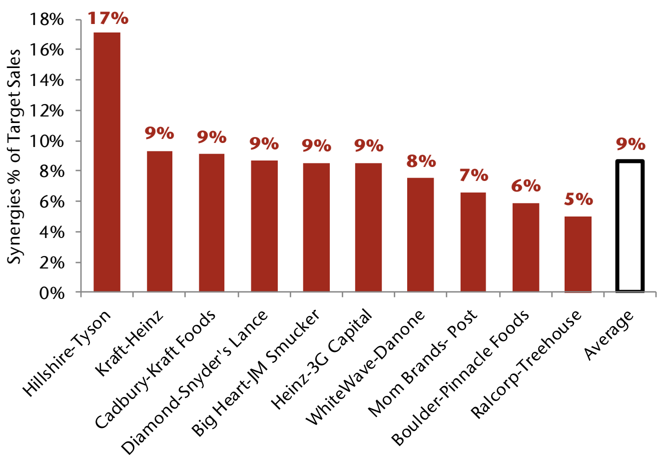
Key assumptions for our acquisition / buyout scenarios are supported by several notable transactions in the food space. Our key assumptions on potential synergies, valuation and deal-related amortization under various acquisition / buyout scenarios are supported by our detailed analysis of several notable transactions within the food space since 2000 (see Charts 75-78 below).

Chart 75: Transaction Multiples For Select Food Industry Transactions (EV/EBITDA)



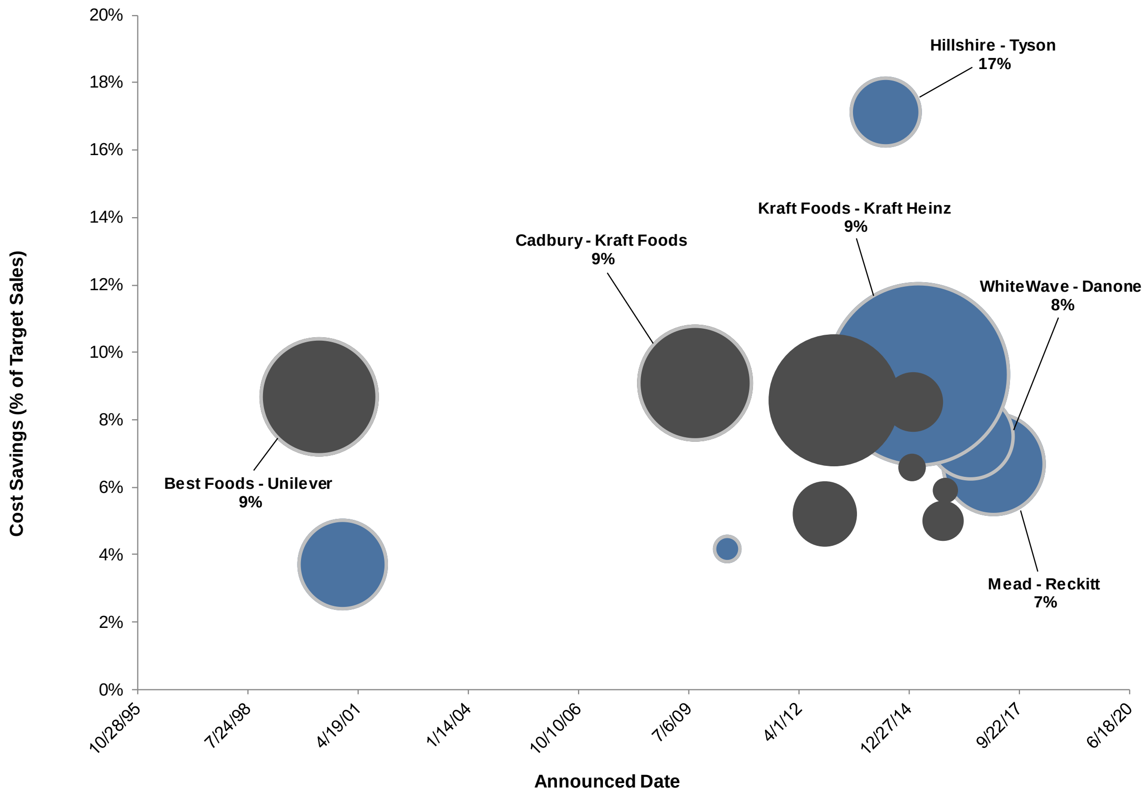
Source: Company data, FactSet, Jefferies estimates

Chart 76: Announced Synergies As % Of Acquired Company's Sales



Source: Company data, FactSet, Jefferies estimates

Chart 77: Timeline And Realized Synergies For Select Food Industry Transactions Since 2000



Source: Company data, Jefferies estimates

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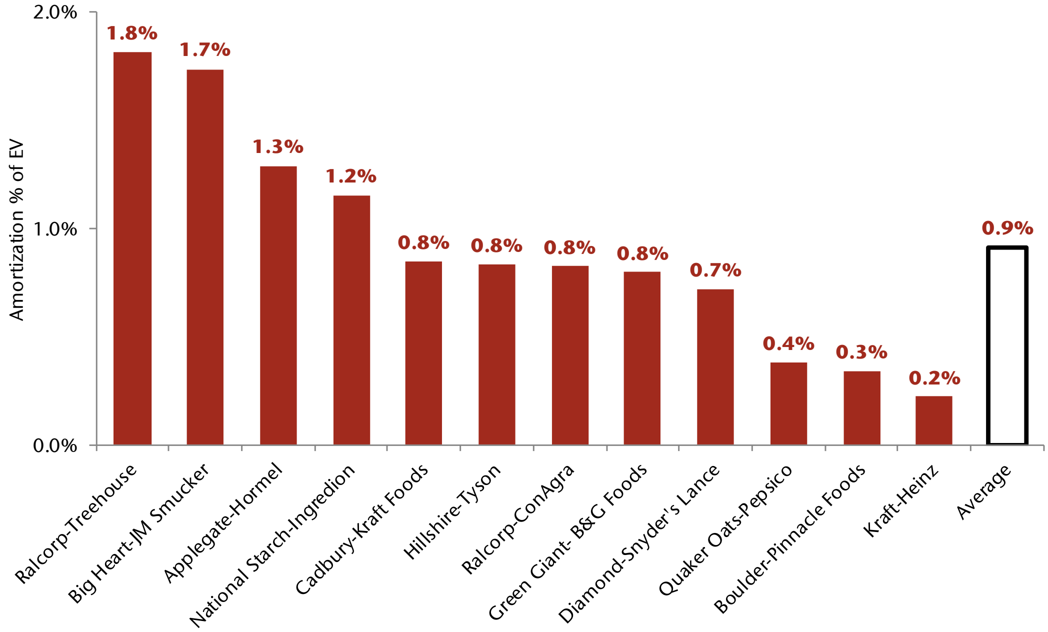
Chart 78: Deal-Related Amortization As % Of EV For Select Food Industry Transactions Since 2016

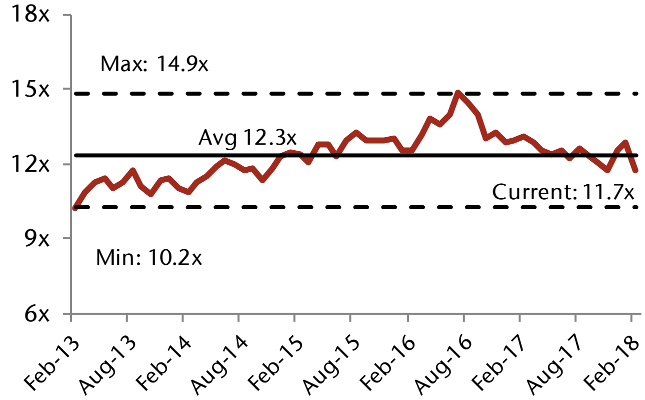


Source: Company data, Jefferies estimates

Improving Sales Growth Performance Should Result In Multiple Expansion

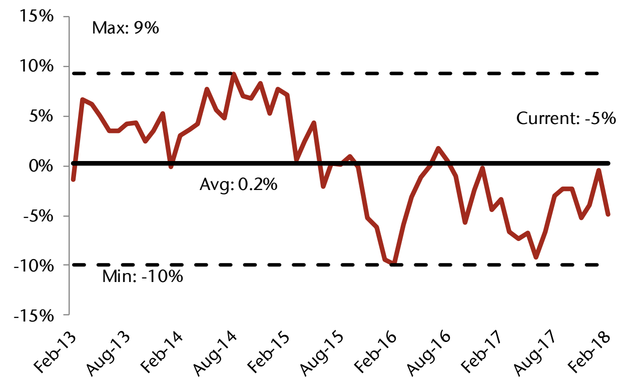
Current valuation is attractive. Consensus EPS contains some noise related to the recent US tax law changes (included in some estimates, but not others). As such, we prefer to look at the valuation on an EV/EBITDA basis. On this metric, the stock currently trades ~8% below its 5-year average and at a 5% discount to its large cap packaged food peers (compared to in-line, on average, over the last 5 years).

Chart 79: GIS EV/EBITDA valuation (NTM)



Source: FactSet

Chart 80: GIS EV/EBITDA Relative to Large Cap Food Group



Source: FactSet

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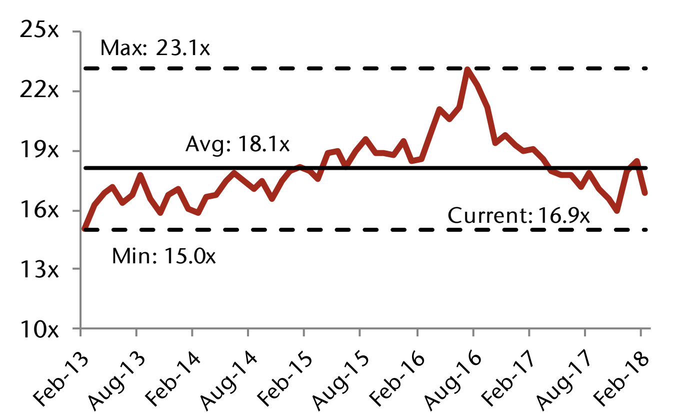
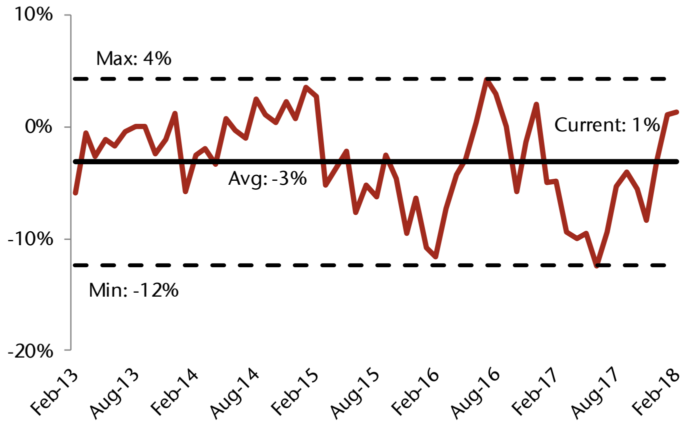
Chart 81: GIS PE Valuation (NTM)



Source: FactSet

Chart 82: GIS PE Relative to Large Cap Food Group



Source: FactSet

We expect improving sales growth trends to result in a multiple expansion. GIS is not alone amongst its large-cap packaged food peers in experiencing relatively weak organic sales growth over the past few years – in fact, many of the large cap food companies continue to face negative y/y organic growth. Although we believe much of the disappointing results are being driven by transitory factors which should abate over time, the market seems to be pricing in the widespread perception that large food brands are "dying", increasingly losing share to private label and steadily losing their pricing power, which is expected to erode margins over time and stifle earnings growth (we decompose this perception and present our counter-argument in greater detail in our BSM report Brands Still Matter). Given that backdrop and the fact that GIS' top-line growth struggles have been more pronounced than some of its peers, it is not surprising that market sentiment on the stock (as evidenced by its valuation) is relatively negative. However, we now believe the risk/reward implied by the current valuation has become sufficiently attractive to warrant a Buy rating and we expect improved sales growth trends to be the catalyst that drives near-term multiple expansion. Longer-term, we believe the company's recent actions to enhance its capabilities (people and processes) and refine its strategy can unlock significant value in GIS' underappreciated portfolio of leading brands, particularly in the emerging e-Commerce channel. Additionally, we expect M&A to play a larger role in GIS' near to midterm growth, which we do not believe is priced into the stock.

We are increasing our price target to $63 (from $56). Our new $63 PT simply assumes a reversion to the mean in terms of EV/EBITDA valuation and does not account for any future M&A, which could represent further upside to our estimate.

Our upside scenario valuation is $70, which is based on an EV/EBITDA multiple of 13.4x (~13% premium to large-cap food peers) our FY19 upside scenario EBITDA of $3.545B. Our upside scenario assumes 2% sales growth (all organic) and ~50 bps of EBIT margin expansion driven by improved capacity utilization and higher cost savings flow-through to the bottom line.

Our downside scenario valuation is $48, which is based on an EV/EBITDA multiple of 11.1x (~7% discount to large-cap food peers) our FY19 downside EBITDA estimate of $3.159B. Our downside scenario assumes a ~2% decline in sales growth driven by continued category weakness and share losses, and ~90bps of EBIT margin contraction as cost-savings continue to be offset by sales volume deleverage.

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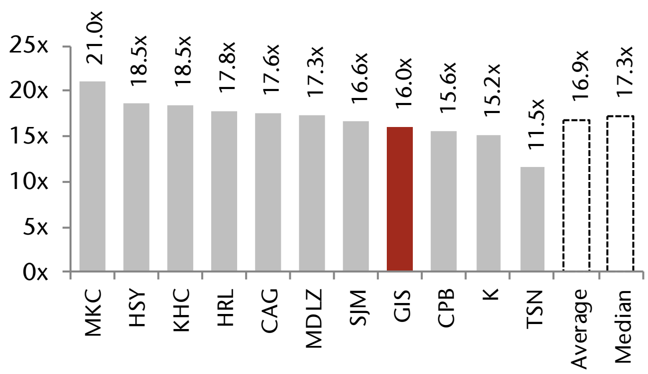
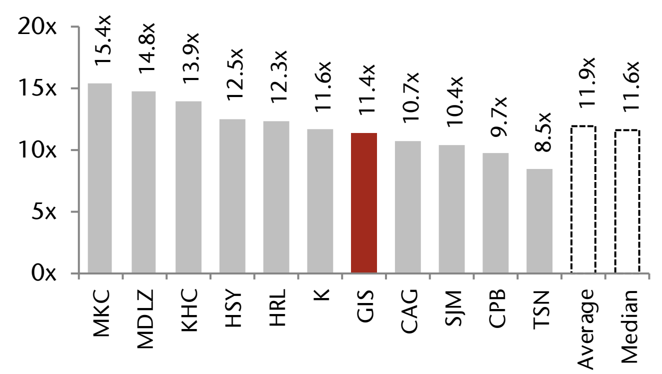
Chart 83: NTM P/E vs. Peers



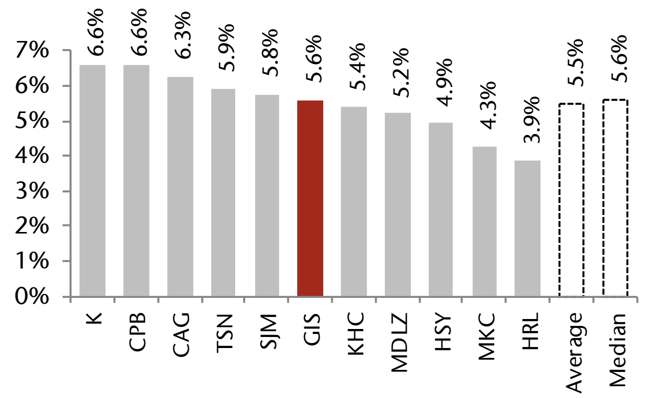
Source: FactSet, Jefferies estimates

Chart 84: EV/EBITDA vs. Peers



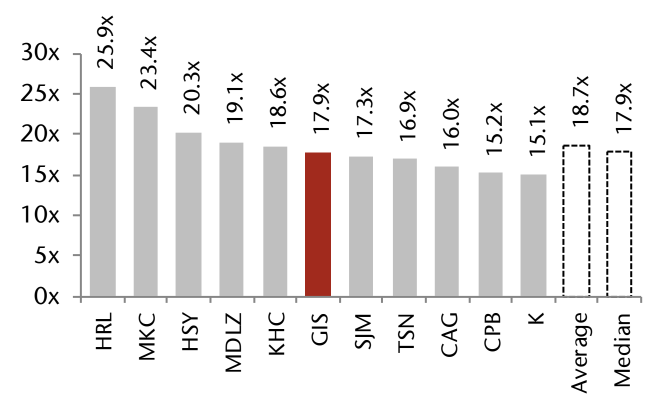
Source: FactSet, Jefferies estimates

Chart 85: Free Cash Flow Yield vs. Peers



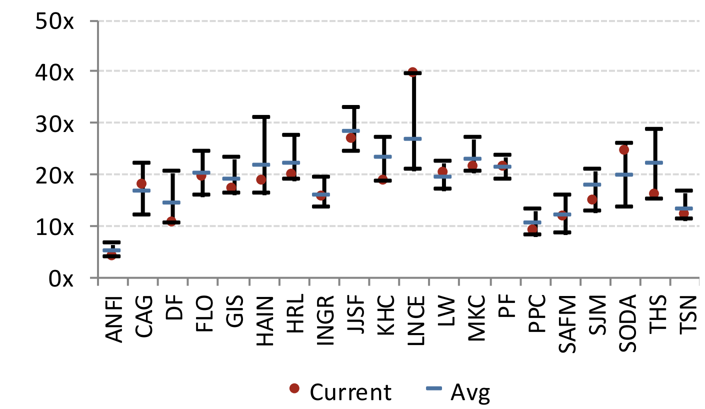
Source: FactSet, Jefferies estimates

Chart 86: Free Cash Flow Multiple vs. Peers



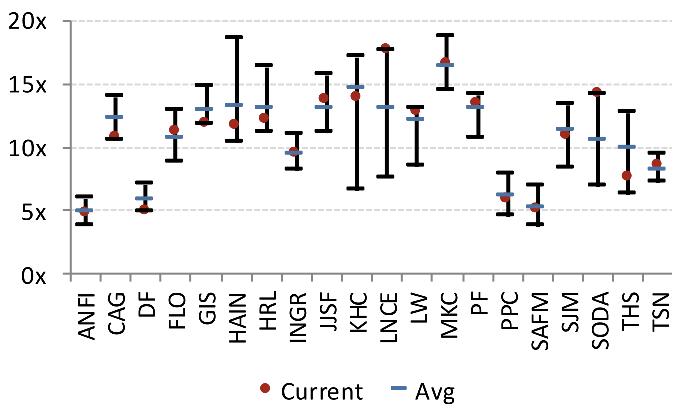
Source: FactSet, Jefferies estimates

Chart 87: Coverage Universe Historical P/E Range



Source: FactSet

Chart 88: Coverage Universe Historical EV/EBITDA Range



Source: FactSet

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Chart 89: GIS – Financial Summary

Financial Summary	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18	2Q18	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
($ in millions)	May-14	May-15	May-16	Aug-16	Nov-16	Feb-17	May-17	May-17	Aug-17	Nov-17	Feb-18	May-18	May-18	May-19	May-20	May-21
Total Revenues	**17,910**	**17,630**	**16,563**	**3,908**	**4,112**	**3,793**	**3,807**	**15,620**	**3,769**	**4,199**	**3,878**	**3,859**	**15,704**	**15,862**	**16,095**	**16,384**
% change	1%	-2%	-6%	-7%	-7%	-5%	-3%	-6%	-4%	2%	2%	1%	1%	1%	1%	2%
Cost of Sales	11,588	11,519	10,661	2,447	2,598	2,466	2,474	9,985	2,447	2,755	2,501	2,450	10,154	10,177	10,310	10,479
Adjusted Gross Profit	**6,321**	**6,112**	**5,903**	**1,461**	**1,514**	**1,327**	**1,333**	**5,635**	**1,322**	**1,443**	**1,376**	**1,409**	**5,550**	**5,685**	**5,785**	**5,905**
SG&A	3,412	3,304	3,119	712	708	688	693	2,801	679	712	693	680	2,764	2,792	2,793	2,800
Adjusted EBIT	**2,909**	**2,808**	**2,784**	**749**	**806**	**640**	**639**	**2,834**	**643**	**732**	**683**	**729**	**2,787**	**2,893**	**2,992**	**3,105**
% change	0%	-3%	-1%	-3%	1%	1%	11%	2%	-14%	-9%	7%	14%	-2%	4%	3%	4%
Net Interest Expense	302	315	304	74	76	76	69	295	72	75	75	78	300	294	255	212
Adjusted EBITDA	3,495	3,396	3,392	901	955	787	795	3,438	788	877	834	880	3,379	3,512	3,539	3,662
Adjusted Net Income	1,819	1,778	1,790	477	510	423	430	1,840	416	475	456	509	1,856	2,022	2,127	2,246
Adjusted EPS	**$2.82**	**$2.87**	**$2.92**	**$0.78**	**$0.85**	**$0.72**	**$0.73**	**$3.08**	**$0.71**	**$0.82**	**$0.79**	**$0.88**	**$3.19**	**$3.55**	**$3.82**	**$4.12**
% change	3%	2%	2%	-3%	4%	10%	11%	5%	-9%	-4%	10%	20%	4%	11%	8%	8%
Operating cash flow	2,541	2,543	2,630	288	699	571	755	2,313	591	976	(424)	1,158	2,301	2,763	2,793	2,917
Capex	664	712	729	154	165	157	209	684	116	144	175	185	620	714	624	635
Free cash flow	1,878	1,830	1,901	135	535	414	545	1,629	474	833	(598)	973	1,681	2,049	2,169	2,282
Net debt	6,807	8,242	7,397	7,416	7,240	6,882	7,482	7,482	7,607	7,467	8,349	7,660	7,660	6,751	5,742	4,638
Equity	7,990	6,172	6,153	6,130	5,328	5,273	5,596	5,596	5,250	5,383	5,592	5,850	5,850	6,868	7,972	9,176
# of diluted shares	646	619	612	612	600	591	589	598	587	580	579	578	581	570	558	545
Gross Margin (adjusted)	35.3%	34.7%	35.6%	37.4%	36.8%	35.0%	35.0%	36.1%	35.1%	34.4%	35.5%	36.5%	35.3%	35.8%	35.9%	36.0%
SG&A/sales	19.1%	18.7%	18.8%	18.2%	17.2%	18.1%	18.2%	17.9%	18.0%	16.9%	17.9%	17.6%	17.6%	17.6%	17.4%	17.1%
EBIT Margin (adjusted)	16.2%	15.9%	16.8%	19.2%	19.6%	16.9%	16.8%	18.1%	17.1%	17.4%	17.6%	18.9%	17.7%	18.2%	18.6%	19.0%
EBITDA Margin (adjusted)	19.5%	19.3%	20.5%	23.1%	23.2%	20.7%	20.9%	22.0%	20.9%	20.9%	21.5%	22.8%	21.5%	22.1%	22.0%	22.4%
FCF Margin	10.5%	10.4%	11.5%	3.4%	13.0%	10.9%	14.3%	10.4%	12.6%	19.8%	-15.4%	25.2%	10.7%	12.9%	13.5%	13.9%
Tax rate	32.2%	30.5%	29.8%	31.4%	32.4%	24.7%	26.8%	29.2%	30.5%	29.3%	25.5%	24.0%	29.0%	24.0%	24.0%	24.0%
Net debt/TTM EBITDA	1.9x	2.4x	2.2x	2.2x	2.1x	2.0x	2.2x	2.2x	2.3x	2.3x	2.5x	2.3x	2.3x	1.9x	1.6x	1.3x
Net debt/cap	46%	57%	55%	55%	58%	57%	57%	57%	59%	58%	60%	57%	57%	50%	42%	34%
ROIC	17.2%	16.2%	16.6%	17.9%	20.9%	17.3%	16.3%	18.0%	16.8%	19.2%	16.2%	18.0%	17.2%	17.7%	18.1%	18.7%

Source: Jefferies estimates, company data

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Chart 90: GIS – Segment Summary

Segment Summary	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18	2Q18	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
Revenues																
North America Retail	11,802	11,612	10,937	2,557	2,749	2,499	2,392	10,197	2,438	2,772	2,549	2,416	10,175	10,226	10,328	10,483
% change		-1.6%	-5.8%	-7.5%	-8.6%	-7.0%	-3.4%	-6.8%	-4.6%	0.8%	2.0%	1.0%	-0.2%	0.5%	1.0%	1.5%
Convenience Stores and Foodservice	1,919	1,995	1,924	446	488	449	488	1,870	447	512	462	493	1,914	1,952	1,991	2,031
% change	-2.1%	4.0%	-3.6%	-6.6%	-3.6%	-1.1%	0.2%	-2.8%	0.2%	5.1%	3.0%	1.0%	2.3%	2.0%	2.0%	2.0%
Europe & Australia	2,192	2,127	1,998	478	435	425	487	1,825	492	467	437	501	1,897	1,897	1,935	1,974
% change		-3.0%	-6.0%	-8.9%	-6.7%	-3.4%	-14.2%	-8.7%	2.8%	7.3%	3.0%	3.0%	4.0%	0.0%	2.0%	2.0%
Asia & Latin America	1,996	1,897	1,705	426	441	421	440	1,728	392	448	430	449	1,719	1,787	1,841	1,896
% change		-5.0%	-10.1%	-3.0%	-0.7%	-0.4%	10.4%	1.4%	-8.0%	1.7%	2.0%	2.0%	-0.6%	4.0%	3.0%	3.0%
Total Revenues	**17,910**	**17,630**	**16,563**	**3,908**	**4,112**	**3,793**	**3,807**	**15,620**	**3,769**	**4,199**	**3,878**	**3,859**	**15,704**	**15,862**	**16,095**	**16,384**
% of Total																
North America Retail	66%	66%	66%	65%	67%	66%	63%	65%	65%	66%	66%	63%	65%	64%	64%	64%
Convenience Stores and Foodservice	11%	11%	12%	11%	12%	12%	13%	12%	12%	12%	12%	13%	12%	12%	12%	12%
Europe & Australia	12%	12%	12%	12%	11%	11%	13%	12%	13%	11%	11%	13%	12%	12%	12%	12%
Asia & Latin America	11%	11%	10%	11%	11%	11%	12%	11%	10%	11%	11%	12%	11%	11%	11%	12%
Adj. EBIT																
North America Retail		2,382.7	2,351.2	628.2	651.0	516.7	507.7	2,303.6	533.2	622.9	565.3	561.1	2,282.5	2,345.0	2,399.4	2,466.9
% margin		20.5%	21.5%	24.6%	23.7%	20.7%	21.2%	22.6%	21.9%	22.5%	22.2%	23.2%	22.4%	22.9%	23.2%	23.5%
% change			-1.3%	-7.8%	-0.1%	-6.5%	9.1%	-2.0%	-15.1%	-4.3%	9.4%	10.5%	-0.9%	2.7%	2.3%	2.8%
bps change			98 bp	-8 bp	203 bp	10 bp	243 bp	109 bp	-270 bp	-121 bp	150 bp	200 bp	-16 bp	50 bp	30 bp	30 bp
Convenience Stores and Foodservice	307.3	353.1	378.9	92.7	109.1	93.6	105.8	401.2	84.8	106.5	98.7	115.5	405.5	423.4	440.8	458.7
% margin	16.0%	17.7%	19.7%	20.8%	22.4%	20.9%	21.7%	21.5%	19.0%	20.8%	21.4%	23.4%	21.2%	21.7%	22.1%	22.6%
% change	-2.3%	14.9%	7.3%	16.2%	6.1%	3.3%	0.1%	5.9%	-8.5%	-2.4%	5.5%	9.1%	1.1%	4.4%	4.1%	4.1%
bps change	-4 bp	168 bp	200 bp	407 bp	206 bp	90 bp	-3 bp	176 bp	-180 bp	-159 bp	50 bp	175 bp	-27 bp	50 bp	45 bp	45 bp
Europe & Australia		179.4	200.3	43.9	41.3	42.0	37.0	164.2	30.6	26.9	29.0	55.6	142.2	157.4	174.1	191.4
% margin		8.4%	10.0%	9.2%	9.5%	9.9%	7.6%	9.0%	6.2%	5.8%	6.6%	11.1%	7.5%	8.3%	9.0%	9.7%
% change			11.6%	-29.9%	-13.4%	25.0%	-34.4%	-18.0%	-30.3%	-34.9%	-30.8%	50.4%	-13.4%	10.7%	10.6%	9.9%
bps change			159 bp	-274 bp	-73 bp	225 bp	-235 bp	-103 bp	-296 bp	-373 bp	-325 bp	350 bp	-150 bp	80 bp	70 bp	70 bp
Asia & Latin America		119.8	69.1	22.3	29.0	10.0	22.3	83.6	15.5	16.7	20.9	31.7	84.9	97.2	109.3	122.1
% margin		6.3%	4.1%	5.2%	6.6%	2.4%	5.1%	4.8%	4.0%	3.7%	4.9%	7.1%	4.9%	5.4%	5.9%	6.4%
% change			-42.3%	829.2%	-22.3%	300.0%	-17.1%	21.0%	-30.5%	-42.4%	109.4%	42.3%	1.5%	14.5%	12.5%	11.7%
bps change			-226 bp	469 bp	-182 bp	178 bp	-168 bp	78 bp	-128 bp	-285 bp	250 bp	200 bp	10 bp	50 bp	50 bp	50 bp
Segment EBIT		**3,035**	**3,000**	**787**	**830**	**662**	**673**	**2,953**	**664**	**773**	**714**	**764**	**2,915**	**3,023**	**3,124**	**3,239**
% margin		17.2%	18.1%	20.1%	20.2%	17.5%	17.7%	18.9%	17.6%	18.4%	18.4%	19.8%	18.6%	19.1%	19.4%	19.8%
% change			-1.2%	-4.8%	-1.1%	-2.5%	2.8%	-1.6%	-15.6%	-6.9%	7.8%	13.5%	-1.3%	3.7%	3.3%	3.7%
bps change			89 bp	50 bp	122 bp	49 bp	102 bp	79 bp	-252 bp	-178 bp	95 bp	212 bp	-34 bp	50 bp	35 bp	36 bp
Corporate expense		(227)	(216)	(38)	(24)	(23)	(34)	(119)	(21.4)	(41.3)	(31.0)	(34.7)	(128.5)	(129.7)	(131.7)	(134.0)
% of sales		1.3%	1.3%	1.0%	0.6%	0.6%	0.9%	0.8%	0.6%	1.0%	0.8%	0.9%	0.8%	0.8%	0.8%	0.8%
Total Adj. EBIT (incl. corp exp)		**2,808**	**2,784**	**749**	**806**	**640**	**639**	**2,834**	**642.7**	**731.7**	**683.0**	**729.2**	**2,786.6**	**2,893.2**	**2,992.0**	**3,105.1**
% margin		15.9%	16.8%	19.2%	19.6%	16.9%	16.8%	18.1%	17.1%	17.4%	17.6%	18.9%	17.7%	18.2%	18.6%	19.0%
% change			-0.9%	-3.5%	1.0%	0.5%	11.5%	1.8%	-14.2%	-9.2%	6.7%	14.1%	-1.7%	3.8%	3.4%	3.8%
bps change			88 bp	73 bp	157 bp	97 bp	219 bp	134 bp	-211 bp	-218 bp	74 bp	210 bp	-40 bp	50 bp	35 bp	36 bp
% of Total																
North America Retail		79%	78%	80%	78%	78%	75%	78%	80%	81%	79%	73%	78%	78%	77%	76%
Convenience Stores and Foodservice		12%	13%	12%	13%	14%	16%	14%	13%	14%	14%	15%	14%	14%	14%	14%
Europe & Australia		6%	7%	6%	5%	6%	5%	6%	5%	3%	4%	7%	5%	5%	6%	6%
Asia & Latin America		4%	2%	3%	3%	2%	3%	3%	2%	2%	3%	4%	3%	3%	3%	4%

Source: Jefferies estimates, company data

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Chart 91: GIS – Balance Sheet

Balance Sheet	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18	2Q18	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
($ in millions)	May-14	May-15	May-16	Aug-16	Nov-16	Feb-17	May-17	May-17	Aug-17	Nov-17	Feb-18	May-18	May-18	May-19	May-20	May-21
Assets																
Cash & cash equivalents	867	334	764	766	810	899	766	766	821	962	91	780	780	1,689	2,698	3,802
Receivables	1,484	1,387	1,361	1,446	1,383	1,428	1,430	1,430	1,547	1,511	1,551	1,415	1,415	1,430	1,451	1,477
Inventories	1,559	1,541	1,414	1,548	1,526	1,461	1,484	1,484	1,595	1,517	2,029	1,742	1,742	1,746	1,770	1,799
Prepaid expenses and other current assets	409	424	399	434	394	340	382	382	376	345	345	345	345	345	345	345
Total Current Assets	**4,319**	**3,686**	**3,937**	**4,193**	**4,112**	**4,128**	**4,061**	**4,061**	**4,339**	**4,334**	**4,016**	**4,282**	**4,282**	**5,210**	**6,264**	**7,423**
Land, buildings and equipment	3,942	3,783	3,744	3,655	3,571	3,575	3,688	3,688	3,648	3,631	3,655	3,689	3,689	3,785	3,861	3,939
Goodwill	8,651	8,875	8,741	8,758	8,679	8,706	8,747	8,747	8,832	8,828	8,828	8,828	8,828	8,828	8,828	8,828
Other intangible assets	5,014	4,677	4,539	4,552	4,487	4,500	4,530	4,530	4,593	4,582	4,582	4,582	4,582	4,582	4,582	4,582
Other assets	1,146	811	752	754	753	762	786	786	797	816	816	816	816	816	816	816
Non-Current Assets	**18,752**	**18,146**	**17,775**	**17,720**	**17,491**	**17,542**	**17,751**	**17,751**	**17,871**	**17,857**	**17,881**	**17,915**	**17,915**	**18,011**	**18,087**	**18,165**
Total Assets	**23,072**	**21,832**	**21,712**	**21,913**	**21,602**	**21,670**	**21,813**	**21,813**	**22,210**	**22,192**	**21,897**	**22,198**	**22,198**	**23,221**	**24,351**	**25,589**
Liabilities																
Accounts payable	1,611	1,684	2,047	1,945	1,938	1,855	2,120	2,120	2,173	2,467	1,952	1,996	1,996	2,000	2,027	2,060
Current portion of long-term debt	1,251	1,000	1,103	1,103	1,508	605	605	605	605	201	212	212	212	212	212	212
Notes Payable	1,112	616	270	691	1,422	1,942	1,234	1,234	1,660	1,298	1,298	1,298	1,298	1,298	1,298	1,298
Other current liabilities	1,450	1,590	1,595	1,476	1,377	1,342	1,372	1,372	1,452	1,384	1,384	1,384	1,384	1,384	1,384	1,384
Total Current Liabilities	**5,424**	**4,890**	**5,015**	**5,215**	**6,244**	**5,744**	**5,331**	**5,331**	**5,890**	**5,350**	**4,846**	**4,889**	**4,889**	**4,894**	**4,921**	**4,954**
Long-term debt	6,424	7,575	7,058	7,078	6,542	7,176	7,643	7,643	7,823	8,228	8,228	8,228	8,228	8,228	8,228	8,228
Deferred income taxes	1,592	1,450	1,400	1,443	1,506	1,548	1,719	1,719	1,761	1,791	1,791	1,791	1,791	1,791	1,791	1,791
Other liabilities	1,643	1,745	2,088	2,048	1,982	1,930	1,523	1,523	1,486	1,440	1,440	1,440	1,440	1,440	1,440	1,440
Total Liabilities	**15,082**	**15,660**	**15,560**	**15,784**	**16,275**	**16,398**	**16,216**	**16,216**	**16,959**	**16,808**	**16,305**	**16,348**	**16,348**	**16,353**	**16,380**	**16,413**
Redeemable Interest	984	779	846	841	802	869	911	911	968	793	793	793	793	793	793	793
Common stock	76	76	76	76	76	76	76	76	76	76	76	76	76	76	76	76
Additional paid-in capital	1,232	1,297	1,177	1,185	1,179	1,130	1,121	1,121	1,071	1,243	1,268	1,293	1,293	1,393	1,493	1,593
Retained earnings	11,787	11,991	12,617	12,735	12,932	13,009	13,139	13,139	13,259	13,409	13,593	13,825	13,825	14,744	15,747	16,852
Capital stock in treasury	-5,219	-6,056	-6,327	-6,602	-7,529	-7,800	-7,763	-7,763	-8,270	-8,253	-8,253	-8,253	-8,253	-8,253	-8,253	-8,253
Accumulated other comprehensive loss	-1,340	-2,311	-2,612	-2,485	-2,477	-2,350	-2,245	-2,245	-2,232	-2,244	-2,244	-2,244	-2,244	-2,244	-2,244	-2,244
Non-controlling interest	471	396	377	380	345	340	358	358	379	359	359	359	359	359	359	359
Total Shareholders' Equity	**7,990**	**6,172**	**6,153**	**6,130**	**5,328**	**5,273**	**5,596**	**5,596**	**5,250**	**5,383**	**5,592**	**5,850**	**5,850**	**6,868**	**7,972**	**9,176**
Total Liabilities & Shareholders' Equity	**23,072**	**21,832**	**21,712**	**21,913**	**21,602**	**21,670**	**21,813**	**21,813**	**22,210**	**22,192**	**21,897**	**22,198**	**22,198**	**23,221**	**24,351**	**25,589**

Source: Jefferies estimates, company data

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Chart 92: GIS – Statement of Cash Flows

Statement of Cash Flows	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18	2Q18	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
($ in millions)	May-14	May-15	May-16	Aug-16	Nov-16	Feb-17	May-17	May-17	Aug-17	Nov-17	Feb-18	May-18	May-18	May-19	May-20	May-21
Operating Activities																
Net Income (loss)	1,861	1,259	1,737	420	496	370	416	1,701	409	444	468	516	1,836	2,059	2,163	2,282
Depreciation & Amortization	585	588	608	153	149	147	155	604	145	146	151	150	593	619	547	557
After tax earnings from joint ventures	(90)	(84)	(88)	(24)	(30)	(11)	(20)	(85)	(24)	(24)			(48)	-	-	-
Distribution of earnings from joint ventures	91	73	75	26	6	12	32	76	29	16			45	-	-	-
Stock-based compensation	109	106	90	39	17	20	19	96	30	19	25	25	98	100	100	100
Deferred income taxes	173	25	121	36	59	46	44	184	38	32	-	-	70	-	-	-
Tax benefit on exercised options	(69)	(75)	(94)	(53)	(7)	(5)	1	(64)					-	-	-	-
Pension and other postretirement benefit plan contributions	(50)	(50)	(48)	(11)	(11)	(11)	(11)	(45)	(6)	(7)			(13)	-	-	-
Pension and other postretirement benefit plan costs	124	91	118	9	9	9	9	36	1	1			2	-	-	-
Divestitures loss (gain)	(66)	-	(148)	-	14	-	-	14					-	-	-	-
Restructuring, impairment and other exit costs	(19)	531	107	57	14	70	(24)	117	(9)	2			(7)	-	-	-
Other, net	(76)	(138)	(106)	(5)	(1)	(43)	(38)	(86)	(5)	(33)			(37)	-	-	-
Changes in working capital:													-			
Receivables	(41)	7	(7)	(82)	36	(30)	6	(69)	(88)	34	(41)	136	42	(15)	(21)	(26)
Inventories	(88)	(24)	(146)	(122)	2	79	(19)	(62)	(90)	74	(512)	287	(241)	(4)	(23)	(29)
Prepaid expenses and other current assets	11	(51)	(0)	(34)	32	56	(37)	17	12	30	-	-	42	-	-	-
Accounts payable	192	146	319	(50)	30	(81)	200	100	79	298	(515)	44	(94)	5	27	33
Other current liabilities	(105)	137	93	(69)	(115)	(56)	22	(217)	70	(57)	-	-	13	-	-	-
Net Cash From Operating Activities	**2,541**	**2,543**	**2,630**	**288**	**699**	**571**	**755**	**2,313**	**591**	**976**	**(424)**	**1,158**	**2,301**	**2,763**	**2,793**	**2,917**
Investing activities																
Purchases of land, buildings, and equipment	(664)	(712)	(729)	(154)	(165)	(157)	(209)	(684)	(116)	(144)	(175)	(185)	(620)	(714)	(624)	(635)
Acquisitions, net of cash acquired	-	(822)	(84)	-	-	-	-	-					-	-	-	-
Investments in affiliates, net	(55)	(102)	64	8	(16)	13	(2)	3	(7)	(1)			(7)	-	-	-
Proceeds from disposal of land, buildings, and equipment	7	11	4	0	-	1	3	4	0	0			1	-	-	-
Proceeds from divestitures	122	-	829	-	18	-	-	18					-	-	-	-
Exchangeable note	29	28	21	13	-	-	-	13					-	-	-	-
Other, net	(1)	(4)	(11)	5	10	(0)	(15)	(1)	(0)	(4)			(4)	-	-	-
Net Cash From Investing Activities	**(562)**	**(1,602)**	**93**	**(127)**	**(153)**	**(144)**	**(223)**	**(647)**	**(123)**	**(148)**	**(175)**	**(185)**	**(630)**	**(714)**	**(624)**	**(635)**
Financing activities																
Changes in notes payable	573	(510)	(324)	420	745	517	(719)	962	414	(361)	11	-	64	-	-	-
Issuance of long-term debt	1,673	2,253	543	-	-	750	322	1,072		500	-	-	500	-	-	-
Payment of long-term debt	(1,445)	(1,146)	(1,000)	-	(0)	(1,003)	3	(1,000)		(500)			(500)	-	-	-
Proceeds from common stock issued on exercised options	108	164	172	64	13	14	22	113	41	10			51	-	-	-
Tax benefit on exercised options	69	75	94	53	7	5	(1)	64					-	-	-	-
Purchases of common stock for treasury	(1,745)	(1,162)	(607)	(400)	(950)	(301)	(1)	(1,652)	(600)	(0)			(601)	-	-	-
Dividends paid	(983)	(1,018)	(1,072)	(291)	(285)	(281)	(279)	(1,135)	(284)	(281)	(284)	(283)	(1,132)	(1,140)	(1,160)	(1,178)
Distributions to noncontrolling and redeemable interest holders	(74)	(41)	(92)	(1)	(3)	(55)	(11)	(70)	(22)	(47)			(69)	-	-	-
Net Cash From Financing Activities	**(1,824)**	**(1,385)**	**(2,286)**	**(156)**	**(473)**	**(354)**	**(663)**	**(1,646)**	**(451)**	**(680)**	**(273)**	**(283)**	**(1,687)**	**(1,140)**	**(1,160)**	**(1,178)**
Effect of exchange rate changes on cash and cash equivalents	(29)	(89)	(8)	(3)	(29)	16	(2)	(19)	38	(7)	-	-	31	-	-	-
Net change in cash & cash equivalents	**126**	**(533)**	**429**	**2**	**44**	**89**	**(133)**	**2**	**55**	**141**	**(871)**	**689**	**14**	**909**	**1,009**	**1,104**
Cash & equivalents at beginning of period	741	867	334	764	766	810	899	764	766	821	962	91	766	780	1,689	2,698
Cash & equivalents at end of period	**867**	**334**	**764**	**766**	**810**	**899**	**766**	**766**	**821**	**962**	**91**	**780**	**780**	**1,689**	**2,698**	**3,802**

Source: Jefferies estimates, company data

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Other Estimate Changes

We are updating estimates for TSN and FLO following their recent earnings announcements. We are updating our estimates for TSN and FLO primarily to reflect the lower tax rate. Our FY18 EPS for TSN is increasing from $5.76 to $6.75 reflecting a lower tax rate assumption (now at 24.5% vs. 34.5% previously) slightly offset by a higher interest expense (now at $335M vs. $325M previously). For perspective, our new FY18 EPS estimate compares to consensus of $6.44 and to management's updated guidance range of $6.55-$6.70. As for FLO, our FY18 estimate is increasing from $0.93 to $1.07 primarily reflecting a lower tax rate assumption (now at 25.5% vs. 35.5% before). Our estimate compares to consensus of $1.04 and guidance of $1.04-$1.16.

Chart 93: TSN - Financial Summary

Financial Summary	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18	2Q18E	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
($ in millions)	Sep-14	Sep-15	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Sep-18	Sep-19	Sep-20	Sep-21
Total Revenues	**37,580**	**41,373**	**36,881**	**9,182**	**9,083**	**9,850**	**10,145**	**38,260**	**10,229**	**9,766**	**10,573**	**10,474**	**41,042**	**41,993**	**42,895**	**43,821**
% change	9%	10%	-11%	0%	-1%	5%	11%	4%	11%	8%	7%	3%	7%	2%	2%	2%
Cost of Sales	34,895	37,456	32,184	7,699	8,036	8,648	8,794	33,177	8,778	8,497	9,067	9,168	35,511	36,095	36,796	37,594
Adjusted Gross Profit	**2,685**	**3,917**	**4,697**	**1,483**	**1,047**	**1,202**	**1,351**	**5,083**	**1,451**	**1,269**	**1,505**	**1,306**	**5,531**	**5,898**	**6,099**	**6,226**
SG&A	1,255	1,748	1,864	501	476	505	670	2,152	524	512	542	350	1,928	1,974	2,016	2,060
Adjusted EBIT	**1,642**	**2,253**	**2,833**	**982**	**623**	**756**	**902**	**3,263**	**950**	**757**	**963**	**956**	**3,626**	**3,924**	**4,083**	**4,167**
% change	19%	37%	26%	27%	-12%	-1%	54%	15%	-3%	21%	27%	6%	11%	8%	4%	2%
Net Interest Expense	125	284	243	56	55	69	92	272	86	86	85	80	336	338	291	241
Adjusted EBITDA	2,172	2,964	3,538	1,159	802	943	1,287	4,191	1,179	955	1,178	1,168	4,480	4,785	4,963	5,065
Adjusted Net Income	1,071	1,303	1,713	593	374	473	527	1,966	670	506	663	661	2,500	2,692	2,847	2,947
Adjusted EPS	**$2.94**	**$3.15**	**$4.39**	**$1.59**	**$1.01**	**$1.28**	**$1.43**	**$5.31**	**$1.81**	**$1.36**	**$1.79**	**$1.79**	**$6.75**	**$7.40**	**$8.05**	**$8.57**
% change	32%	7%	39%	38%	-6%	6%	49%	21%	14%	35%	40%	25%	27%	10%	9%	7%
Operating cash flow	1,178.0	2,570.0	2,716.0	1,134.0	(152.0)	467.0	1,150.0	2,599.0	1,126.0	385.5	745.4	1,123.2	3,380.0	3,536.2	3,683.5	3,797.6
Capex	632.0	854.0	695.0	200.0	267.0	315.0	287.0	1,069.0	296.0	364.3	394.4	390.7	1,445.3	1,049.8	1,072.4	1,095.5
Free cash flow	546.0	1,716.0	2,021.0	934.0	(419.0)	152.0	863.0	1,530.0	830.0	21.2	351.0	732.5	1,934.7	2,486.3	2,611.1	2,702.1
Net debt	7,740.0	6,037.0	5,930.0	5,660.0	6,205.0	10,593.0	9,885.0	9,885.0	9,393.0	9,506.5	9,315.0	8,766.8	8,766.8	7,642.6	6,446.2	5,209.6
Equity	8,904.0	9,706.0	9,624.0	9,567.0	9,789.0	10,137.0	10,559.0	10,559.0	11,974.0	12,345.4	12,849.0	13,325.7	13,325.7	14,653.1	16,082.6	17,561.2
# of diluted shares	364.3	414.0	390.5	373.0	370.0	370.0	369.0	370.5	371.0	371.0	370.7	370.0	370.7	363.8	353.8	343.8
Gross Margin (adjusted)	7.1%	9.5%	12.7%	16.2%	11.5%	12.2%	13.3%	13.3%	14.2%	13.0%	14.2%	12.5%	13.5%	14.0%	14.2%	14.2%
SG&A/sales	2.8%	4.0%	5.1%	5.5%	4.7%	4.5%	4.4%	4.8%	4.9%	5.2%	5.1%	3.3%	4.6%	4.7%	4.7%	4.7%
EBIT Margin (adjusted)	4.4%	5.4%	7.7%	10.7%	6.9%	7.7%	8.9%	8.5%	9.3%	7.8%	9.1%	9.1%	8.8%	9.3%	9.5%	9.5%
EBITDA Margin (adjusted)	5.8%	7.2%	9.6%	12.6%	8.8%	9.6%	12.7%	11.0%	11.5%	9.8%	11.1%	11.2%	10.9%	11.4%	11.6%	11.6%
FCF Margin	1.5%	4.1%	5.5%	10.2%	-4.6%	1.5%	8.5%	4.0%	8.1%	0.2%	3.3%	7.0%	4.7%	5.9%	6.1%	6.2%
Tax rate	31.6%	36.3%	31.8%	34.9%	34.3%	27.4%	31.9%	32.3%	24.3%	24.5%	24.5%	24.5%	24.5%	25.0%	25.0%	25.0%
Net debt/TTM EBITDA	3.6x	2.0x	1.7x	1.5x	1.7x	2.9x	2.4x	2.4x	2.2x	2.2x	2.0x	2.0x	2.0x	1.6x	1.3x	1.0x
Net debt/cap	47%	38%	38%	37%	39%	51%	48%	48%	44%	44%	42%	40%	40%	34%	29%	23%
ROIC	7.4%	7.9%	11.2%	19.0%	17.7%	15.3%	15.7%	10.4%	15.8%	16.4%	15.8%	17.2%	12.3%	12.5%	12.4%	11.9%

Source: Jefferies estimates, company data

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Chart 94: TSN - Segment Summary

Segment Summary	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17	1Q18	2Q18E	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
Chicken																
Sales	10,988	11,390	10,927	2,706	2,798	2,870	3,035	11,409	2,997	3,054	3,131	3,235	12,417	12,667	12,985	13,312
Reported EBIT	883	1,366	1,305	263	233	298	322	1,116	281	328	367	365	1,341	1,648	1,753	1,863
Adjusted EBIT	888	1,340	1,305	263	233	298	322	1,116	281	328	367	365	1,341	1,648	1,753	1,863
Adjusted EBIT margin	8.1%	11.8%	11.9%	9.7%	8.3%	10.4%	10.6%	9.8%	9.4%	10.7%	11.7%	11.3%	10.8%	13.0%	13.5%	14.0%
RTC (bn pounds)	8.9	9.1	9.0	2.2	2.2	2.3	2.3	9.1	2.4	2.3	2.3	2.4	9.4	9.5	9.6	9.7
EBIT per RTC pound ($ cents)	10.0	14.8	14.5	11.7	10.4	13.2	13.8	12.3	11.7	14.2	15.8	15.2	14.2	17.3	18.2	19.1
Beef																
Sales	16,177	17,236	14,513	3,528	3,487	4,000	3,808	14,823	3,886	3,661	4,200	3,998	15,746	15,903	16,062	16,223
Reported EBIT	347	-66	347	299	126	147	313	885	257	126	273	270	926	749	641	525
Adjusted EBIT	347	-53	347	299	126	147	313	885	257	126	273	270	926	749	641	525
Adjusted EBIT margin	2.1%	-0.3%	2.4%	8.5%	3.6%	3.7%	8.2%	6.0%	6.6%	3.5%	6.5%	6.8%	5.9%	4.7%	4.0%	3.2%
Cattle heads processed (M)	5.9	5.8	5.8	1.5	1.5	1.5	1.4	5.9	1.5	1.6	1.6	1.5	6.2	6.3	6.5	6.7
Adj EBIT per head ($)	59	-9	60	205	83	98	217	150	169	80	175	180	150	118	98	78
Pork																
Sales	6,304	5,262	4,909	1,252	1,302	1,322	1,362	5,238	1,283	1,361	1,382	1,424	5,450	5,587	5,727	5,871
Reported EBIT	455	380	528	247	141	136	124	648	152	105	101	92	450	499	517	536
Adjusted EBIT	455	373	528	247	141	136	124	648	152	105	101	92	450	499	517	536
Adjusted EBIT margin	7.2%	7.1%	10.8%	19.7%	10.8%	10.3%	9.1%	12.4%	11.8%	7.7%	7.3%	6.4%	8.3%	8.9%	9.0%	9.1%
Hog heads processed (M)	20.8	20.2	20.2	5.4	5.1	4.9	4.9	20.3	5.3	5.3	5.1	5.1	20.7	21.0	21.3	21.7
Adj EBIT per head ($)	22	18	26	46	28	28	25	32	29	20	20	18	22	24	24	25
Prepared Foods																
Sales	3,927	7,679	7,346	1,895	1,751	1,944	2,263	7,853	2,292	1,942	2,144	2,137	8,514	8,907	9,177	9,455
Reported EBIT	-60	588	734	190	139	195	152	676	273	211	235	241	960	1,058	1,192	1,262
Adjusted EBIT	53	636	734	190	139	195	152	676	273	211	235	241	960	1,058	1,192	1,262
Adjusted EBIT margin	1.3%	8.3%	10.0%	10.0%	7.9%	10.0%	6.7%	8.6%	11.9%	10.9%	11.0%	11.3%	11.3%	11.9%	13.0%	13.4%
International																
Sales	1,324	879	380	90	82	85	92	349	88	84	88	95	355	369	384	399
Reported EBIT	-37	-60	-81	-17	-16	-20	-9	-62	-13	-13	-13	-13	-52	-30	-20	-20
Adjusted EBIT	-79	-43	-81	-17	-16	-20	-9	-62	-13	-13	-13	-13	-52	-30	-20	-20
Adjusted EBIT margin	-6.0%	-4.9%	-21.3%	-18.9%	-19.5%	-23.5%	-9.8%	-17.8%	-14.8%	-15.4%	-14.8%	-13.7%	-14.7%	-8.1%	-5.2%	-5.0%

Source: Jefferies estimates, company data

Chart 95: FLO - Financial Summary

Financial Summary	FY13	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17E	1Q18E	2Q18E	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
($ in millions)	Dec-13	Dec-14	Dec-15	Dec-16	Apr-17	Jul-17	Oct-17	Dec-17	Dec-17	Apr-18	Jul-18	Oct-18	Dec-18	Dec-18	Dec-19	Dec-20	Dec-21
Total Revenues	**3,751**	**3,749**	**3,779**	**3,927**	**1,188**	**927**	**933**	**874**	**3,921**	**1,199**	**935**	**941**	**882**	**3,957**	**4,070**	**4,192**	**4,317**
% change	23%	0%	1%	4%	-1%	-1%	2%	1%	0%	1%	1%	1%	1%	1%	3%	3%	3%
Cost of Sales	1,972	1,951	1,963	2,026	608	468	476	457	2,009	604	466	476	450	1,996	2,038	2,085	2,133
Adjusted Gross Profit	**1,660**	**1,669**	**1,683**	**1,760**	**533**	**424**	**424**	**384**	**1,765**	**547**	**436**	**431**	**400**	**1,814**	**1,881**	**1,952**	**2,025**
SG&A	1,357	1,369	1,375	1,454	445	345	344	326	1,460	452	351	356	340	1,499	1,538	1,578	1,620
Adjusted EBIT	**303**	**300**	**309**	**306**	**87**	**80**	**79**	**59**	**305**	**95**	**84**	**75**	**60**	**315**	**343**	**373**	**405**
% change	33%	-1%	3%	-1%	-8%	-8%	15%	6%	0%	9%	6%	-5%	3%	3%	9%	9%	8%
Net Interest Expense	13	7	5	14	5	3	3	3	14	3	3	3	3	12	20	20	20
Adjusted EBITDA	421	429	441	447	133	114	112	91	450	142	118	109	92	462	494	528	564
Adjusted Net Income	192	192	197	194	53	51	48	36	187	68	61	54	43	226	241	263	287
Adjusted EPS	**$0.91**	**$0.90**	**$0.92**	**$0.92**	**$0.25**	**$0.24**	**$0.23**	**$0.17**	**$0.89**	**$0.32**	**$0.29**	**$0.26**	**$0.20**	**$1.07**	**$1.14**	**$1.25**	**$1.36**
% change	32%	-1%	2%	0%	-10%	-7%	9%	-3%	-3%	30%	19%	11%	20%	20%	7%	9%	9%
Operating cash flow	270.5	314.0	324.2	346.0	75.7	85.2	50.4	46.5	257.7	118.4	96.2	98.0	58.6	371.1	392.5	419.4	447.6
Capex	99.2	83.8	90.8	101.7	17.5	14.5	19.3	49.8	101.0	30.6	23.4	23.5	22.0	99.5	101.7	104.8	107.9
Free cash flow	171.3	230.2	233.5	244.3	58.2	70.7	31.1	(3.3)	156.7	87.8	72.8	74.5	36.5	271.6	290.8	314.6	339.6
Net debt	915.2	755.9	994.2	951.7	885.8	839.8	849.0	886.1	886.1	832.1	793.0	752.4	749.6	749.6	593.9	414.3	209.8
Equity	1,076.2	1,123.0	1,243.1	1,210.1	1,244.8	1,264.6	1,192.0	1,194.0	1,194.0	1,228.7	1,255.4	1,275.5	1,284.6	1,284.6	1,390.4	1,518.7	1,670.3
# of diluted shares	211.9	212.7	213.4	210.1	210.3	210.3	209.6	211.0	210.3	211.0	211.0	211.0	211.0	211.0	211.0	211.0	211.0
Gross Margin (adjusted)	44.3%	44.5%	44.5%	44.8%	44.8%	45.8%	45.4%	44.0%	45.0%	45.7%	46.6%	45.8%	45.4%	45.9%	46.2%	46.6%	46.9%
SG&A/sales	36.2%	36.5%	36.4%	37.0%	37.5%	37.2%	36.9%	37.3%	37.2%	37.7%	37.6%	37.8%	38.5%	37.9%	37.8%	37.7%	37.5%
EBIT Margin (adjusted)	8.1%	8.0%	8.2%	7.8%	7.4%	8.6%	8.5%	6.7%	7.8%	7.9%	9.0%	8.0%	6.9%	8.0%	8.4%	8.9%	9.4%
EBITDA Margin (adjusted)	11.2%	11.4%	11.7%	11.4%	11.2%	12.3%	12.0%	10.4%	11.5%	11.9%	12.6%	11.6%	10.5%	11.7%	12.1%	12.6%	13.1%
FCF Margin	4.6%	6.1%	6.2%	6.2%	4.9%	7.6%	3.3%	-0.4%	4.0%	7.3%	7.8%	7.9%	4.1%	6.9%	7.1%	7.5%	7.9%
Tax rate	33.6%	34.5%	35.5%	34.1%	36.1%	33.8%	37.0%	36.1%	35.7%	25.5%	25.5%	25.5%	25.5%	25.5%	25.5%	25.5%	25.5%
Net debt/TTM EBITDA	2.2x	1.8x	2.3x	2.1x	2.0x	1.9x	1.9x	2.0x	2.0x	1.8x	1.7x	1.6x	1.6x	1.6x	1.2x	0.8x	0.4x
Net debt/cap	46%	40%	44%	44%	42%	40%	42%	43%	43%	40%	39%	37%	37%	37%	30%	21%	11%
ROIC	12.1%	9.0%	9.6%	8.1%	9.6%	8.9%	8.4%	6.3%	8.2%	10.4%	9.3%	8.6%	6.9%	9.0%	10.0%	11.2%	12.4%

Source: Jefferies estimates, company data

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Chart 96: FLO - Segment Summary

Segment Summary	FY13	FY14	FY15	FY16	1Q17	2Q17	3Q17	4Q17	FY17E	1Q18E	2Q18E	3Q18E	4Q18E	FY18E	FY19E	FY20E	FY21E
Revenues		502	506														
DSD	3,098.0	3,155.6	3,179.3	3,284.2	999.9	792.9	787.3	738.6	3,318.6	1,009.9	800.8	795.1	745.9	3,351.7	3,452.3	3,555.9	3,662.5
% change	23.5%	1.9%	0.8%	3.3%	0.1%	0.9%	2.4%	1.1%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	3.0%	3.0%	3.0%
Warehouse	653.0	593.4	599.2	642.7	187.8	133.7	145.6	135.1	602.2	188.7	134.4	146.3	135.7	605.2	617.3	635.8	654.9
% change	21.5%	-9.1%	1.0%	7.3%	-8.6%	-10.4%	-2.9%	-2.3%	-6.3%	0.5%	0.5%	0.5%	0.5%	0.5%	2.0%	3.0%	3.0%
Total Revenues	**3,751**	**3,749**	**3,779**	**3,927**	**1,188**	**927**	**933**	**874**	**3,921**	**1,199**	**935**	**941**	**882**	**3,957**	**4,070**	**4,192**	**4,317**
% of Total																	
DSD	82.6%	84.2%	84.1%	83.6%	84.2%	85.6%	84.4%	84.5%	84.6%	84.3%	85.6%	84.5%	84.6%	84.7%	84.8%	84.8%	84.8%
Warehouse	17.4%	15.8%	15.9%	16.4%	15.8%	14.4%	15.6%	15.5%	15.4%	15.7%	14.4%	15.5%	15.4%	15.3%	15.2%	15.2%	15.2%
EBIT																	
DSD	300.5	293.5	306.9	295.9	88.2	79.6	78.9	60.8	307.5	96.7	86.4	78.1	63.0	324.1	351.1	379.4	409.1
EBIT margin	9.7%	9.3%	9.7%	9.0%	8.8%	10.0%	10.0%	8.2%	9.3%	9.6%	10.8%	9.8%	8.4%	9.7%	10.2%	10.7%	11.2%
% change	27.7%	-2.3%	4.5%	-3.6%	-4.1%	-0.7%	16.8%	8.2%	3.9%	9.6%	8.5%	-1.0%	3.6%	5.4%	8.3%	8.1%	7.8%
bps change	32 bp	-40 bp	35 bp	-64 bp	-38 bp	-16 bp	123 bp	54 bp	26 bp	75 bp	75 bp	-20 bp	21 bp	40 bp	50 bp	50 bp	50 bp
Warehouse	48.5	51.5	55.3	58.5	15.8	11.6	11.0	7.6	46.0	16.3	11.9	11.4	10.7	50.2	53.1	56.6	60.2
EBIT margin	7.4%	8.7%	9.2%	9.1%	8.4%	8.7%	7.6%	5.6%	7.6%	8.6%	8.9%	7.8%	7.9%	8.3%	8.6%	8.9%	9.2%
% change	33.9%	6.0%	7.4%	5.8%	-15.6%	-26.2%	-10.6%	-35.3%	-21.3%	2.9%	2.8%	3.2%	41.1%	9.2%	5.7%	6.6%	6.5%
bps change	69 bp	124 bp	55 bp	-13 bp	-70 bp	-186 bp	-65 bp	-286 bp	-146 bp	20 bp	20 bp	20 bp	226 bp	66 bp	30 bp	30 bp	30 bp
Corporate and other expenses	(46.0)	(44.9)	(53.6)	(48.4)	(16.6)	(11.6)	(10.5)	(9.9)	(48.6)	(18.0)	(14.0)	(14.1)	(13.2)	(59.4)	(61.0)	(62.9)	(64.8)
As % of revenues	1.2%	1.2%	1.4%	1.2%	1.4%	1.3%	1.1%	1.1%	1.2%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%
Total Adjusted EBIT	**303**	**300**	**309**	**306**	**87**	**80**	**79**	**59**	**305**	**95**	**84**	**75**	**60**	**315**	**343**	**373**	**405**
% of Total																	
DSD	86.1%	85.1%	84.7%	83.5%	84.8%	87.3%	87.8%	88.9%	87.0%	85.6%	87.9%	87.3%	85.5%	86.6%	86.9%	87.0%	87.2%
Warehouse	13.9%	14.9%	15.3%	16.5%	15.2%	12.7%	12.2%	11.1%	13.0%	14.4%	12.1%	12.7%	14.5%	13.4%	13.1%	13.0%	12.8%

Source: Jefferies estimates, company data

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Hormel Foods Corporation

Buy: $38 Price Target

Scenarios

Base Case

- Assumes no incremental contribution from M&A
- Refrigerated Foods segment EBIT up ~11% y/y driven by improved pork packer margins and improved mix owing to recent value-added acquisitions; segment EBIT margin expands ~85 bps y/y
- JOTS segment EBIT up 8% y/y (margins up ~60 bps) as oversupply in commodity turkey markets abates and turkey pricing improves significantly
- Consolidated EBIT up 8% y/y; margin up ~50 bps
- FY19 EPS: $2.00; Target Multiple: 19.0x; Target Price $38

Upside Scenario

- Company completes an accretive acquisition adding ~$350M in sales
- Refrig. Foods segment EBIT up ~13% y/y driven by strong pork cutout prices (better than expected pork demand) and improved value-added mix from recent acquisitions
- JOTS segment EBIT up 13% y/y owing to strong turkey demand growth in excess of supply
- Consolidated EBIT up 15% y/y; margin up ~70 bps
- FY19 EPS: $2.05; Target Multiple: 20.0x; Target Price $41

Downside Scenario

- Ref. Foods segment EBIT declines ~10% y/y as pork industry capacity expands faster than expected, outpacing hog supply growth and driving live hog prices meaningfully higher
- JOTS segment EBIT down 15% y/y as commodity oversupply situation worsens adding further pressure to turkey prices / producer margins
- Consolidated EBIT down 8% y/y; margin down ~90 bps
- FY19 EPS: $1.64; Target Multiple: 18.0x; Target Price $29

Investment Thesis / Where We Differ

- Near-term compression of pork packer margins likely not as bad as we previously feared and should be largely offset by recent acquisitions in Refrig. Foods
- Synergy guidance on recent deals seems conservative
- Although oversupply remains in commodity turkey markets, the situation seems to have stabilized – i.e. no meaningful improvement or deterioration for now
- HRL is becoming more aggressive in utilizing its solid balance sheet to do accretive M&A deals – we expect M&A to be a bigger driver of earnings growth over the next few years

Catalysts

- Movements in commodity pricing trends, particularly hogs, turkey and feed ingredients (corn and soybean meal)
- Additional pork industry capacity expansion announcements (or increases in number of shifts at existing facilities) is a potential negative catalyst
- Turkey supply growth indicators (reported by USDA)
- Potential acquisition announcements – we expect HRL to be more active in M&A in the near to mid-term

Long Term Analysis

Long Term Financial Model Drivers

LT Earnings CAGR	**10%**
Organic Revenue Growth	5%
Operating Margin Expansion, M&A and Deleveraging	5%

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General Mills, Inc.

Buy: $63 Price Target

Scenarios

Base Case

- Assumes ~1% organic sales growth y/y as market share losses and category growth trends stabilize
- Assumes no incremental contribution from M&A
- ~50 bps of gross margin expansion driven by improved volume growth, low y/y comps & continued solid execution on cost-savings plan
- EBIT margin expands ~50 bps y/y in line with gross margin expansion as improved cost-savings flow-through offsets increased investments in brand marketing to support new product launches
- Share price: $63. P/E multiple of 17.8x our FY19 base case EPS estimate of $3.55 (11% y/y growth)

Upside Scenario

- Organic sales up ~2% y/y driven by solid contribution from new product innovation, price/mix gains and improving market share trends
- Assumes no incremental contribution from M&A but we estimate there could be ~7-10% upside to our upside scenario EPS if the company were to make a transformative deal similar to the one we have hypothesized
- EBIT margin up ~50 bps y/y driven by stronger sales growth and solid execution on cost-savings initiative
- Share price: $70. P/E multiple of 19.5x our FY19 bull case EPS estimate of $3.61 (13% y/y growth)

Downside Scenario

- Organic sales decline ~2% y/y owing to weak category trends and continued market share losses. Sales from new products come in lower than expected
- Assumes no incremental contribution from M&A
- Gross margin contracts ~65 bps y/y as productivity gains are more than offset by volume deleverage and inflation
- SG&A/sales up ~25 bps as sales deleverage is partially offset by a pull-back in brand marketing and lower incentive comp; EBIT margin down ~90 bps y/y
- Share price: $48. P/E multiple of 15.5x our FY19 bear case EPS estimate of $3.13 (2% y/y decline)

Investment Thesis / Where We Differ

- Our BSM project gives us added confidence that, over time, GIS can unlock significant value from its underappreciated portfolio of leading brands, especially in the e-Commerce channel
- Recent reported results and scanner data point to improving sales growth trends – if this momentum can be sustained, we expect margin expansion (driven by cost-savings flow-through) to accelerate and for the stock to re-rate higher
- Significant untapped M&A optionality – buyout value at ~$70 & EPS accretion from transformative deal could be ~7-10%

Catalysts

- Monthly scanner data (e.g. Nielsen / IRI), particularly for the Yogurt, RTE Cereal and Snacks categories
- 3Q18 earnings (expected late March)
- Potential acquisitions announcements

Long Term Analysis

Long Term Financial Model Drivers (Company Guidance)

LT Earnings CAGR	**HSD**
Organic Revenue Growth	Low Single-Digit
Adjusted EBIT	Mid Single-Digit
Share Buybacks	2%
Dividend Yield	2-3%

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Tyson Foods, Inc.

Buy: $85 Price Target

Scenarios

Base Case

- Assumes Chicken segment margin of 13% (up~220 bps y/y), above the high end of management's normalized range
- Pork EBIT margin of 8.9% (up ~67bps y/y) assumes pork industry capacity expansion is largely offset by hog supply growth and solid demand
- Prepared Foods margin of 11.9% (up ~60bps y/y) driven by APFH synergy capture, partially offset by higher A&P expenses
- Share price: $85; P/E multiple of 11.5x; FY19 EPS of $7.40

Upside Scenario

- Assumes Chicken segment margin of 14.0% (above normalized range)
- Pork segment margin of 9.5% assumes pork industry capacity expansion is slower than expected and while hog supply and demand growth remain robust
- Prepared Foods margins improve to 12.5% (slightly above high end of normalized range) driven by higher than expected synergies related to APFH
- Share price: $122; P/E multiple of 15.0x; FY19 EPS of $8.11

Downside Scenario

- Assumes Chicken segment margin of ~9.5% (down ~130 bps y/y) driven by increased supply & higher grain prices
- Pork segment margin of 7.5% (down 80bps) as industry capacity expansion outpaces hog supply growth and demand is soft
- Prepared Foods margin is flat y/y as synergy capture is offset by higher brand marketing expenses
- Share price: $61; P/E multiple of 11.0x; FY19 EPS of $5.50

Investment Thesis / Where We Differ

- We believe FY18 guidance will likely end up being conservative given TSN's recent history of over-delivering on cost-savings/synergies (we would not be surprised if the company exceeds its AdvancePierre synergy guidance)
- Prepared Food margins (core to our thesis) should improve meaningfully y/y in FY18 and could be an incremental source of estimates upside relative to consensus
- Long term, we expect the stock to re-rate higher and trade more like a branded packaged food company as opposed to a commodity producer (owing to its increasing value-added mix)

Catalysts

- Chicken industry supply data (e.g: eggs set, pullet placements, breeder flock size, etc.) are potential read-throughs
- Movements in commodities prices (including chicken part prices, boxed beef and pork, corn and soybeans, live cattle and hogs) could serve as potential catalysts

Protein demand shocks within international markets (e.g. China, Mexico) could represent catalysts

Long-Term Analysis

Long-Term Financial Model Drivers

LT Earnings CAGR	**11%**
Organic Revenue Growth	1%
Operating Margin Expansion	6%

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Flower Foods Inc.

Hold $19 Price Target

Scenarios

Base Case

- Assumes ~3% organic sales growth driven by modest share gains and growth in organic bread sales (DKB)
- Stable market share trends in cake business
- Assumes ~50bps of EBIT margin expansion driven by Project Centennial cost savings and positive volume growth, resulting in better fixed cost absorption
- FY19 EPS: $1.14; Target Multiple: 16.6x; Target Price $19

Upside Scenario

- Organic sales growth accelerates to ~4% driven by share gains in bread, DKB growth and lower promotional activity
- Modest share gains in cake business
- Cost savings from Project Centennial come in higher than guidance implies
- EBIT margin expands ~120 bps y/y driven by Proj. Centennial cost savings and higher fixed cost absorption

FY19 EPS: $1.26; Target Multiple: 19.0x; Target Price $24

Downside Scenario

- Organic sales decline ~0.5% y/y driven by ineffective promotions and weak bread category sales growth
- Pricing environment does not rationalize
- EBIT margin contracts ~500 bps owing to lower than expected cost savings from Proj. Centennial, fixed cost deleverage and ineffective promotions

FY19 EPS: $0.97; Target Multiple: 15.5x; Target Price $15

Investment Thesis / Where We Differ

- The macro environment in FLO's categories remains challenged
- Increased focus on private label in the food space potentially represents a key threat especially in the bread and baked food category.
- Project Centennial initiatives can improve FLO's margin & earnings profile LT. However, NT execution risk is frontloaded while the cost savings are back-end loaded.

Catalysts

- Further developments on IO related litigation and/or DOL inquiry
- Monthly POS data showing improvements in bread industry pricing trends (i.e. less promotional activity) could positively impact sentiment on the stock
- Future updates on Project Centennial cost-savings progress
- Capital allocation – share buybacks and/or M&A

Long Term Analysis

Long Term Financial Model Drivers

LT Earnings CAGR	**8-10%**
Revenue Growth	**2-4%**
EBITDA margin	**13-14%**

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Company Description

Hormel Foods Corp. engages in the production of a variety of meat and food products and the marketing of those products throughout the U.S. and internationally. The company markets its products through Hormel Foods International Corp., a wholly owned subsidiary. It operates business through five segments: Grocery Products, Refrigerated Foods, Jennie-O Turkey Store, Specialty Foods and Other. The Grocery Products segment consists primarily of the processing, marketing, and sale of shelf-stable food products sold predominantly in the retail market. The Refrigerated Foods segment includes the Hormel Refrigerated operating segment and the Affiliated Business Units. This segment consists primarily of the processing, marketing, and sale of branded and unbranded pork and beef products for retail, foodservice and fresh product customers. The Jennie-O Turkey Store segment consists primarily of the processing, marketing, and sale of branded and unbranded turkey products for retail, foodservice and fresh product customers. The Specialty Foods segment includes the Diamond Crystal brands, Century Foods International, and Hormel Specialty Products operating segments. This segment consists of the packaging and sale of various sugar and sugar substitute products, salt and pepper products, liquid portion products, dessert mixes, ready-to-drink products, sports nutrition products, gelatin products, and private label canned meats to retail and foodservice customers. The All Other segment includes the Hormel Foods International operating segment, which manufactures, markets, and sells company products internationally. This segment also includes the results from the company's international joint ventures and miscellaneous corporate sales. Hormel Foods was founded by George A. Hormel in 1891 and is headquartered in Austin, MN.

General Mills, Inc. is a leading global manufacturer and marketer of branded consumer foods sold through retail stores and a leading supplier of branded and unbranded food products to the foodservice and commercial baking industries.

Tyson Foods, Inc. is a meat protein and food production company. It produces a wide range of fresh, value-added, frozen and refrigerated food products. It operates through the following segments: Chicken, Beef, Pork, Prepared Foods, and International. The Chicken segment handles domestic operations related to raising and processing live chickens into fresh, frozen, and value-added chicken products, as well as sales from allied products. The Beef segment includes operations related to processing live fed cattle and fabricating dressed beef carcasses into primal and sub-primal meat cuts and case-ready products. The Pork segment operates with live markets hogs and fabricating pork carcasses into primal and sub-primal cuts and case-ready products. The Prepared Foods segment manufactures and markets frozen and refrigerated food products and logistic operations to move products through the supply chain. The International segment includes foreign operations related to raising and processing live chickens into fresh, frozen and value-added chicken products. The company was founded by John W. Tyson in 1935 and is headquartered in Springdale, AR.

Flowers Foods, Inc. produces and markets packaged bakery foods in the U.S. It operates its business through two segments: Direct Store Delivery and Warehouse Delivery. The Direct Store Delivery segment markets a variety of fresh bakery foods, including fresh breads, buns, rolls, tortillas, and snack cakes. These products are sold through a DSD route delivery system to retail and foodservice customers from New England to Florida and west through the South, Southwest, and into California. The Warehouse Delivery segment produces snack cakes and breads and rolls for national retail, foodservice, vending, and co-pack customers, which are delivered through customers' warehouse channels and one bakery mix plant. The company markets its products under the brands names: Nature's Own, Wonder, Bluebird, Tastykake, Cobblestone Mill, Home Pride, Mary Jane & Friends, Captain John Derst's, Micasa, Broad Street Bakery, Mrs. Freshley's and Tesoritos. Flowers Foods was founded in 2000 and is headquartered in Thomasville, GA.

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I, Akshay Jagdale, certify that all of the views expressed in this research report accurately reflect my personal views about the subject security(ies) and subject company(ies). I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report.

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Investment Recommendation Record

(Article 3(1)e and Article 7 of MAR)

Recommendation Published	, 00:14 ET. February 14, 2018
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JEF is acting as financial advisor to Amplify Snack Brands in the sale of the company to The Hershey Co.

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Other Companies Mentioned in This Report

- Amazon.com, Inc (AMZN: $1,414.51, BUY)
- Amira Nature Foods Ltd. (ANFI: $4.03, BUY)
- Conagra Brands, Inc. (CAG: $35.47, BUY)
- Flowers Foods, Inc. (FLO: $20.67, HOLD)
- General Mills, Inc. (GIS: $54.79, BUY)
- Hain Celestial (HAIN: $33.27, BUY)
- Hormel Foods Corporation (HRL: $33.08, BUY)
- J &J Snack Foods Corp. (JJSF: $134.61, HOLD)
- Lamb Weston Holdings, Inc. (LW: $54.54, BUY)
- McCormick & Company, Inc. (MKC: $102.71, BUY)

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- Pinnacle Foods, Inc. (PF: $58.54, BUY)
- Snyder's-Lance, Inc. (LNCE: $49.97, HOLD)
- SodaStream International Ltd. (SODA: $78.61, HOLD)
- The J. M. Smucker Company (SJM: $119.69, BUY)
- The Kraft Heinz Company (KHC: $71.71, BUY)
- TreeHouse Foods, Inc. (THS: $41.39, BUY)
- Tyson Foods, Inc. (TSN: $74.73, BUY)

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			IB Serv./Past 12 Mos.		JIL Mkt Serv./Past 12 Mos.	
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