SMITHFIELD FOODS INC
Form 10-Q
December 06, 2013

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

FORM 10-Q

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

For the quarterly period ended October 27, 2013

COMMISSION FILE NUMBER 1-15321

SMITHFIELD FOODS, INC.

200 Commerce Street
Smithfield, Virginia 23430
(757) 365-3000

Virginia	52-0845861
(State of Incorporation)	(I.R.S. Employer Identification Number)

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

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

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

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

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

At November 29, 2013, 1,000 shares of the registrant's Common Stock (no par value per share) were outstanding.

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PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SMITHFIELD FOODS, INC.
CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(in millions and unaudited)

	Successor	Predecessor	
	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012
Sales	$1,139.1	$2,286.2	$3,225.8
Cost of sales	1,046.8	2,101.0	2,848.5
Gross profit	92.3	185.2	377.3
Selling, general and administrative expenses	63.4	140.5	205.7
Merger related costs	20.7	14.0	—
Income from equity method investments	(1.2)	(1.2)	(6.7)
Operating profit	9.4	31.9	178.3
Interest expense	31.1	22.8	41.5
Loss on debt extinguishment	—	—	120.7
(Loss) income before income taxes	(21.7)	9.1	16.1
Income tax (benefit) expense	(5.1)	(3.3)	5.2
Net (loss) income	$(16.6)	$12.4	$10.9

	Successor	Predecessor	
	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012
Sales	$1,139.1	$5,679.5	$6,317.1
Cost of sales	1,046.8	5,190.1	5,607.6
Gross profit	92.3	489.4	709.5
Selling, general and administrative expenses	63.4	341.7	406.8
Merger related costs	20.7	18.0	—
(Income) loss from equity method investments	(1.2)	0.5	(7.4)
Operating profit	9.4	129.2	310.1
Interest expense	31.1	64.6	84.0
Loss on debt extinguishment	—	—	120.7
(Loss) income before income taxes	(21.7)	64.6	105.4
Income tax (benefit) expense	(5.1)	12.7	32.8
Net (loss) income	$(16.6)	$51.9	$72.6

See Notes to Consolidated Condensed Financial Statements

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SMITHFIELD FOODS, INC.
CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME
(in millions and unaudited)

	Successor	Predecessor	
	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012
Net (loss) income	$(16.6)	$12.4	$10.9
Other comprehensive income (loss), net of tax:			
Foreign currency translation	27.9	12.6	49.5
Pension accounting	—	6.0	8.0
Hedge accounting	(4.3)	(7.0)	(28.9)
Total other comprehensive income	23.6	11.6	28.6
Comprehensive income	$7.0	$24.0	$39.5

	Successor	Predecessor	
	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012
Net (loss) income	$(16.6)	$51.9	$72.6
Other comprehensive income (loss), net of tax:			
Foreign currency translation	27.9	16.9	(34.6)
Pension accounting	—	15.1	16.2
Hedge accounting	(4.3)	(34.0)	30.3
Total other comprehensive income (loss)	23.6	(2.0)	11.9
Comprehensive income	$7.0	$49.9	$84.5

See Notes to Consolidated Condensed Financial Statements

SMITHFIELD FOODS, INC.
CONSOLIDATED CONDENSED BALANCE SHEETS
(in millions, except share data, and unaudited)

	Successor October 27, 2013	Predecessor April 28, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$134.1	$310.6
Accounts receivable, net	808.2	663.2
Inventories	2,527.8	2,348.3
Prepaid expenses and other current assets	210.1	229.7
Total current assets	3,680.2	3,551.8
Property, plant and equipment, net	2,750.6	2,298.4
Goodwill	1,601.8	782.4
Investments	499.8	532.4
Intangible assets, net	1,406.3	390.4
Other assets	175.9	161.0
Total assets	$10,114.6	$7,716.4
LIABILITIES AND EQUITY		
Current liabilities:		
Current portion of long-term debt and capital lease obligations	$63.1	$676.1
Accounts payable	518.7	429.1
Accrued expenses and other current liabilities	618.0	641.0
Total current liabilities	1,199.8	1,746.2
Long-term debt and capital lease obligations	3,376.1	1,829.2
Other liabilities	1,321.5	1,030.6
Redeemable noncontrolling interests	47.2	12.7
Commitments and contingencies		
Equity:		
Shareholders' equity:		
Preferred stock, $1.00 par value, 1,000,000 authorized shares (Predecessor)	—	—
Common stock, no par value, 1,000 shares authorized; 1,000 issued and outstanding (Successor)	—	—
Common stock, $.50 par value, 500,000,000 authorized shares; 138,919,056 issued and outstanding (Predecessor)	—	69.5
Additional paid-in capital	4,162.4	1,389.9
Stock held in trust	—	(68.8)
Retained (losses) earnings	(16.6)	2,322.6
Accumulated other comprehensive income (loss)	23.6	(616.2)
Total shareholders’ equity	4,169.4	3,097.0
Noncontrolling interests	0.6	0.7
Total equity	4,170.0	3,097.7

Total liabilities and equity	$10,114.6	$7,716.4

See Notes to Consolidated Condensed Financial Statements

SMITHFIELD FOODS, INC.
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(in millions and unaudited)

	Successor	Predecessor	
	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012
Cash flows from operating activities:			
Net (loss) income	$(16.6)	$51.9	$72.6
Adjustments to reconcile net cash flows from operating activities:			
Depreciation and amortization	18.0	106.5	117.7
(Income) loss from equity method investments	(1.2)	0.5	(7.4)
Impact of inventory fair value step-up on cost of sales	24.8	—	—
Pension expense	4.0	44.8	48.0
Pension contributions	—	(9.7)	(8.6)
Changes in operating assets and liabilities and other, net	(70.9)	(219.8)	(412.8)
Net cash flows from operating activities	(41.9)	(25.8)	(190.5)
Cash flows from investing activities:			
Acquisition of Smithfield Foods, Inc. common stock	(4,896.6)	—	—
Capital expenditures	(13.8)	(139.8)	(127.7)
Business acquisitions, net of cash acquired	—	(32.8)	(23.1)
Net proceeds (expenditures) from breeding stock transactions	2.1	(5.3)	(13.4)
Proceeds from the sale of property, plant and equipment	1.3	1.7	10.7
Advance note	—	(10.0)	—
Net cash flows from investing activities	(4,907.0)	(186.2)	(153.5)
Cash flows from financing activities:			
Net proceeds from equity contribution	4,162.1	—	—
Proceeds from the issuance of long-term debt	900.0	—	1,019.2
Principal payments on long-term debt and capital lease obligations	(200.5)	(458.7)	(711.4)
Proceeds from Securitization Facility	—	170.0	—
Payments on Securitization Facility	—	(50.0)	—
Net (payments) proceeds from revolving credit facilities	(11.0)	490.3	66.7
Repurchase of common stock	—	—	(212.3)
Debt issuance cost and other	(20.1)	0.1	(17.9)
Net cash flows from financing activities	4,830.5	151.7	144.3
Effect of foreign exchange rate changes on cash	2.0	0.2	(1.0)
Net change in cash and cash equivalents	(116.4)	(60.1)	(200.7)
Cash and cash equivalents at beginning of period	250.5	310.6	324.3
Cash and cash equivalents at end of period	$134.1	$250.5	$123.6

See Notes to Consolidated Condensed Financial Statements

SMITHFIELD FOODS, INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Organization

Smithfield Foods, Inc., together with its subsidiaries ("Smithfield," "the Company," "we," "us" or "our"), is the largest hog producer and pork processor in the world. We produce and market a wide variety of fresh meat and packaged meats products both domestically and internationally. We conduct our operations through four reportable segments: Pork, Hog Production, International and Corporate, each of which is comprised of a number of subsidiaries, joint ventures and other investments.

On September 26, 2013 (the Merger Date), pursuant to the Agreement and Plan of Merger dated May 28, 2013 (the Merger Agreement) with Shuanghui International Holdings Limited, a corporation formed under the laws of the Cayman Islands (Shuanghui), the Company merged with Sun Merger Sub, Inc., a Virginia corporation and wholly owned subsidiary of Shuanghui (the Merger Sub), in a transaction hereinafter referred to as the Merger. As a result of the Merger, the Company survived as a wholly owned subsidiary of Shuanghui. See Note 2—Merger and Acquisition for further information on the Merger.

Basis of Presentation

The Merger was accounted for as a business combination using the acquisition method of accounting in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification 805, Business Combinations. Shuanghui's cost of acquiring the Company has been pushed-down to establish a new accounting basis for the Company. Accordingly, the interim consolidated condensed financial statements are presented for two periods, Predecessor and Successor, which relate to the accounting periods preceding and succeeding the completion of the Merger. The Predecessor and Successor periods have been separated by a vertical line on the face of the consolidated financial statements to highlight the fact that the financial information for such periods has been prepared under two different historical-cost bases of accounting.

Successor—The consolidated financial statements as of October 27, 2013, and for the period from September 27, 2013 through October 27, 2013, include the accounts of the Company subsequent to the closing of the Merger on September 26, 2013.

Predecessor—The consolidated condensed financial statements of the Company prior to the Merger on September 26, 2013.

The accompanying unaudited consolidated condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. You should read these statements in conjunction with the audited consolidated financial statements and the related notes included in our Annual Report on Form 10-K for the fiscal year ended April 28, 2013. The information reflects all normal recurring adjustments which we believe are necessary to present fairly the financial position and results of operations for all periods included.

Recently Issued Accounting Pronouncements

In July 2013, FASB issued guidance on the financial statement presentation of certain unrecognized tax benefits when a net operating loss carryforward, similar tax loss or tax credit carryforward exists. The new guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2013. The guidance is not currently effective for us and has not been applied in this Form 10-Q.

NOTE 2: MERGER AND ACQUISITION

Shuanghui Merger

On May 28, 2013, we entered into the Merger Agreement with Shuanghui and the Merger Sub. The Merger was consummated on September 26, 2013, and as a result, Merger Sub merged with and into the Company, with the Company surviving as a wholly owned subsidiary of Shuanghui. Upon completion of the Merger, Shuanghui acquired all outstanding shares of Smithfield and the Company's shareholders received $34.00 in cash (the Merger Consideration) for each share of common stock held prior to the effective time of the Merger. Additionally, all outstanding stock-based compensation awards, both vested and unvested, were converted into the right to receive the Merger Consideration, less the exercise price of such awards, if any. The total consideration paid in connection with the Merger was approximately $4.9 billion.

On July 31, 2013, the Merger Sub issued $500.0 million aggregate principal amount of 5.25% senior notes due August 1, 2018 and $400.0 million aggregate principal amount of 5.875% senior notes due August 1, 2021 (together, the Merger Sub Notes). The Merger Sub incurred $20.4 million in transaction fees in connection with issuance of the Merger Sub Notes, which are being amortized over the life of the Merger Sub Notes. As a result of the Merger and the transactions entered into in connection therewith, we have assumed the liabilities and obligations of the Merger Sub, including the Merger Sub's obligations under the Merger Sub Notes. Proceeds from the Merger Sub Notes were held in escrow prior to the Merger Date and used in funding the Merger. The proceeds were used to fund a portion of the total consideration paid, repay certain outstanding debt of the Company and pay certain transaction fees associated with the Merger.

Shuanghui is the majority shareholder of Henan Shuanghui Investment & Development Co., which is China's largest meat processing enterprise and China's largest publicly traded meat products company as measured by market capitalization. Shuanghui is a pioneer in the Chinese meat processing industry with over 30 years of history. Shuanghui's businesses include hog production, meat processing, fresh meat and packaged meats production and distribution. The merging of Shuanghui's distribution network with our strong management team, leading brands and vertically integrated model will allow us to provide high-quality, competitively priced and safe U.S. meat products to consumers in markets around the world.

Shuanghui's cost of acquiring the Company has been pushed-down to establish a new accounting basis for the Company. The preliminary allocation of consideration to the assets acquired and liabilities assumed by Shuanghui in the Merger reflects preliminary fair value estimates based on management's analysis, including preliminary work performed by third-party valuation specialists, which are subject to change within the measurement period as valuations are finalized. Measurement period adjustments that the Company determines to be material will be applied retrospectively to the Merger Date.

The following is a summary of the preliminary allocation of the total purchase consideration to the estimated fair values of our assets acquired, liabilities assumed and noncontrolling interests by Shuanghui in the transaction:

	(in millions)
Cash and cash equivalents	$250.5
Accounts receivable	764.8
Inventories	2,506.9
Prepaid expenses and other current assets	215.0
Property, plant and equipment	2,743.7
Goodwill	1,601.8
Investments	495.5
Intangible assets	1,403.0
Other assets	171.2
Assets acquired by Shuanghui	10,152.4
Current portion of long-term debt and capital lease obligations	239.1
Accounts payable	535.3
Accrued expenses and other current liabilities	576.2
Long-term debt and capital lease obligations	2,509.1
Other liabilities	1,341.5
Liabilities assumed by Shuanghui	5,201.2
Redeemable noncontrolling interests and noncontrolling interests	48.2
Total purchase consideration	$4,903.0

Accounts receivable and accounts payable, as well as certain other current and non-current assets and liabilities, were valued at their existing carrying values as they approximated fair value of those items at the time of the Merger, based on management's judgments and estimates.

Inventories were valued using a net realizable value approach with the exception of manufacturing supplies and other inventories, which were valued using the replacement cost approach.

Property, plant and equipment have been valued using a combination of the market approach and the indirect cost approach which is based on current replacement and/or reproduction cost of the asset as new, less depreciation attributable to physical, functional, and economic factors.

Intangible assets acquired include trademarks, customer relations assets, contractual relationships and rights with fair values of $1.3 billion, $55.0 million, $40.0 million and $3.0 million, respectively. The customer relations assets, contractual relationships and rights will be amortized over useful lives of 14 years, 17 years and 12 years, respectively. The trademarks are not subject to amortization.

Trademarks have been valued using the relief from royalty method. We utilized a bottoms-up approach to assess the appropriate royalty rates for trade names focused on consideration of the profitability of each trade name, the implied premium margin earned on branded versus private label sales of similar products for each trade name, market studies, and third-party comparable licensing agreements.

Customer relations assets were determined using the multi-period excess earnings methodology utilizing our forecasted metrics and/or a market participant distributor model.

Contractual relationships were valued based on the time and associated costs that would be required to recreate the existing relationships in addition to the lost profits over this time period using the avoided costs or lost profits method. Rights were also valued using an avoided costs or lost profits method.

The benefit obligation for both our qualified and non-qualified defined benefit pension plans was remeasured as of the Merger Date with the assistance of an independent third-party actuary.
Existing long-term debt assumed in the Merger was fair valued based on quoted market prices. Long-term debt assumed included our outstanding 6.625% senior unsecured notes due August 2022 (the 2022 Notes) and our outstanding 7.75% senior unsecured notes due July 2017 (the 2017 Notes).
Deferred income tax assets and liabilities as of the acquisition date represent the expected future tax consequences of temporary differences between the fair values of the assets acquired and the liabilities assumed as a result of the Merger and their tax basis.
Goodwill reflects the amount of the total consideration paid that exceeded the fair value of the identifiable assets acquired, liabilities assumed and noncontrolling interests. Goodwill recognized as a result of the Merger has not been allocated to our reportable segments as of October 27, 2013. The amount of goodwill relating to the Merger that is expected to be deductible for tax purposes has not yet been determined.
In connection with the Merger, we incurred $20.7 million and $18.0 million of professional fees during the Successor and Predecessor periods, respectively. These fees are recognized in merger related costs on the consolidated condensed statements of income. In addition, the Merger Sub deferred $17.3 million of debt issuance costs for a financing arrangement. We recognized these deferred costs in interest expense during the Successor period upon termination of the financing arrangement following the Merger. All of these charges are reflected in the results of our Corporate segment.
The following unaudited pro forma financial data summarizes the Company's results of operations as if the Merger had occurred as of April 29, 2012. The pro forma data is for informational purposes only and may not necessarily reflect the actual results of operations had the Merger been consummated on April 29, 2012.

	Three Months Ended		Six Months Ended	
	October 27, 2013	October 28, 2012	October 27, 2013	October 28, 2012
		(in million)		
Sales	$3,425.3	$3,225.8	$6,818.6	$6,317.1
Net income	$57.3	$29.8	$115.9	$86.4

The most significant pro forma adjustments were to reflect the impact of fair value step-ups of both assets and liabilities (e.g., inventory, property, plant and equipment, long-term debt) and fees and expenses related to the Merger noted above.
Kansas City Sausage Company, LLC
In May 2013, we acquired a 50% interest in Kansas City Sausage Company, LLC (KCS) for $36.0 million in cash. Upon closing, in addition to the cash purchase price, we advanced $10.0 million to the seller in exchange for a promissory note, which is secured by the remaining membership interests in KCS held by the seller (the Advance Note). The Advance Note was recorded in other assets in the consolidated condensed balance sheet. Additionally, we entered into a revolving loan agreement with KCS, under which we agreed to make loans from time to time up to an aggregate principal amount of $20.0 million. The aggregate amount of any obligations incurred under the revolving loan agreement is secured by a first priority security interest in all of the assets of KCS.
KCS is a leading U.S. sausage producer and sow processor with annual revenues of approximately $200 million. The merging of KCS's low-cost, efficient operations and high-quality products with our strong brands and sales and marketing team should contribute growth in our packaged meats business. KCS operates in Des Moines, Iowa and Kansas City, Missouri. In Des Moines, KCS produces premium raw materials for sausage, as well as value-added products, including boneless hams and hides. The Kansas City plant is a modern sausage processing facility and is designed for optimum efficiency to provide retail and foodservice customers with high quality products. With our strong ongoing focus on building our packaged meats business, and with 15% of the U.S. sow population, this joint venture is a logical fit for the Company. It is expected to provide a growth platform in two key packaged meats categories — breakfast sausage and dinner sausage — and to allow us to expand our product offerings to our customers. These categories represent over $4.0 billion in industry retail and foodservice sales annually.

KCS is managed by its Board of Directors, which makes decisions that most significantly impact the economic performance of KCS. We have the right to nominate and elect the majority of the members of the Board of Directors of KCS, and based on the associated voting rights, we have determined that we have a controlling financial interest in KCS. As a result, the acquisition of our interest in KCS was accounted for in the Pork segment using the acquisition method of accounting, which requires, among other things, that assets acquired, liabilities assumed and noncontrolling interests in the acquiree be recognized at their fair values as of the acquisition date. The purchase price allocation includes assets acquired, excluding goodwill, of $39.2 million, liabilities assumed of $10.7 million, goodwill of $43.5 million and redeemable noncontrolling interest of $36.0 million.

Our initial estimate of the fair value of the noncontrolling interest was measured based on market multiples for similar companies in our industry and consideration of the terms of the acquisition, which provide the noncontrolling interest holder the right to exercise a put option at any time after the fifth anniversary of the acquisition, which would obligate us to redeem their interest. The noncontrolling interest is classified outside of equity as redeemable noncontrolling interests in the consolidated condensed balance sheet. The redemption amount is the greater of $45.0 million or the result of a computed amount based on a fixed multiple of earnings. We have elected to accrete changes in the redemption amount of the noncontrolling interest over the five year period until it becomes redeemable. If the noncontrolling interest had been redeemable as of October 27, 2013, the redemption amount would have been $45.0 million.

NOTE 3: INVENTORIES

Inventories consist of the following:

	Successor October 27, 2013	Predecessor April 28, 2013
	(in millions)	
Livestock	$1,169.6	$1,113.5
Fresh and packaged meats	1,129.1	960.8
Grains	112.7	162.0
Manufacturing supplies	65.3	57.7
Other	51.1	54.3
Total inventories	$2,527.8	$2,348.3

NOTE 4: DERIVATIVE FINANCIAL INSTRUMENTS

Our meat processing and hog production operations use various raw materials, primarily live hogs, corn and soybean meal, which are actively traded on commodity exchanges. We hedge these commodities when we determine conditions are appropriate to mitigate price risk. While this hedging may limit our ability to participate in gains from favorable commodity fluctuations, it also tends to reduce the risk of loss from adverse changes in raw material prices. We attempt to closely match the commodity contract terms with the hedged item. We also periodically enter into interest rate swaps to hedge exposure to changes in interest rates on certain financial instruments and foreign exchange forward contracts to hedge certain exposures to fluctuating foreign currency rates.

We record all derivatives in the balance sheet as either assets or liabilities at fair value. Accounting for changes in the fair value of a derivative depends on whether it qualifies and has been designated as part of a hedging relationship. For derivatives that qualify and have been designated as hedges for accounting purposes, changes in fair value have no net impact on earnings, to the extent the derivative is considered perfectly effective in achieving offsetting changes in fair value or cash flows attributable to the risk being hedged, until the hedged item is recognized in earnings (commonly referred to as the “hedge accounting” method). For derivatives that do not qualify or are not designated as hedging instruments for accounting purposes, changes in fair value are recorded in current period earnings (commonly referred to as the “mark-to-market” method). We may elect either method of accounting for our derivative portfolio, assuming all the necessary requirements are met. We have in the past availed ourselves of either acceptable method and expect to do so in the future. We believe all of our derivative instruments represent economic hedges against changes in prices and rates, regardless of their designation for accounting purposes.

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We do not offset the fair value of derivative instruments with cash collateral held with or received from the same counter-party under a master netting arrangement. As of October 27, 2013, prepaid expenses and other current assets included $26.0 million representing cash on deposit with brokers to cover losses on our open derivative instruments. As of October 27, 2013, we had no cash on hand to cover gains on our open derivative instruments. Changes in commodity prices could have a significant impact on cash deposit requirements under our broker and counter-party agreements. Additionally, certain of our derivative contracts contain credit risk-related contingent features, which would require us to post additional cash collateral to cover net losses on open derivative instruments if our credit rating was downgraded. As of October 27, 2013, the net liability position of our open derivative instruments that are subject to credit risk related contingent features was not material.

We are exposed to losses in the event of nonperformance or nonpayment by counter-parties under financial instruments. Although our counter-parties primarily consist of financial institutions that are investment grade, there is still a possibility that one or more of these companies could default. However, a majority of our financial instruments are exchange traded futures contracts held with brokers and counter-parties with whom we maintain margin accounts that are settled on a daily basis, thereby limiting our credit exposure to non-exchange traded derivatives. Determination of the credit quality of our counter-parties is based upon a number of factors, including credit ratings and our evaluation of their financial condition. As of October 27, 2013, we had credit exposure of $2.0 million on non-exchange traded derivative contracts, excluding the effects of netting arrangements. As a result of netting arrangements, we had no credit exposure as of October 27, 2013. No significant concentrations of credit risk existed as of October 27, 2013.

The size and mix of our derivative portfolio varies from time to time based upon our analysis of current and future market conditions. All derivative contracts are recorded in prepaid expenses and other current assets or accrued expenses and other current liabilities within the consolidated condensed balance sheets, as appropriate.

The following table presents the fair values of our open derivative financial instruments in the consolidated condensed balance sheets on a gross basis.

	Assets		Liabilities	
	Successor	Predecessor	Successor	Predecessor
	October 27, 2013	April 28, 2013	October 27, 2013	April 28, 2013
	(in millions)		(in millions)	
Derivatives using the "hedge accounting" method:				
Grain contracts	$1.1	$2.5	$8.3	$73.0
Livestock contracts	—	4.1	3.4	1.1
Foreign exchange contracts	0.7	0.2	0.1	0.1
Total	1.8	6.8	11.8	74.2
Derivatives using the "mark-to-market" method:				
Grain contracts	—	6.2	0.1	13.7
Livestock contracts	1.4	12.4	4.3	0.7
Energy contracts	0.4	3.1	0.3	0.6
Foreign exchange contracts	0.2	0.6	0.5	0.3
Total	2.0	22.3	5.2	15.3
Total fair value of derivative instruments	$3.8	$29.1	$17.0	$89.5

Hedge Accounting Method

Cash Flow Hedges

We enter into derivative instruments, such as futures, swaps and options contracts, to manage our exposure to the variability in expected future cash flows attributable to commodity price risk associated with the forecasted sale of live hogs and fresh pork, and the forecasted purchase of corn and soybean meal. In addition, we enter into foreign exchange contracts to manage our exposure to the variability in expected future cash flows attributable to changes in foreign exchange rates associated with the forecasted purchase or sale of assets denominated in foreign currencies. As

of October 27, 2013, we had no cash flow hedges for forecasted transactions beyond December 2014.

When cash flow hedge accounting is applied, derivative gains or losses are recognized as a component of other comprehensive income (loss) and reclassified into earnings in the same period or periods during which the hedged transactions affect earnings. Derivative gains and losses, when reclassified into earnings, are recorded in cost of sales for grain contracts, sales for lean hog contracts and selling, general and administrative expenses (SG&A) for foreign exchange contracts. Gains and losses on derivatives designed to hedge price risk associated with fresh pork sales are recorded in the Hog Production segment.

During the six months ended October 27, 2013, the range of notional volumes associated with open derivative instruments designated in cash flow hedging relationships was as follows:

	Minimum	Maximum	Metric
Commodities:			
Corn	48,440,000	86,625,000	Bushels
Soybean meal	321,414	581,656	Tons
Lean hogs	86,600,000	777,360,000	Pounds
Foreign currency [1]	22,189,407	48,005,327	U.S. Dollars

[1] Amounts represent the U.S. dollar equivalent of various foreign currency contracts.

The following tables present the effects on our consolidated condensed financial statements of pre-tax gains and losses on derivative instruments designated in cash flow hedging relationships for the fiscal periods indicated:

	Gains (Losses) Recognized in Other Comprehensive Income (Loss) on Derivative (Effective Portion)			Gains (Losses) Reclassified from Accumulated Other Comprehensive Loss into Earnings (Effective Portion)			Gains (Losses) Recognized in Earnings on Derivative (Ineffective Portion)		
	Successor	Predecessor		Successor	Predecessor		Successor	Predecessor	
	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012
	(in millions)			(in millions)			(in millions)		
Commodity contracts:									
Grain contracts	$(6.8)	$7.5	$(4.4)	$(0.1)	$(1.4)	$18.9	$(1.6)	$(0.5)	$0.7
Lean hog contracts	(0.8)	(24.6)	(1.4)	0.2	(3.2)	25.6	—	(0.8)	0.2
Foreign exchange contracts	0.7	0.6	1.6	—	(0.2)	(0.4)	—	—	—
Total	$(6.9)	$(16.5)	$(4.2)	$0.1	$(4.8)	$44.1	$(1.6)	$(1.3)	$0.9

	Successor	Predecessor		Successor	Predecessor		Successor	Predecessor	
	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012
	(in millions)			(in millions)			(in millions)		

Commodity contracts:									
Grain contracts	$(6.8)	$3.1	$ 129.5	$(0.1)	$23.6	$ 21.6	$(1.6)	$1.3	$ 3.4
Lean hog contracts	(0.8)	(29.3)	(1.1)	0.2	5.9	57.8	—	(0.8)	0.3
Foreign exchange contracts	0.7	(0.4)	(0.2)	—	(0.3)	(0.6)	—	—	—
Total	$(6.9)	$(26.6)	$ 128.2	$0.1	$29.2	$ 78.8	$(1.6)	$0.5	$ 3.7

For the fiscal periods presented, foreign exchange contracts were determined to be highly effective. We have excluded from the assessment of effectiveness differences between spot and forward rates, which we have determined to be immaterial.

As of October 27, 2013, there were deferred net losses of $4.4 million, net of tax of $2.9 million, in accumulated other comprehensive income (loss). We expect to reclassify $1.6 million ($1.0 million net of tax) of deferred net gains on closed commodity contracts into earnings within the next twelve months. We are unable to estimate the amount of unrealized gains or losses to be reclassified into earnings within the next twelve months related to open contracts as their values are subject to change.

Fair Value Hedges

We enter into derivative instruments (primarily futures contracts) that are designed to hedge changes in the fair value of live hog inventories and firm commitments to buy grains. When fair value hedge accounting is applied, derivative gains and losses are recognized in earnings currently along with the change in fair value of the hedged item attributable to the risk being hedged. The gains or losses on the derivative instruments and the offsetting losses or gains on the related hedged items are recorded in cost of sales for commodity contracts.

During the six months ended October 27, 2013, the range of notional volumes associated with open derivative instruments designated in fair value hedging relationships was as follows:

	Minimum	Maximum	Metric
Commodities:			
Corn	—	4,130,000	Bushels

The following tables present the effects on our consolidated condensed statements of income of gains and losses on derivative instruments designated in fair value hedging relationships and the related hedged items for the fiscal periods indicated:

	Gains (Losses) Recognized in Earnings on Derivative			Gains (Losses) Recognized in Earnings on Related Hedged Item		
	Successor	Predecessor		Successor	Predecessor	
	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012
	(in millions)			(in millions)		
Commodity contracts	$—	0.1	$7.7	$—	$(0.1)	$(9.1)

	Successor	Predecessor		Successor	Predecessor	
	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012
	(in millions)			(in millions)		
Commodity contracts	$—	$0.5	$(18.7)	$—	$(0.5)	$11.2

In connection with the Merger, we closed all commodity derivative contracts on September 26, 2013. As a result, we did not recognize gain or losses during the Successor period September 27 - October 27, 2013 on closed commodity derivative contracts. We recognized gains of $2.0 million during the Predecessor period July 29 - September 26, 2013 and $1.1 million for the three months ended October 28, 2012 on closed commodity derivative contracts as the underlying cash transactions affected earnings. We recognized gains of $4.1 million during the Predecessor period April 29 - September 26, 2013, and $4.5 million for the six months ended October 28, 2012 on closed commodity derivative contracts as the underlying cash transactions affected earnings.

For fair value hedges of inventory, we elect to exclude from the assessment of effectiveness differences between the spot and futures prices. These differences are recorded directly into earnings as they occur. These differences resulted in losses of $1.2 million for the three months ended October 28, 2012 and losses of $7.5 million for the six months ended October 28, 2012. There were no fair value hedges of inventory during the six months ended October 27, 2013,

and therefore no differences between spot and futures prices were recognized during the Successor period ended October 27, 2013 nor during the Predecessor period April 29 - September 26, 2013.

Mark-to-Market Method

Derivative instruments that are not designated as a hedge, have been de-designated from a hedging relationship, or do not meet the criteria for hedge accounting are marked-to-market with the unrealized gains and losses together with actual realized gains and losses from closed contracts being recognized in current period earnings. Under the mark-to-market method, gains and losses are recorded in cost of sales for commodity contracts, and SG&A for foreign exchange contracts.

During the six months ended October 27, 2013, the range of notional volumes associated with open derivative instruments using the "mark-to-market" method was as follows:

	Minimum	Maximum	Metric
Commodities:			
Lean hogs	3,280,000	82,400,000	Pounds
Corn	25,000	10,115,000	Bushels
Soybean meal	—	34,145	Tons
Soybeans	—	1,220,000	Bushels
Wheat	—	750,000	Bushels
Natural gas	8,470,000	10,870,000	Million BTU
Diesel	1,764,000	3,360,000	Gallons
Foreign currency [1]	22,987,556	60,968,251	U.S. Dollars

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[1] Amounts represent the U.S. dollar equivalent of various foreign currency contracts.

The following tables present the amount of gains and losses recognized in the consolidated condensed statements of income on derivative instruments using the "mark-to-market" method by type of derivative contract for the fiscal periods indicated:

	Successor	Predecessor	
	September 27 - October 27, 2013	July 29 - September 26, 2013	Three Months Ended October 28, 2012
	(in millions)		
Commodity contracts	$1.7	$2.5	$17.1
Foreign exchange contracts	0.4	0.1	(0.4)
Total	$2.1	$2.6	$16.7

	Successor	Predecessor	
	September 27 - October 27, 2013	April 29 - September 26, 2013	Six Months Ended October 28, 2012
	(in millions)		
Commodity contracts	$1.7	$8.5	$8.9
Foreign exchange contracts	0.4	(0.2)	4.2
Total	$2.1	$8.3	$13.1

The tables above reflect gains and losses from both open and closed contracts including, among other things, gains and losses related to contracts designed to hedge price movements that occur entirely within a quarter. The tables include amounts for both realized and unrealized gains and losses. The tables are not, therefore, simple representations of unrealized gains and losses recognized in the income statement during any period presented.

NOTE 5: INVESTMENTS

Investments consist of the following:

Equity Investment	% Owned	Successor October 27, 2013	Predecessor April 28, 2013
		(in millions)	
Campofrío Food Group (CFG)	37%	$349.9	$376.2
Mexican joint ventures	50%	122.1	129.6
Other	Various	27.8	26.6
Total investments		$499.8	$532.4

We record our share of earnings and losses from our equity method investments in (income) loss from equity method investments. Some of these results are reported on a one-month lag which, in our opinion, does not materially impact our consolidated condensed financial statements.

As of October 27, 2013, we held 37.8 million shares of CFG common stock. Shares of CFG are publicly traded on the Bolsa de Madrid Exchange (Madrid Exchange). Our investment in CFG contractually entitles us to two seats on CFG's 9-person board of directors, giving us the ability to exert significant influence over the strategic and operational decisions of our investee. The stock is very thinly traded on the Madrid Exchange. CFG is a closely held company, with the three largest shareholders owning approximately 74% of the outstanding shares. We are CFG's largest shareholder, with approximately a 37% interest.

As discussed in Note 2—Merger and Acquisition, we performed a preliminary allocation of the total purchase consideration from the Merger between the assets acquired and liabilities assumed by Shuanghui, including our investments. In assessing the fair value of our investment in CFG, we considered a variety of information, including CFG’s history of positive cash flows, expectations about the future cash flows of CFG, market multiples for comparable businesses, and an influence premium applied to the market price of CFG's shares on the Madrid Exchange to adjust for our contractual right to two board seats and our ability to exert significant influence over the operational and strategic decisions.

In November 2013, Mexican processed meats producer Sigma Alimentos (Sigma) announced its intention to tender for all of CFG’s outstanding shares at a bid price of €6.80 per share (the Bid Price). As part of the announcement, Sigma publicly acknowledged that it has obtained commitments to purchase approximately 44.5% of CFG's outstanding shares at the Bid Price. The Bid Price offered by Sigma was also considered in our fair value assessment discussed above. We, along with Shuanghui, are currently weighing our options and no decision has been made regarding Sigma’s offer.

(Income) loss from equity method investments consists of the following:

Equity Investment	Segment	Successor September 27 - October 27, 2013	Predecessor July 29 - September 26, 2013	Three Months Ended October 28, 2012
		(in millions)		
CFG [1]	International	$(0.1)	$(0.3)	$ (1.3)
Mexican joint ventures	International	(1.4)	(0.9)	(5.9)
All other equity method investments	Various	0.3	—	0.5
Income from equity method investments		$(1.2)	$(1.2)	$ (6.7)

Equity Investment	Segment	Successor September 27 - October 27, 2013	Predecessor April 29 - September 26, 2013	Six Months Ended October 28, 2012
		(in millions)		
CFG [1]	International	$(0.1)	$(0.4)	$ (1.4)
Mexican joint ventures	International	(1.4)	2.1	(5.5)
All other equity method investments	Various	0.3	(1.2)	(0.5)
(Income) loss from equity method investments		$(1.2)	$0.5	$ (7.4)

(1) CFG prepares its financial statements in accordance with International Financial Reporting Standards. Our share of CFG's results reflects U.S. GAAP adjustments and thus, there may be differences between the amounts we report for CFG and the amounts reported by CFG.

NOTE 6: DEBT

Long-term debt consists of the following:

	Successor October 27, 2013	Predecessor April 28, 2013
	(in millions)	
6.625% senior unsecured notes, due August 2022, including unamortized premiums of $22.0 million (Successor) and unamortized discounts of $4.7 million (Predecessor)	$1,021.6	$995.3
7.75% senior unsecured notes, due July 2017, including unamortized premiums of $56.8 million (Successor)	556.8	500.0
5.25% senior unsecured notes, due August 2018	500.0	—
5.875% senior unsecured notes, due August 2021	400.0	—
7.75% senior unsecured notes, due May 2013	—	55.0
4% senior unsecured Convertible Notes, due June 2013, including unamortized discounts of $4.1 million	—	395.9