

SANDERSON FARMS INC  
Form 10-Q  
May 29, 2012  
[Table of Contents](#)

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

**FORM 10-Q**

(MARK ONE)

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

For the quarterly period ended April 30, 2012

OR

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

For the transition period from                      to

Commission file number 1-14977

**Sanderson Farms, Inc.**

(Exact name of registrant as specified in its charter)

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<b>Mississippi</b> (State or other jurisdiction of incorporation or organization)	<b>64-0615843</b> (I.R.S. Employer Identification No.)
<b>127 Flynt Road, Laurel, Mississippi</b> (Address of principal executive offices)	<b>39443</b> (Zip Code)
<b>(601) 649-4030</b> (Registrant's telephone number, including area code)	
(Former name, former address and former fiscal year, if changed since last report.)	

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

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

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

Large accelerated filer <input checked="" type="checkbox"/>	Accelerated filer <input type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS

DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ☐ No ☐

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common Stock, \$1 Par Value Per Share: 22,968,868 shares outstanding as of May 24, 2012.



**Table of Contents**

INDEX

SANDERSON FARMS, INC. AND SUBSIDIARIES

PART I.	<u>FINANCIAL INFORMATION</u>	3
Item 1.	<u>Financial Statements (Unaudited)</u>	3
	<u>Condensed consolidated balance sheets April 30, 2012 and October 31, 2011</u>	3
	<u>Condensed consolidated statements of operations Three and six months ended April 30, 2012 and 2011</u>	4
	<u>Condensed consolidated statements of cash flows Six months ended April 30, 2012 and 2011</u>	5
	<u>Notes to condensed consolidated financial statements April 30, 2012</u>	6
	<u>Report of Independent Registered Public Accounting Firm</u>	10
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	11
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	20
Item 4.	<u>Controls and Procedures</u>	21
PART II	<u>OTHER INFORMATION</u>	22
Item 1.	<u>Legal Proceedings</u>	22
Item 1A.	<u>Risk Factors</u>	23
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	23
Item 6.	<u>Exhibits</u>	24
	<u>SIGNATURES</u>	26
Ex-15		
Ex-31.1		
Ex-31.2		
Ex-32.1		
Ex-32.2		

**Table of Contents**

## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

SANDERSON FARMS, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

	April 30, 2012 (Unaudited)	October 31, 2011 (Note 1)
	(In thousands)	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 7,693	\$ 11,075
Accounts receivable, net	101,852	94,021
Inventories	213,142	211,753
Refundable income taxes	2,387	88,512
Deferred income taxes	3,886	6,357
Prepaid expenses and other current assets	26,819	26,240
<b>Total current assets</b>	<b>355,779</b>	<b>437,958</b>
Property, plant and equipment	965,849	939,535
Less accumulated depreciation	(462,121)	(434,030)
	503,728	505,505
<b>Other assets</b>	<b>4,409</b>	<b>5,058</b>
<b>Total assets</b>	<b>\$ 863,916</b>	<b>\$ 948,521</b>
<b>Liabilities and stockholders' equity</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 98,268	\$ 102,556
Current maturities of long-term debt	11,106	11,106
<b>Total current liabilities</b>	<b>109,374</b>	<b>113,662</b>
Long-term debt, less current maturities	178,116	273,670
Claims payable	4,200	3,300
Deferred income taxes	54,786	50,989
<b>Stockholders' equity:</b>		
Preferred Stock:		
Series A Junior Participating Preferred Stock, \$100 par value: authorized 500,000 shares, none issued		
Par value to be determined by the Board of Directors: authorized 4,500,000 shares; none issued		
Common Stock, \$1 par value: authorized 100,000,000 shares; issued and outstanding shares 22,969,318 and 22,871,588 at April 30, 2012 and October 31, 2011, respectively	22,969	22,872
Paid-in capital	132,903	130,528
Retained earnings	361,568	353,500
<b>Total stockholders' equity</b>	<b>517,440</b>	<b>506,900</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 863,916</b>	<b>\$ 948,521</b>

See notes to condensed consolidated financial statements.



**Table of Contents**

## SANDERSON FARMS, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2012	2011	2012	2011
	(in thousands, except per share amounts)		(in thousands, except per share amounts)	
Net sales	\$ 595,046	\$ 479,342	\$ 1,112,872	\$ 907,074
Cost and expenses:				
Cost of sales	535,901	479,366	1,044,905	938,305
Live inventory adjustment	0	6,000	0	6,000
Selling, general and administrative	18,165	16,813	36,068	37,224
	554,066	502,179	1,080,973	981,529
OPERATING INCOME (LOSS)	40,980	(22,837)	31,899	(74,455)
Other income (expense):				
Interest income	4	9	6	30
Interest expense	(2,426)	(1,491)	(5,388)	(1,947)
Other	(1)	468	(565)	497
	(2,423)	(1,014)	(5,947)	(1,420)
INCOME (LOSS) BEFORE INCOME TAXES	38,557	(23,851)	25,952	(75,875)
Income tax expense (benefit)	14,692	(7,575)	10,076	(26,043)
NET INCOME (LOSS)	\$ 23,865	\$ (16,276)	15,876	\$ (49,832)
Earnings (loss) per share:				
Basic	\$ 1.04	\$ (0.74)	\$ 0.69	\$ (2.25)
Diluted	\$ 1.04	\$ (0.74)	\$ 0.69	\$ (2.25)
Dividends per share	\$ 0.17	\$ 0.17	\$ 0.34	\$ 0.34

See notes to condensed consolidated financial statements.

**Table of Contents**

## SANDERSON FARMS, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	Six Months Ended	
	2012	April 30, 2011
	(In thousands)	
Operating activities		
Net income (loss)	\$ 15,876	\$ (49,832)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	29,761	24,158
Non-cash stock compensation	2,437	2,810
Live inventory adjustment	(9,000)	6,000
Deferred income taxes	6,268	7,307
Change in assets and liabilities:		
Accounts receivable, net	(7,831)	15,090
Refundable income taxes	86,125	(34,591)
Inventories	7,611	(66,555)
Prepaid expenses and other assets	(211)	(2,667)
Accounts payable, accrued expenses and other liabilities	(7,293)	(24,443)
Total adjustments	107,867	(72,891)
Net cash provided by (used in) operating activities	123,743	(122,723)
Investing activities		
Capital expenditures	(27,704)	(37,764)
Net proceeds from sale of property and equipment	0	47
Net cash used in investing activities	(27,704)	(37,717)
Financing activities		
Principal payments on long-term debt	(10,352)	(335)
Borrowings from revolving line of credit	30,000	92,701
Payments on revolving line of credit	(115,201)	0
Proceeds from issuance of restricted stock under stock compensation plans	401	553
Payments from common stock issued under stock compensation plans	(1,071)	(969)
Tax benefit on exercised stock options and vesting of restricted stock grants	705	97
Dividends paid	(3,903)	(3,855)
Net cash provided by (used in) financing activities	(99,421)	88,192
Net change in cash and cash equivalents	(3,382)	(72,248)
Cash and cash equivalents at beginning of period	11,075	73,419
Cash and cash equivalents at end of period	\$ 7,693	\$ 1,171
Supplemental disclosure of non-cash financing activity:		
Dividends payable	\$ (3,905)	\$ (3,874)

See notes to condensed consolidated financial statements.





**Table of Contents**

## SANDERSON FARMS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

April 30, 2012

**NOTE 1 BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments consisting of normal recurring accruals considered necessary for a fair presentation have been included. Operating results for the three and six months ended April 30, 2012 are not necessarily indicative of the results that may be expected for the year ending October 31, 2012.

The condensed consolidated balance sheet at October 31, 2011 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. For further information, reference is made to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the year ended October 31, 2011.

The Company has made reclassifications to prior year financial statements to conform with the presentation for the current year financial statements. The reclassifications are for consistency of presentation and do not affect previously reported net income (loss), stockholder's equity or total assets.

**NOTE 2 INVENTORIES**

Inventories consisted of the following:

	April 30, 2012	October 31, 2011
	(In thousands)	
Live poultry-broilers and breeders	\$ 135,055	\$ 124,260
Feed, eggs and other	34,896	43,628
Processed poultry	29,672	27,892
Prepared chicken	6,613	9,392
Packaging materials	6,906	6,581
	\$ 213,142	\$ 211,753

**NOTE 3 STOCK COMPENSATION PLANS**

Refer to Note 9 of the Company's October 31, 2011 audited financial statements for further information on our employee benefit plans and stock based compensation plans. Total stock based compensation expense during the six months ended April 30, 2012 and April 30, 2011 was \$2,437,000 and \$2,810,000, respectively, and is detailed below.

During the six months ended April 30, 2012, participants in the Company's Management Share Purchase Plan elected to receive a total of 7,690 shares of restricted stock at an average price of \$51.58 per share instead of a specified percentage of their cash compensation and the Company issued 1,881 matching restricted shares. During the six months ended April 30, 2012 and 2011, the Company recorded compensation cost, included in the total stock based compensation expense above, of \$104,000 and \$99,000, respectively, related to the Management Share Purchase Plan.

On November 1, 2011, the Company entered into performance share agreements that grant certain officers and key employees the right to receive a target number of 95,175 shares of the Company's common stock, subject to the Company's achievement of certain performance

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measures. The Company also has performance share agreements in place with certain officers and key employees that were entered into during fiscal 2011. The aggregate target

**Table of Contents**

number of shares specified in performance share agreements outstanding as of April 30, 2012 totaled 175,625. The Company recorded no compensation cost during the first six months of fiscal 2012 related to outstanding performance share agreements granted during fiscal 2012 and fiscal 2011, as achievement of the applicable performance based criteria is not deemed probable. During the first six months of fiscal 2011, the Company did record compensation cost, included in the total stock based compensation expense above, of \$724,000 related to the performance share agreements entered into during fiscal 2009, which vested during the fourth quarter of fiscal 2011.

On November 1, 2011, the Company granted 95,175 shares of restricted stock to certain officers and key management employees. The restricted stock had a grant date fair value of \$48.45 per share and will vest on November 1, 2015. On February 16, 2012, the Company granted 23,000 shares of restricted stock to all of its non-employee directors. The restricted stock had a grant date fair value of \$48.70 per share and vest one, two or three years from the date of grant. The Company has unvested restricted stock grants outstanding that were granted during prior fiscal years to its officers, key employees and outside directors. The aggregate number of shares outstanding at April 30, 2012 related to all unvested restricted stock grants totaled 613,500. During the six months ended April 30, 2012 and 2011 the Company recorded compensation cost, included in the total stock based compensation expense above, of \$2,333,000 and \$1,987,000, respectively, related to restricted stock grants.

**NOTE 4 EARNINGS PER SHARE**

Certain share-based payment awards entitling holders to receive non-forfeitable dividends before vesting are considered participating securities and thus included in the calculation of basic earnings per share, to the extent they are dilutive. All share based awards were anti-dilutive during the three and six months ended April 30, 2011 because the Company incurred a net loss, and the shares were not included in the calculation of loss per common share below. These awards are included in the calculation of basic earnings per share under the two-class method. The two-class method allocates earnings for the period between common shareholders and other security holders. The participating awards receiving dividends are allocated the same amount of income as if they were vested shares.

The following table presents earnings (loss) per share calculated in accordance with requirements of ASC 260.

	<b>For the three months ended</b>	
	<b>April 30, 2012</b>	<b>April 30, 2011</b>
Net Income (loss)	\$ 23,865	\$ (16,276)
Distributed and undistributed (earnings) losses to unvested restricted stock	\$ (713)	\$ 0
Distributed and undistributed (earnings) losses to common shareholders Basic	\$ 23,152	\$ (16,276)
Weighted average shares outstanding Basic	22,277	22,133
Weighted average shares outstanding Diluted	22,280	22,133
Earnings (loss) per common share Basic	\$ 1.04	\$ (0.74)
Earnings (loss) per common share Diluted	\$ 1.04	\$ (0.74)

	<b>For the six months ended</b>	
	<b>April 30, 2012</b>	<b>April 30, 2011</b>
Net Income (loss)	\$ 15,876	\$ (49,832)
Distributed and undistributed (earnings) losses to unvested restricted stock	\$ (481)	\$ 0
Distributed and undistributed (earnings) losses to common shareholders Basic	\$ 15,395	\$ (49,832)
Weighted average shares outstanding Basic	22,264	22,115
Weighted average shares outstanding Diluted	22,267	22,115
Income (loss) per common share Basic	\$ 0.69	\$ (2.25)
Income (loss) per common share Diluted	\$ 0.69	\$ (2.25)

**Table of Contents****NOTE 5 NEW ACCOUNTING PRONOUNCEMENTS**

In May 2011, FASB issued ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS. The amendments in this update generally represent clarifications of Topic 820, but also include some instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed. This update results in common principles and requirements for measuring fair value and for disclosing information about fair value measurements in accordance with U.S. GAAP and IFRS. This update is effective for annual and interim periods beginning after December 15, 2011. This update did not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

**NOTE 6 FAIR VALUE OF FINANCIAL INSTRUMENTS**

The carrying amounts for cash and temporary cash investments approximate their fair values. Fair values for debt are based on quoted market prices or published forward interest rate curves. The fair value and carrying value of the Company's borrowings under its credit facilities, long-term debt and capital lease obligations were as follows (in millions):

	April 30, 2012		October 31, 2011	
	Fair Value	Carrying Value	Fair Value	Carrying Value
Total Debt (in millions)	\$ 191	\$ 189	\$ 285	\$ 285

**NOTE 7 OTHER MATTERS**

On February 16, 2012, two of our former employees sued us and seven of our current and former employees in the United States District Court for the Middle District of Georgia for damages allegedly caused to them by the defendants' alleged violations of the federal and State of Georgia's Racketeer Influenced and Corrupt Organizations (RICO) Acts. The plaintiffs filed the lawsuit on behalf of all hourly-paid workers legally authorized to be employed in the United States who have been employed at our processing plant located in Moultrie, Georgia since 2008.

The plaintiffs allege in their complaint that the defendants conspired to knowingly hire undocumented immigrants at the Moultrie plant to save Sanderson millions of dollars in labor costs because illegal aliens will work for extremely low wages, will typically not complain about workplace conditions and injuries, and because of their vulnerable situation, will accede to managers' demands to work harder than American citizens and legal aliens. The action is brought as a class action lawsuit on behalf of all persons legally authorized to be employed in the United States who have been employed at the Moultrie plant as hourly wage earners in the four years before the filing of the case, and the plaintiffs seek certification of that class. The plaintiffs are suing for money damages, injunctive relief and revocation of our license to conduct business in the State of Georgia.

Based on our present knowledge, we consider the claims made in this lawsuit to be baseless.

The Company is involved in other various claims and litigation incidental to its business. Although the outcome of these matters cannot be determined with certainty, management, upon the advice of counsel, is of the opinion the final outcome should not have a material effect on the Company's consolidated results of operations or financial position.

The Company recognizes the costs of legal defense for the legal proceedings to which it is a party in the periods incurred. After a considerable analysis of each case, the Company determines the amount of reserves required, if any. At this time, the Company has not accrued any reserve for any of these matters. Future reserves may be

**Table of Contents**

required if losses are deemed reasonably estimable and probable due to changes in the Company's assumptions, the effectiveness of legal strategies, or other factors beyond the Company's control. Future results of operations may be materially affected by the recording of reserves or by accruals of losses to reflect any adverse determinations in these legal proceedings.

**NOTE 8 CREDIT AGREEMENT**

The Company has a \$500 million revolving credit facility. The facility limits capital expenditures to \$60.0 million during fiscal year 2011 and \$55.0 million for fiscal years 2012, 2013, 2014 and 2015, plus, for each year, up to \$10.0 million permitted to be spent in the preceding year but not actually spent therein. The capital expenditure limitation for fiscal 2012, with the permitted carry over, is \$62.0 million. The credit facility also permits the Company to spend up to \$115.0 million in capital expenditures on the construction of a second poultry complex in North Carolina, which expenditures are in addition to the annual limits. Under the revolving credit facility the Company may not exceed a maximum debt to total capitalization ratio of 55% from the date of the agreement through October 30, 2014, and 50% thereafter. The Company has a one-time right, at any time during the Company's fiscal years ending October 31, 2011 or October 31, 2012, to increase the maximum debt to total capitalization ratio then in effect by 5% in connection with the construction of a second potential North Carolina complex for the four fiscal quarters beginning on the first day of the fiscal quarter during which the Company gives written notice of its intent to exercise this right. The Company has not exercised this right. The facility also sets a minimum net worth requirement that at April 30, 2012 was approximately \$463.0 million. The credit is unsecured and, unless extended, will expire on February 23, 2016. As of April 30, 2012, the Company had borrowed \$137.5 million under the revolving credit facility, and had \$9.6 million outstanding letters of credit under the facility. As of May 25, 2012, the Company had borrowed \$132.5 million under the facility.

**Table of Contents**

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

Sanderson Farms, Inc.

We have reviewed the condensed consolidated balance sheet of Sanderson Farms, Inc. and subsidiaries as of April 30, 2012, and the related condensed consolidated statements of operations for the three-month and six-month periods ended April 30, 2012 and 2011 and the condensed consolidated statements of cash flows for the six-month periods ended April 30, 2012 and 2011. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Sanderson Farms, Inc. and subsidiaries as of October 31, 2011, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended not presented herein, and in our report dated December 20, 2011, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of October 31, 2011, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Ernst & Young LLP

New Orleans, Louisiana

May 29, 2012

## **Table of Contents**

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

#### General

The following Discussion and Analysis should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included in Item 7 of the Company's Annual Report on Form 10-K for its fiscal year ended October 31, 2011.

This Quarterly Report, and other periodic reports filed by the Company under the Securities Exchange Act of 1934, and other written or oral statements made by it or on its behalf, may include forward-looking statements, which are based on a number of assumptions about future events and are subject to various risks, uncertainties and other factors that may cause actual results to differ materially from the views, beliefs and estimates expressed in such statements. These risks, uncertainties and other factors include, but are not limited to the following:

- (1) Changes in the market price for the Company's finished products and feed grains, both of which may fluctuate substantially and exhibit cyclical characteristics typically associated with commodity markets.
- (2) Changes in economic and business conditions, monetary and fiscal policies or the amount of growth, stagnation or recession in the global or U.S. economies, either of which may affect the value of inventories, the collectability of accounts receivable or the financial integrity of customers, and the ability of the end user or consumer to afford protein.
- (3) Changes in the political or economic climate, trade policies, laws and regulations or the domestic poultry industry of countries to which the Company or other companies in the poultry industry ship product, and other changes that might limit the Company's or the industry's access to foreign markets.
- (4) Changes in laws, regulations, and other activities in government agencies and similar organizations applicable to the Company and the poultry industry and changes in laws, regulations and other activities in government agencies and similar organizations related to food safety.
- (5) Various inventory risks due to changes in market conditions, including, but not limited to, the risk that market values of live and processed poultry inventories might be lower than the cost of such inventories, requiring a downward adjustment to record the value of such inventories at the lower of cost or market as required by generally accepted accounting principles.
- (6) Changes in and effects of competition, which is significant in all markets in which the Company competes, and the effectiveness of marketing and advertising programs. The Company competes with regional and national firms, some of which have greater financial and marketing resources than the Company.
- (7) Changes in accounting policies and practices adopted voluntarily by the Company or required to be adopted by accounting principles generally accepted in the United States.
- (8) Disease outbreaks affecting the production performance and/or marketability of the Company's poultry products, or the contamination of its products.
- (9) Changes in the availability and cost of labor and growers.
- (10) The loss of any of the Company's major customers.
- (11) Inclement weather that could hurt Company flocks or otherwise adversely affect its operations, or changes in global weather patterns that could impact the supply of feed grains.
- (12) Failure to respond to changing consumer preferences.



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(13) Failure to successfully and efficiently start up and run a new plant or integrate any business the Company might acquire.

## **Table of Contents**

Readers are cautioned not to place undue reliance on forward-looking statements made by or on behalf of Sanderson Farms. Each such statement speaks only as of the day it was made. The Company undertakes no obligation to update or to revise any forward-looking statements. The factors described above cannot be controlled by the Company. When used in this report, the words *believes*, *estimates*, *plans*, *expects*, *should*, *outline*, *anticipates* and similar expressions as they relate to the Company or its management are intended to identify forward-looking statements. Examples of forward-looking statements include statements about management's beliefs about future demand for fresh chicken and future chicken market prices.

The Company's poultry operations are integrated through its control of all functions relative to the production of its chicken products, including hatching egg production, hatching, feed manufacturing, raising chickens to marketable age (grow out), processing, and marketing. Consistent with the poultry industry, the Company's profitability is substantially impacted by the market prices for its finished products and feed grains, both of which may fluctuate substantially and exhibit cyclical characteristics typically associated with commodity markets. Other costs, excluding feed grains, related to the profitability of the Company's poultry operations, including hatching egg production, hatching, growing, and processing cost, are responsive to efficient cost containment programs and management practices.

The Company's prepared chicken product line includes approximately 60 institutional and consumer packaged chicken items that it sells nationally, primarily to distributors and food service establishments. A majority of the prepared chicken items are made to the specifications of food service users.

Sanderson Farms began operations at its new feed mill, poultry processing plant and hatchery on separate sites in Kinston and Lenoir County, North Carolina during the first fiscal quarter of 2011. The Kinston facilities comprise a state-of-the-art poultry complex with the capacity, at full production, to process 1,250,000 birds per week for the retail chill pack market. At full capacity the complex will employ approximately 1,500 people, will require 130 contract growers, and will be equipped to process and sell 6.7 million pounds per week of dressed poultry meat. During the second quarter of fiscal 2012 the new Kinston processing plant sold 78.2 million pounds of dressed poultry meat.

On March 29, 2010, the Company announced intentions to construct a potential second new poultry complex in North Carolina, subject to various contingencies including, among others, obtaining an acceptable economic incentive package from the state and local governments. The Company announced on February 24, 2011 that this new complex would be placed on hold pending improvement in market fundamentals, including assurance that the supply of corn and other feed grains in the United States and the world will be adequate to meet the demands of end users of such grains at reasonable prices. The project, if completed, will consist of an expansion of the feed mill for the Kinston, North Carolina plant, a hatchery, a processing plant with capacity to process 1.25 million chickens per week and a waste water treatment facility. At full capacity, the plant is expected to employ approximately 1,100 people, will require approximately 150 contract growers and will be equipped to process and sell 8.9 million pounds of dressed poultry per week. We will need to identify a site, obtain permits, enter into construction contracts and complete construction before the complex can open. See *The construction and potential benefits of our new North Carolina facilities are subject to risks and uncertainties* in the Risk Factors Section of our Annual Report on Form 10-K for the year ended October 31, 2011.

On February 23, 2011, the Company entered into a new revolving credit facility to, among other things, increase the available credit to \$500.0 million from \$300.0 million, and to increase the annual capital expenditure limitation to \$60.0 million during fiscal year 2011 and \$55.0 million for fiscal years, 2012, 2013, 2014 and 2015, plus, for each year, up to \$10.0 million permitted to be spent in the preceding fiscal year but not actually spent therein. The capital expenditure limitation for fiscal 2012, with the permitted carry over, is \$62.0 million. The new credit facility also permits the Company to spend up to \$115.0 million in capital expenditures on the construction of a second poultry complex in North Carolina, which expenditures are in addition to the annual limits. Under the facility, the Company may not exceed a maximum debt to total capitalization ratio of 55% from the date of the agreement through October 31, 2014, and 50% thereafter. The Company has a one-time right, at any time during the Company's fiscal year ending October 31, 2011 or October 31, 2012, to increase the maximum debt to capitalization ratio then in effect by 5% in connection with the construction of a second potential North Carolina complex for the four fiscal quarters beginning on the first day of the fiscal quarter during which the Company gives written notice of its intent to exercise this right. The Company has not exercised this right. The facility also sets a minimum net worth

## **Table of Contents**

requirement that at April 30, 2012 was approximately \$463.0 million. The credit remains unsecured and, unless extended, will expire on February 23, 2016. As of April 30, 2012, the Company had \$137.5 million outstanding under the revolving credit facility, and had \$9.6 million outstanding letters of credit under the facility. As of May 25, 2012, the Company had borrowed \$132.5 million under the facility.

### **EXECUTIVE OVERVIEW OF RESULTS**

The Company's margins improved during the second quarter of fiscal 2012 when compared to the second quarter of fiscal 2011 reflecting improved market prices for poultry products and lower grain costs. Industry poultry production was lower during the second quarter of fiscal 2012 as compared to the second quarter of fiscal 2011 and resulted in improved market prices for poultry products. While demand for fresh chicken in the retail grocery store and export markets has been stable, market prices for boneless breast meat remained under pressure, even in the face of lower production numbers, reflecting continued weak demand from casual dining customers. The Company expects demand from casual dining customers to remain under pressure until employment numbers and consumer confidence improve. Market prices for boneless breast meat improved seasonally during the first two weeks of May, but the Company believes such improvement was fueled by lower supplies rather than increased demand.

Both corn and soybean meal market prices have stabilized below the highs they set last Fall, and were lower during the second quarter of fiscal 2012 compared to the same quarter of fiscal 2011, but remain high relative to historical averages. During the second quarter of fiscal 2012 as compared to the second quarter of fiscal 2011, the average feed cost per pound of poultry products sold was 9.8% lower. The Company believes uncertainty about the supply of grain will likely support relatively high grain prices at least until the market gets some visibility on the quantity and quality of the 2012 crops. The Company has priced most all of its needs for corn through July, half of its soybean meal needs through June, but has priced none of its needs past July. Had the Company priced its remaining needs at May 24, 2012 market prices, including the additional volume needed during fiscal 2012, cash feed grain costs would be approximately \$23.1 million lower during fiscal 2012 as compared to fiscal 2011.

### **RESULTS OF OPERATIONS**

Net sales for the second quarter ended April 30, 2012 were \$595.0 million as compared to \$479.3 million for the second quarter ended April 30, 2011, an increase of \$115.7 million or 24.1%. Net sales of poultry products for the second quarter ended April 30, 2012 and April 30, 2011 were \$572.9 million and \$451.3 million, respectively, an increase of \$121.6 million or 26.9%. The increase in net sales of poultry products resulted from a 14.5% increase in the average sales price of poultry products sold and a 10.8% increase in the pounds of poultry products sold. During the second quarter of fiscal 2012 the Company sold 743.3 million pounds of poultry products, up from 670.7 million pounds during the second quarter of fiscal 2011. The additional pounds of poultry products sold resulted from a 5.2% increase in the number of chickens sold, primarily attributable to the new Kinston complex, which began initial operation during the first quarter of fiscal 2011 and was closer to full capacity during the second quarter of fiscal 2012. The complex sold 78.2 million pounds, or 10.5% of the total poultry pounds sold by the Company in the second quarter of fiscal 2012, up from 25.2 million pounds of poultry, or 3.8% of the total poultry pounds sold during the second quarter of fiscal 2011. Overall market prices for poultry products increased during the second quarter of fiscal 2012 as compared to the same quarter of fiscal 2011 primarily as a result of a decrease in the supply of poultry products. Urner Barry market prices increased for boneless breast meat, bulk leg quarters, tenders and jumbo wings during the second quarter of fiscal 2012 as compared to the second quarter of fiscal 2011 by 2.3%, 22.4%, 15.4% and 121.5%, respectively. The average market price for Georgia Dock whole birds also showed improvement and increased by approximately 7.5%. Net sales of prepared chicken products for the three months ended April 30, 2012 and 2011 were \$22.1 million and \$28.0 million, respectively, or a decrease of 21.0%, resulting from a 4.3% decrease in the average sales price of prepared chicken products sold and a 17.5% decrease in the pounds of prepared chicken products sold from 14.1 million pounds sold during the second quarter of fiscal 2011 to 11.6 million pounds sold during the second quarter of fiscal 2012.

Net sales for the first six months of fiscal 2012 were \$1,112.9 million as compared to \$907.1 million for the first six months of fiscal 2011, an increase of \$205.8 million or 22.7%. Net sales of poultry products for the first six months of fiscal 2012 and fiscal 2011 were \$1,068.9 million and \$853.8 million, respectively, an increase of \$215.1 million or 25.2%. The increase in net sales of poultry products resulted from a 15.3% increase in the average sales price of poultry products sold and a 8.5% increase in the pounds of poultry products sold. During the first six months of

**Table of Contents**

fiscal 2012 the Company sold 1,412.5 million pounds of poultry products, up from 1,301.4 million pounds during the first six months of fiscal 2011. The additional pounds of poultry products sold resulted from a 6.2% increase in the number of chickens sold, primarily attributable to the new Kinston complex, which began initial operation during the first quarter of fiscal 2011 and was closer to full capacity during the first six months of fiscal 2012. The complex sold 144.6 million pounds, or 10.2% of the total poultry pounds sold by the Company in the first six months of fiscal 2012, up from 33.6 million pounds of poultry, or 2.6 % of the total poultry pounds sold during the first six months of fiscal 2011. Overall market prices for poultry products increased during the first six months of fiscal 2012 as compared to the same period during fiscal 2011, primarily as a result of a decrease in the supply of poultry products. Urner Barry market prices increased for boneless breast meat, bulk leg quarters, tenders and jumbo wings during the first six months of fiscal 2012 compared to fiscal 2011 by 4.9%, 31.1%, 19.1% and 76.6%, respectively. The average market price for Georgia Dock whole birds also showed improvement and increased by approximately 6.4%. Net sales of prepared chicken products for the first six months of fiscal 2012 and 2011 were \$44.0 million and \$53.3 million, respectively, or a decrease of 17.5%, resulting from a 4.7% decrease in the average sales price of prepared chicken products sold and a 13.4% decrease in the pounds of prepared chicken products sold from 27.1 million pounds sold during the first six months of fiscal 2011 to 23.4 million pounds sold during the first six months of fiscal 2012.

Cost of sales for the second quarter of fiscal 2012 was \$535.9 million as compared to \$479.4 million during the second quarter of fiscal 2011, an increase of \$56.5 million or 11.8%. Cost of sales of poultry products sold during the second quarter of fiscal 2012 as compared to the second quarter of fiscal 2011 were \$514.4 million and \$454.0 million, respectively, an increase of \$60.4 million or approximately 13.3%. As illustrated in the table below, which excludes the impact of the \$22.3 million live inventory adjustment at January 31, 2011 for comparative purposes, the increase in the cost of sales of poultry products sold resulted from a 10.8% increase in the pounds of poultry products sold and an increase in all other cost of sales of poultry products of \$.0198 per pound, offset by a decrease in the cost of feed in broiler flocks sold of \$0.0378 per pound.

**Poultry Cost of Sales**

(In thousands, except percentages and per pound data)

Description	Second Quarter 2012		Second Quarter 2011		Incr/(Decr)	
	Dollars	Per Pnd	Dollars	Per Pnd	Dollars	Per Pnd
Feed in broiler flocks sold	\$ 259,542	\$ 0.3492	\$ 259,589	\$ 0.3870	\$ (47)	\$ (0.0378)
All other cost of sales	\$ 254,829	\$ 0.3429	\$ 216,700	\$ 0.3231	\$ 38,129	\$ 0.0198
Total poultry cost of sales	\$ 514,371	\$ 0.6920	\$ 476,289 <sup>(1)</sup>	\$ 0.7101	\$ 38,082	\$ (0.0181)

Poultry Pounds Sold 743,266 670,712

Note (1) Excluding the \$22.3 million live inventory adjustment at January 31, 2011.

Other costs of sales of poultry products include labor, contract grower pay, packaging, freight and certain fixed costs, among other costs. These non-feed related costs of poultry products sold increased \$.0198 per pound, or 6.1%, during this year's second fiscal quarter compared to the same quarter a year ago primarily resulting from changes in the quantity and mix of inventory on hand at the end of each period. Excluding the changes in inventory, these non-feed related costs decreased \$0.0053 per pound. Costs of sales of the Company's prepared chicken products were \$21.5 million as compared to \$25.4 million during fiscal 2011, a decrease of \$3.9 million or 15.4%.

Cost of sales for the six months ended April 30, 2012 was \$1,044.9 million as compared to \$938.3 million during the same period during fiscal 2011, an increase of \$106.6 million or 11.4%. Cost of sales of poultry products sold for the six months ended April 30, 2012 and April 30, 2011 were \$1,002.9 million and \$890.5 million, respectively, an increase of \$112.4 million or approximately 12.6%. As illustrated in the table below, the increase in the cost of sales of poultry products sold resulted from an increase of 8.5% in the pounds of poultry products sold and increases in feed costs and all other cost of sales per pound of \$0.0078 and \$0.0180, respectively.

## Table of Contents

### Poultry Cost of Sales

(In thousands, except percentages and per pound data)

Description	Six Months Ended		Six Months Ended		Incr/(Decr)	
	April 30, 2012		April 30, 2011			
	Dollars	Per Pnd	Dollars	Per Pnd	Dollars	Per Pnd
Feed in broiler flocks sold	\$ 527,180	\$ 0.3732	\$ 475,544	\$ 0.3654	\$ 51,636	\$ 0.0078
All other cost of sales	\$ 475,734	\$ 0.3368	\$ 414,951	\$ 0.3189	\$ 60,783	\$ 0.0180
<b>Total poultry cost of sales</b>	<b>\$ 1,002,914</b>	<b>\$ 0.7100</b>	<b>\$ 890,495</b>	<b>\$ 0.6843</b>	<b>\$ 112,418</b>	<b>\$ 0.0258</b>

Poultry Pounds Sold 1,412,417 1,301,382

Other costs of sales of poultry products include labor, contract grower pay, packaging, freight and certain fixed costs, among other costs. These non-feed related costs of poultry products sold increased \$0.0180 per pound or 5.6% during the first half of fiscal 2012 compared to the first half of fiscal 2011 primarily resulting from changes in inventory. Excluding the changes in inventory, these non-feed related costs increased \$0.0045 per pound. For the first six months of fiscal 2012 costs of sales of the Company's prepared chicken products were \$42.0 million as compared to \$47.8 million during fiscal 2011, a decrease of \$5.8 million or 12.2%, resulting primarily from the decrease in pounds sold of prepared chicken products of 13.4%.

The Company recorded the value of live broiler inventories on hand at April 30, 2012 at cost. When market conditions are favorable, the Company values the broiler inventories on hand at cost, and accumulates costs as the birds are grown to a marketable age subsequent to the balance sheet date. In periods where the Company estimates that the cost to grow live birds in inventory to a marketable age and then process and distribute those birds will be higher than the anticipated sales price, the Company will make an adjustment to lower the value of live birds to the market value. During the second quarter of fiscal 2011, the Company recorded a charge of \$6.0 million to lower the value of live broiler inventories on hand at April 30, 2011 from cost to market value, which resulted primarily from the significant increase in costs for corn and soybean meal and relatively low market prices for poultry products. No charge was required in the second fiscal quarter of 2012.

Selling, general and administrative costs during the three and six months ended April 30, 2012 were \$18.2 million and \$36.1 million, respectively. The following table includes the components of selling, general and administrative costs for the three months and six months ended April 30, 2012 and 2011.

### Selling, General and Administrative Costs

(in thousands)

	Three Months Ended April 30		Six Months Ended April 30	
	2012	2011	2012	2011
Start up expense-Kinston N.C.	\$ 0	\$ 0	\$ 0	\$ 4,502
Trainee expense	910	1,148	1,997	2,375
Stock compensation expense	1,163	1,353	2,286	2,630
ESOP expense	0	0	0	0
All other S,G & A	16,092	14,312	31,785	27,717
<b>Total S,G &amp; A</b>	<b>\$ 18,165</b>	<b>\$ 16,813</b>	<b>\$ 36,068</b>	<b>\$ 37,224</b>

As illustrated in the table above, the increase in selling, general and administrative costs during the second quarter of fiscal 2012 as compared to the second quarter of fiscal 2011 resulted from higher wages and various other administrative costs. During the first half of fiscal 2012 as compared to the first half of fiscal 2011, selling, general and administrative costs decreased \$1.2 million reflecting a decrease of \$4.5 million in

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start up costs at Kinston, offset by higher wages and various other administrative costs. The Company began operations at the new Kinston complex during January 2011, at which time all Kinston costs, excluding customer service department costs, were included in cost of sales.

## **Table of Contents**

The Company's operating income for the three and six months ended April 30, 2012 was \$41.0 million and \$31.9 million, respectively as compared to an operating loss for the three and six months ended April 30, 2011 of \$22.8 million and \$74.5 million. The improvement in the Company's operating margin resulted primarily from improved market prices of poultry products during fiscal 2012 as compared to fiscal 2011, as described above. In addition, the Company recorded a charge of \$6.0 million during the second quarter of fiscal 2011 to lower the value of the Company's inventory of live broilers at April 30, 2011 from cost to market value. At April 30, 2012, market conditions did not warrant such an adjustment and the Company's inventory of live broilers was recorded at cost.

Interest expense during the second quarter and first half of fiscal 2012 was \$2.4 million and \$5.4 million, respectively. During fiscal 2011 interest expense during the same periods was \$1.5 million and \$1.9 million, respectively. The increase in interest expense during fiscal 2012 as compared to 2011 resulted primarily from higher outstanding debt during fiscal 2012 as compared to fiscal 2011. During the first quarter of fiscal 2011, the Company capitalized interest of \$630,000 related to the construction of the new complex in Kinston and Lenoir County, North Carolina. The Company has not capitalized any interest since the first quarter of fiscal 2011.

The Company's effective tax rates for the three and six months ended April 30, 2012 were 38.1% and 38.8%, respectively as compared to 31.8% and 34.3% respectively for the same periods during fiscal 2011. The Company's effective tax rate differs from the statutory federal rate due to state income taxes, certain nondeductible expenses for federal income tax purposes and certain state and federal tax credits.

During the three and six months ended April 30, 2012 the Company's net income was \$23.9 million or \$1.04 per share and \$15.9 million or \$0.69 per share, respectively. For the three and six months ended April 30, 2011 the Company's net loss was \$16.3 million or \$0.74 per share and \$49.8 million or \$2.25 per share, respectively.

### **Liquidity and Capital Resources**

The Company's working capital, calculated by subtracting current liabilities from current assets, at April 30, 2012 was \$246.4 million and its current ratio, calculated by dividing current assets by current liabilities, was 3.3 to 1. The Company's working capital and current ratio at October 31, 2011 were \$324.3 million and 3.9 to 1. These measures reflect the Company's ability to meet its short term obligations and are included here as a measure of the Company's short term market liquidity. The Company's principal sources of liquidity during fiscal 2012 include cash on hand at October 31, 2011, and borrowings under the Company's revolving credit facility with nineteen banks. As described below, on February 23, 2011 the Company entered into a new revolving credit facility to, among other things, increase the line of credit to \$500.0 million from \$300.0 million and to extend the terms until 2016 from 2013. As of April 30, 2012, the Company had borrowed \$137.5 million and had \$9.6 million outstanding letters of credit under the credit facility.

The Company's cash position at April 30, 2012 and October 31, 2011 consisted of \$7.7 million and \$11.1 million, respectively, in cash and cash equivalents. The Company's ability to invest cash is limited by covenants in its revolving credit agreement to short term, conservative investments. All of the Company's cash at April 30, 2012 and October 31, 2011 was held in checking accounts and highly liquid, overnight investment accounts maintained at two banks. There were no restrictions on the Company's access to its cash and cash investments, and such cash and cash investments were available to the Company on demand to fund its operations.

Cash flows provided by (used in) operating activities during the six months ended April 30, 2012 and 2011 were \$123.7 million and (\$122.7) million, respectively. The increase in cash flows from operating activities of \$246.4 million resulted primarily from improved market prices for poultry products during the first half of fiscal 2012 as compared to the first half of fiscal 2011, the receipt of \$82.7 million federal income tax refund on February 27, 2012 and the increase in inventory of live and processed chicken at the new Kinston, North Carolina complex during fiscal 2011.

Cash flows used in investing activities during the first quarter of fiscal 2012 and 2011 were \$27.7 million and \$37.7 million, respectively. The Company's capital expenditures during the first half of fiscal 2012 were \$27.7 million, including \$4.1 million for a new Company aircraft. The Company's capital expenditures during the first half of fiscal 2011 were \$37.8 million and included \$14.3 million for construction of the Company's new Kinston, North Carolina complex.

## **Table of Contents**

Cash flows provided by and (used in) financing activities during the six months ended April 30, 2012 and 2011 were (\$99.4) million and \$88.2 million, respectively. During the first six months of fiscal 2012 the Company reduced net outstanding borrowings under its revolving credit facility by \$85.2 million and made the first of five \$10.0 million annual installments on the Farm Credit services term loan. During the six months ended April 30, 2011, the Company's unfavorable profit margin required it to use cash on hand at the beginning of fiscal 2011, as well as borrowings under the revolving credit facility to fund operations and to invest in fixed assets and inventories at the Company's new complex in Kinston and Lenoir County, North Carolina.

The Company's capital budget for fiscal 2012 is approximately \$43.9 million, excluding leases. The 2012 capital budget will be funded by internally generated working capital, cash flows from operations and, as needed, draws under the Company's revolving credit facility. The Company had \$352.9 million available under the revolving line of credit at April 30, 2012.

The Company has a Form S-3 shelf registration statement on file with the Securities and Exchange Commission to register, for possible future sale, shares of the Company's common and/or preferred stock at an aggregate offering price not to exceed \$1.0 billion. The stock may be offered by the Company in amounts, at prices and on terms to be determined by the board of directors if and when shares are issued.

The Company has a \$500 million revolving credit facility. The facility limits capital expenditures to \$60.0 million during fiscal year 2011 and \$55 million for fiscal years 2012, 2013, 2014 and 2015, plus, for each year, up to \$10.0 million permitted to be spent in the preceding fiscal year but not actually spent therein. The capital expenditure limitation for fiscal 2012, with the permitted carry over, is \$62.0 million. The credit facility also permits the Company to spend up to \$115.0 million in capital expenditures on the construction of a second poultry complex in North Carolina, which expenditures are in addition to the annual limits. Under the facility the Company may not exceed a maximum debt to total capitalization ratio of 55% from the date of the agreement through October 31, 2014, and 50% thereafter. The Company has a one-time right, at any time during the Company's fiscal year ending October 31, 2011 or October 31, 2012, to increase the maximum debt to capitalization ratio then in effect by 5% in connection with the construction of a second potential North Carolina complex for the four fiscal quarters beginning on the first day of the fiscal quarter during which the Company gives written notice of its intent to exercise this right. The Company has not exercised this right. The facility also sets a minimum net worth requirement which, at January 31, 2012, was approximately \$463.0 million. The credit is unsecured and, unless extended, will expire on February 23, 2016. As of April 30, 2012, the Company had borrowed \$137.5 million under the revolving credit facility and had \$9.6 million in outstanding letters of credit. As of May 25, 2012, the Company had \$132.5 million outstanding under the revolving credit facility, leaving \$357.9 million available under the revolving credit facility.

The Company regularly evaluates both internal and external growth opportunities, including acquisition opportunities and the possible construction of new production assets, and conducts due diligence activities in connection with such opportunities. The cost and terms of any financing to be raised in conjunction with any growth opportunity, including the Company's ability to raise debt or equity capital on terms and at costs satisfactory to the Company, and the effect of such opportunities on the Company's balance sheet, are critical considerations in any such evaluation.

### **Critical Accounting Policies and Estimates**

The preparation of financial statements in accordance with accounting standards generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates and assumptions, and the differences could be material.



## **Table of Contents**

The Company's Summary of Significant Accounting Policies, as described in Note 1 of the Notes to the Consolidated Financial Statements that are filed with the Company's latest report on Form 10-K, should be read in conjunction with this Management's Discussion and Analysis of Financial Condition and Results of Operations. Management believes that the critical accounting policies and estimates that are material to the Company's Consolidated Financial Statements are those described below.

### **Allowance for Doubtful Accounts**

In the normal course of business, the Company extends credit to its customers on a short-term basis. Although credit risks associated with our customers are considered minimal, the Company routinely reviews its accounts receivable balances and makes provisions for probable doubtful accounts. In circumstances where management is aware of a specific customer's inability to meet its financial obligations to the Company, a specific reserve is recorded to reduce the receivable to the amount expected to be collected. If circumstances change (i.e., higher than expected defaults or an unexpected material adverse change in a major customer's ability to meet its financial obligations to us), our estimates of the recoverability of amounts due us could be reduced by a material amount, and the allowance for doubtful accounts and related bad debt expense would increase by the same amount.

### **Inventories**

Processed food and poultry inventories and inventories of feed, eggs, medication and packaging supplies are stated at the lower of cost (first-in, first-out method) or market. If market prices for poultry or feed grains move substantially lower, the Company would record adjustments to write down the carrying values of processed poultry and feed inventories to fair market value, which would increase the Company's costs of sales.

Live poultry inventories of broilers are stated at the lower of cost or market and breeders at cost less accumulated amortization. The cost associated with broiler inventories, consisting principally of chicks, feed, medicine and payments to the growers who raise the chicks for us, are accumulated during the growing period. The cost associated with breeder inventories, consisting principally of breeder chicks, feed, medicine and grower payments are accumulated during the growing period. Capitalized breeder costs are then amortized over nine months using the straight-line method. Mortality of broilers and breeders is charged to cost of sales as incurred. If market prices for chicken, feed or medicine or if grower payments increase (or decrease) during the period, the Company could have an increase (or decrease) in the market value of its inventory as well as an increase (or decrease) in costs of sales. Should the Company decide that the nine month amortization period used to amortize the breeder costs is no longer appropriate as a result of operational changes, a shorter (or longer) amortization period could increase (or decrease) the costs of sales recorded in future periods. High mortality from disease or extreme temperatures would result in abnormal charges to cost of sales to write-down live poultry inventories.

As of April 30, 2012, the Company's inventory of live broilers was recorded at cost. Any required reserve would be determined by comparing the accumulated cost of live poultry inventories of broilers at April 30, 2012, plus the estimated remaining costs of their grow-out, processing, marketing and sale, to the ultimate expected sales prices of finished products resulting from the processing of such broiler inventories. Had such estimated cost exceeded the estimated sales price, an adjustment to record inventory at market value would have been necessary. If an adjustment were determined to be appropriate, the value of no individual live broiler flock would be reduced by an amount greater than its accumulated cost as of April 30, 2012. The Company used the latest available information in making these estimates, including the expected cost of grain needed to complete the grow-out of live inventories and the expected market prices for the finished products. However, as with any sensitive estimate, there are uncertainties inherent in making forward-looking projections and the Company's actual results could vary from those estimated.

### **Long-Lived Assets**

Depreciable long-lived assets are primarily comprised of buildings and machinery and equipment. Depreciation is provided by the units of production or straight-line method over the estimated useful lives, which are 15 to 39 years for buildings and 3 to 12 years for machinery and equipment. An increase or decrease in the estimated useful lives would result in changes to depreciation expense.

## **Table of Contents**

The Company continually evaluates the carrying value of its long-lived assets for events or changes in circumstances that indicate that the carrying value may not be recoverable. As part of this evaluation, the Company estimates the future cash flows expected to result from the use of the asset and its eventual disposal. If the sum of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the asset, an impairment loss is recognized to reduce the carrying value of the long-lived asset to the estimated fair value of the asset. If the Company's assumptions with respect to the future expected cash flows associated with the use of long-lived assets currently recorded change, then the Company's determination that no impairment charges are necessary may change and result in the Company recording an impairment charge in a future period. The Company did not identify any indicators of impairment during the current fiscal period.

### **Accrued Self Insurance**

Insurance expense for workers' compensation benefits and employee-related health care benefits are estimated using historical experience and actuarial estimates. The Company accrues expenses in its workers' compensation and employee benefit plans for both known claims as well as claims incurred but not reported. Stop-loss coverage is maintained with third party insurers to limit the Company's total exposure. Management regularly reviews the assumptions used to recognize periodic expenses. Any resulting adjustments to accrued claims are reflected in current operating results. There are no material adjustments to expenses accrued in prior periods in current expenses. If historical experience proves not to be a good indicator of future expenses, if management were to use different actuarial assumptions, or if there is a negative trend in the Company's claims history, there could be a significant increase or decrease in cost of sales depending on whether these expenses increased or decreased, respectively.

### **Income Taxes**

The Company determines its effective tax rate by estimating its permanent differences resulting from differing treatment of items for financial and income tax purposes. The Company is periodically audited by taxing authorities and considers any adjustments made as a result of the audits in considering the tax expense. Any audit adjustments affecting permanent differences could have an impact on the Company's effective tax rate.

### **Contingencies**

See Item 1. Legal Proceedings in Part II. Other Information, below for a description of certain legal matters.

The Company is involved in various claims and litigation incidental to its business. Although the outcome of these matters cannot be determined with certainty, management, upon the advice of counsel, is of the opinion that the final outcome should not have a material effect on the Company's consolidated results of operations or financial position.

The Company recognizes the costs of legal defense for the legal proceedings to which it is a party in the periods incurred. After a considerable analysis of each case, the Company determines the amount of reserves required, if any. At this time, the Company has not accrued any reserve for any of these matters. Future reserves may be required if losses are deemed reasonably estimable and probable due to changes in the Company's assumptions, the effectiveness of legal strategies, or other factors beyond the Company's control. Future results of operations may be materially affected by the creation of reserves or by accruals of losses to reflect any adverse determinations in these legal proceedings.

### **New Accounting Pronouncements**

In May 2011, FASB issued ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS. The amendments in this update generally represent clarifications of Topic 820, but also include some instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed. This update results in common principles and requirements for measuring fair value and for disclosing information about fair value measurements in accordance with U.S. GAAP and IFRS. This update is effective for annual and interim periods beginning after December 15, 2011. We do not expect this update to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

## **Table of Contents**

### Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company is a purchaser of certain commodities, primarily corn and soybean meal, for use in manufacturing feed for its chickens. As a result, the Company's earnings are affected by changes in the price and availability of such feed ingredients. Feed grains are subject to volatile price changes caused by factors described below that include weather, size of harvest, transportation and storage costs and the agricultural policies of the United States and foreign governments. The price fluctuations of feed grains have a direct and material effect on the Company's profitability.

Generally, the Company purchases feed ingredients for deferred delivery from one month to six months after the time of purchase. The Company sometimes purchases its feed ingredients for prompt delivery to its feed mills at market prices at the time of such purchases. The grain purchases are made directly with our usual grain suppliers, which are companies in the regular business of supplying grain to end users, and do not involve options to purchase. Such purchases occur when senior management concludes that market factors indicate that prices at the time the grain is needed are likely to be higher than current prices, or where, based on current and expected market prices for the Company's poultry products, management believes it can purchase feed ingredients at prices that will allow the Company to earn a reasonable return for its shareholders. Market factors considered by management in determining whether or not and to what extent to buy grain for deferred delivery include:

Current market prices;

Current and predicted weather patterns in the United States, South America, China and other grain producing areas, as such weather patterns might affect the planting, growing, harvesting and yield of feed grains;

The expected size of the harvest of feed grains in the United States and other grain producing areas of the world as reported by governmental and private sources;

Current and expected changes to the agricultural policies of the United States and foreign governments;

The relative strength of United States currency and expected changes therein as it might impact the ability of foreign countries to buy United States feed grain commodities;

The current and expected volumes of export of feed grain commodities as reported by governmental and private sources;

The current and expected use of available feed grains for uses other than as livestock feed grains (such as the use of corn for the production of ethanol, which use is impacted by the price of crude oil); and

Current and expected market prices for the Company's poultry products.

The Company purchases physical grain, not financial instruments such as puts, calls or straddles that derive their value from the value of physical grain. Thus, the Company does not use derivative financial instruments as defined in ASC 815, "Accounting for Derivatives for Instruments and Hedging Activities," or any market risk sensitive instruments of the type contemplated by Item 305 of Regulation S-K. The Company does not enter into any derivative transactions or purchase any grain-related contracts other than the physical grain contracts described above.

Although the Company does not use derivative financial instruments as defined in ASC 815 or purchase market risk sensitive instruments of the type contemplated by Item 305 of Regulation S-K, the commodities that the Company does purchase for physical delivery, primarily corn and soybean meal, are subject to price fluctuations that have a direct and material effect on the Company's profitability as mentioned above. During

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the second quarter of fiscal 2012, the Company purchased approximately 22.1 million bushels of corn and approximately 191.149 tons of soybean meal for use in manufacturing feed for its live chickens. Thus, a \$1.00 change in the average market price paid per bushel for corn would have impacted the Company's cash outlays for corn by approximately \$22.1 million in the second quarter of fiscal 2012. Likewise, a \$10.00 change in the price paid per ton for soybean meal would impact the Company's cash outlays by approximately \$1.91 million.

**Table of Contents**

Although changes in the market price paid for feed grains impact cash outlays at the time the Company purchases the grain, such changes do not immediately impact cost of sales. The cost of feed grains is recognized in cost of sales, on a first-in-first-out basis, at the same time that the sales of the chickens that consume the feed grains are recognized. Thus, there is a lag between the time cash is paid for feed ingredients and the time the cost of such feed ingredients is reported in cost of goods sold. For example, corn delivered to a feedmill and paid for one week might be used to manufacture feed the following week. However, the chickens that eat that feed might not be processed and sold for another 48-62 days, and only at that time will the costs of the feed consumed by the chicken become included in cost of goods sold.

During the second quarter of fiscal 2012, the Company's average feed cost per pound of poultry products sold totaled \$0.3492 per pound. Feed costs per pound of poultry products sold consist primarily of feed grains, but also include other feed ingredients such as vitamins, fat and mineral feed supplements. The average feed cost per pound is influenced not only by the price of feed ingredients, but also by the efficiency with which live chickens convert feed into body weight. Factors such as weather, poultry husbandry, quality of feed ingredients and the quality and health of the bird, among others, affect the quantity of feed necessary to mature chickens to the target live weight and the efficiency of that process. Generally, however, a \$1.00 change in the average price paid per bushel of corn fed to a chicken during its life would have impacted average feed cost per pound of chicken products sold by \$0.0297, based on the quantity of grain used during the second fiscal quarter of 2012. Similarly, a \$10.00 change in the average price paid per ton of soybean meal would have influenced the average feed cost per pound of chicken products sold by \$0.0026 during the second fiscal quarter of 2012.

The following table shows the impact of hypothetical changes in the price of corn and soybean meal on both the Company's cash flow and cost of goods sold, based on quantities actually purchased in the second fiscal quarter of 2012:

Feed Ingredient	Quantity Purchased during the Second Fiscal Quarter of 2012	Hypothetical Price Change	Impact on Cash Outlay	Ultimate Impact on Feed Cost per Pound of Poultry Products Sold
Corn	22.1 million bushels	\$1.00 per bushel	\$ 22.1 million	\$ 0.0297/pound sold
Soybean meal	191,149 tons	\$10.00 per ton	\$ 1.91 million	\$ 0.0026/pound sold

The Company's interest expense is sensitive to changes in the general level of interest rates in the United States. The Company maintains certain of its debt as fixed rate in nature to mitigate the impact of fluctuations in interest rates. The fair value of the Company's fixed rate debt approximates the carrying amount at April 30, 2012. Management believes the potential effects of near-term changes in interest rates on the Company's debt are not material.

**Item 4. Controls and Procedures**

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

An evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective as of April 30, 2012. There have been no changes in the Company's internal control over financial reporting during the fiscal quarter ended April 30, 2012 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **Table of Contents**

### **PART II. OTHER INFORMATION**

#### **Item 1. Legal Proceedings**

On February 16, 2012, two of our former employees sued us and seven of our current and former employees in the United States District Court for the Middle District of Georgia for damages allegedly caused to them by the defendants' alleged violations of the federal and State of Georgia's Racketeer Influenced and Corrupt Organizations ( " RICO " ) Acts. The plaintiffs filed the lawsuit on behalf of all hourly-paid workers legally authorized to be employed in the United States who have been employed at our processing plant located in Moultrie, Georgia since 2008.

The plaintiffs allege in their complaint that the defendants conspired to knowingly hire undocumented immigrants at the Moultrie plant to save Sanderson millions of dollars in labor costs because illegal aliens will work for extremely low wages, will typically not complain about workplace conditions and injuries, and because of their vulnerable situation, will accede to managers' demands to work harder than American citizens and legal aliens. The action is brought as a class action lawsuit on behalf of all persons legally authorized to be employed in the United States who have been employed at the Moultrie plant as hourly wage earners in the four years before the filing of the case, and the plaintiffs seek certification of that class. The plaintiffs are suing for money damages, injunctive relief and revocation of our license to conduct business in the State of Georgia.

Based on our present knowledge, we consider the claims made in this lawsuit to be baseless.

The Company is involved in other various claims and litigation incidental to its business. Although the outcome of these matters cannot be determined with certainty, management, upon the advice of counsel, is of the opinion that the final outcome should not have a material effect on the Company's consolidated results of operations or financial position.

The Company recognizes the costs of legal defense for the legal proceedings to which it is a party in the periods incurred. After a considerable analysis of each case, the Company determines the amount of reserves required, if any. At this time, the Company has not accrued any reserve for any of these matters. Future reserves may be required if losses are deemed reasonably estimable and probable due to changes in the Company's assumptions, the effectiveness of legal strategies, or other factors beyond the Company's control. Future results of operations may be materially affected by the creation of reserves or by accruals of losses to reflect any adverse determinations in these legal proceedings.

**Table of Contents**

## Item 1A. Risk Factors

There have been no material changes from the risk factors previously disclosed in the Company's Form 10-K for the fiscal year ended October 31, 2011.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

During its first fiscal quarter, the company repurchased shares of its common stock as follows:

Period	(a) Total Number of Shares Purchased <sup>1</sup>	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>2</sup>	(d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs <sup>3</sup>
February 1, 2012 - February 29, 2012	8,818	\$ 49.02	8,818	1,000,000
March 1, 2012 - March 31, 2012	1,527	\$ 53.03	1,527	1,000,000
April 1, 2012 - April 30, 2012	0	\$ 0	0	1,000,000
Total	10,345	\$ 49.61	10,345	1,000,000

<sup>1</sup> All purchases were made pursuant to the Company's Stock Incentive Plan under which participants may satisfy tax withholding obligations incurred upon the vesting of restricted stock by requesting the Company to withhold shares with a value equal to the amount of the withholding obligation.

<sup>2</sup> On February 16, 2012, the Company's Board of Directors approved a share repurchase program under which the Company may purchase up to 1 million shares of its common stock in open market transactions or negotiated purchases, subject to market conditions, share price and other considerations. The authorization will expire on February 16, 2014. Unlike the Company's previous share repurchase programs, the Company's repurchase of vested restricted stock to satisfy tax withholding obligations of its Stock Incentive Plan participants will not be made under the 2012 general repurchase plan.

<sup>3</sup> Does not include vested restricted shares that may yet be repurchased under the Stock Incentive Plan as described in Note 1.

## **Table of Contents**

### Item 6. Exhibits

The following exhibits are filed with this report.

Exhibit 3.1 Articles of Incorporation of the Registrant dated October 19, 1978. (Incorporated by reference to Exhibit 4.1 filed with the registration statement on Form S-8 filed by the Registrant on July 15, 2002, Registration No. 333-92412.)

Exhibit 3.2 Articles of Amendment, dated March 23, 1987, to the Articles of Incorporation of the Registrant. (Incorporated by reference to Exhibit 4.2 filed with the registration statement on Form S-8 filed by the Registrant on July 15, 2002, Registration No. 333-92412.)

Exhibit 3.3 Articles of Amendment, dated April 21, 1989, to the Articles of Incorporation of the Registrant. (Incorporated by reference to Exhibit 4.3 filed with the registration statement on Form S-8 filed by the Registrant on July 15, 2002, Registration No. 333-92412.)

Exhibit 3.4 Certificate of Designations of Series A Junior Participating Preferred Stock of the Registrant dated April 21, 1989. (Incorporated by reference to Exhibit 4.4 filed with the registration statement on Form S-8 filed by the Registrant on July 15, 2002, Registration No. 333-92412.)

Exhibit 3.5 Article of Amendment, dated February 20, 1992, to the Articles of Incorporation of the Registrant. (Incorporated by reference to Exhibit 4.5 filed with the registration statement on Form S-8 filed by the Registrant on July 15, 2002, Registration No. 333-92412.)

Exhibit 3.6 Article of Amendment, dated February 27, 1997, to the Articles of Incorporation of the Registrant. (Incorporated by reference to Exhibit 4.6 filed with the registration statement on Form S-8 filed by the Registrant on July 15, 2002, Registration No. 333-92412.)

Exhibit 3.7 Bylaws of the Registrant, amended and restated as of April 23, 2009. (Incorporated by reference to Exhibit 3 filed with the Registrant's Current Report on Form 8-K on April 28, 2009.)

Exhibit 15\* Accountants' Letter re: Unaudited Financial Information.

Exhibit 31.1\* Certification of Chief Executive Officer.

Exhibit 31.2\* Certification of Chief Financial Officer.

Exhibit 32.1\*\* Section 1350 Certification.

Exhibit 32.2\*\* Section 1350 Certification.

Exhibit 101.INS\*\*\* XBRL Instance Document

Exhibit 101.SCH\*\*\* XBRL Taxonomy Extension Schema

Exhibit 101.CAL\*\*\* XBRL Taxonomy Extension Calculation Linkbase

Exhibit 101.DEF\*\*\* XBRL Taxonomy Extension Definition Linkbase

Exhibit 101.LAB\*\*\* XBRL Taxonomy Extension Label Linkbase

Exhibit 101.PRE\*\*\* XBRL Taxonomy Extension Presentation Linkbase



**Table of Contents**

- \* Filed herewith.
- \*\* Furnished herewith.
- \*\*\* Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability under these sections.
- + Management contract or compensatory plan or arrangement.

**Table of Contents**

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SANDERSON FARMS, INC.  
(Registrant)

Date: May 29, 2012

By: /s/ D. Michael Cockrell  
Treasurer and Chief Financial Officer

Date: May 29, 2012

By: /s/ James A. Grimes  
Secretary, Corporate Controller and  
Chief Accounting Officer

## **Table of Contents**

### INDEX TO EXHIBITS

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**Table of Contents**

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