SMITHFIELD FOODS INC
Form 10-Q
March 12, 2010

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 January 31, 2010

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 ¨

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 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 ¨

Non-accelerated filer ¨ Smaller reporting company ¨

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

At March 5, 2010, 165,835,632 shares of the registrant's Common Stock ($.50 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, except per share data)

	Three Months Ended		Nine Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(unaudited)		(unaudited)	
Sales	$2,884.7	$3,348.2	$8,292.4	$9,637.1
Cost of sales	2,600.5	3,263.9	7,741.2	9,125.0
Gross profit	284.2	84.3	551.2	512.1
Selling, general and administrative expenses	194.5	202.2	558.3	602.5
Equity in (income) loss of affiliates	(6.8)	17.6	(30.6)	41.6
Operating profit (loss)	96.5	(135.5)	23.5	(132.0)
Interest expense	67.2	62.2	198.9	163.7
Other (income) loss	-	(63.5)	11.0	(63.5)
Income (loss) from continuing operations before income taxes	29.3	(134.2)	(186.4)	(232.2)
Income tax benefit	(8.0)	(26.1)	(89.6)	(62.5)
Income (loss) from continuing operations	37.3	(108.1)	(96.8)	(169.7)
Income from discontinued operations, net of tax of $2.1 and $44.3	-	2.4	-	52.5
Net income (loss)	$37.3	$(105.7)	$(96.8)	$(117.2)
Income (loss) per basic and diluted share:				
Continuing operations	$.22	$(.75)	$(.63)	$(1.21)
Discontinued operations	-	.01	-	.37
Net income (loss)	$.22	$(.74)	$(.63)	$(.84)
Weighted average shares:				
Weighted average basic shares	165.8	143.6	154.2	140.3
Effect of dilutive stock options	0.2	-	-	-
Weighted average diluted shares	166.0	143.6	154.2	140.3

See Notes to Consolidated Condensed Financial Statements

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

	January 31, 2010 (Unaudited)	May 3, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 401.7	$ 119.0
Accounts receivable, net	651.1	595.2
Inventories	1,843.4	1,896.1
Prepaid expenses and other current assets	372.6	174.2
Total current assets	3,268.8	2,784.5
Property, plant and equipment, net	2,376.9	2,443.0
Goodwill	823.0	820.0
Investments	643.9	601.6
Intangible assets, net	390.7	392.2
Other assets	201.1	158.9
Total assets	$ 7,704.4	$ 7,200.2
LIABILITIES AND EQUITY		
Current liabilities:		
Notes payable	$ 25.1	$ 17.5
Current portion of long-term debt and capital lease obligations	86.1	320.8
Accounts payable	378.6	390.2
Accrued expenses and other current liabilities	631.6	558.3
Total current liabilities	1,121.4	1,286.8
Long-term debt and capital lease obligations	2,892.8	2,567.3
Other liabilities	783.4	715.5
Redeemable noncontrolling interests	-	8.3
Commitments and contingencies		
Equity:		
Shareholders' equity:		
Preferred stock, $1.00 par value, 1,000,000 authorized shares	-	-
Common stock, $.50 par value, 500,000,000 authorized shares; 165,835,632 and 143,576,842 issued and outstanding	82.9	71.8
Additional paid-in capital	1,612.6	1,353.8
Stock held in trust	(65.4)	(64.8)
Retained earnings	1,543.3	1,640.1
Accumulated other comprehensive loss	(275.2)	(388.5)
Total shareholders’ equity	2,898.2	2,612.4

Noncontrolling interests		8.6		9.9
Total equity		2,906.8		2,622.3
Total liabilities and equity	$	7,704.4	$	7,200.2

See Notes to Consolidated Condensed Financial Statements

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

	Nine Months Ended	
	January 31, 2010	February 1, 2009
	(Unaudited)	
Cash flows from operating activities:		
Net loss	$ (96.8)	$ (117.2)
Adjustments to reconcile net cash flows from operating activities:		
Income from discontinued operations, net of tax	-	(52.5)
Impairment of assets	45.1	78.2
Equity in (income) loss of affiliates	(30.6)	41.6
Depreciation and amortization	178.3	207.3
Loss on sale of property, plant and equipment	18.5	9.9
Gain on sale of investments	(4.5)	(57.6)
Changes in operating assets and liabilities and other, net	32.5	(29.4)
Net cash flows from operating activities	142.5	80.3
Cash flows from investing activities:		
Capital expenditures	(136.4)	(154.4)
Dispositions	23.3	575.5
Insurance proceeds	9.9	-
Investments and other	12.5	3.7
Net cash flows from investing activities	(90.7)	424.8
Cash flows from financing activities:		
Proceeds from the issuance of long-term debt	840.1	600.0
Principal payments on long-term debt and capital lease obligations	(323.7)	(169.4)
Net repayments on revolving credit facilities and notes payables	(479.4)	(892.3)
Proceeds from the issuance of common stock and stock option exercises	294.8	122.3
Repurchases of debt	-	(86.2)
Purchase of call options	-	(88.2)
Proceeds from the sale of warrants	-	36.7
Debt issuance costs and other	(62.8)	(11.0)
Purchase of redeemable noncontrolling interest	(38.9)	-
Net cash flows from financing activities	230.1	(488.1)
Cash flows from discontinued operations:		
Net cash flows from operating activities	-	34.7
Net cash flows from investing activities	-	(7.0)
Net cash flows from financing activities	-	(0.8)
Net cash flows from discontinued operations activities	-	26.9
Effect of foreign exchange rate changes on cash	0.8	(10.6)
Net change in cash and cash equivalents	282.7	33.3
Cash and cash equivalents at beginning of period	119.0	57.3
Cash and cash equivalents at end of period	$ 401.7	$ 90.6

Non-cash investing and financing activities:		
Investment in Butterball	$ -	$ (24.5)
Common stock issued for acquisition	$ -	$ (60.4)

See Notes to Consolidated Condensed Financial Statements

SMITHFIELD FOODS, INC.
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

NOTE 1: GENERAL

Smithfield Foods, Inc., together with its subsidiaries (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 five reporting segments: Pork, International, Hog Production, Other and Corporate.

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 May 3, 2009. The enclosed interim consolidated condensed financial information is unaudited. 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.

Unless otherwise stated, the amounts presented in these notes to our consolidated condensed financial statements are based on continuing operations for all fiscal periods included. The three months ended January 31, 2010 correspond to the third quarter of fiscal 2010 and the three months ended February 1, 2009 correspond to the third quarter of fiscal 2009. Certain prior year amounts have changed as a result of the adoption of certain accounting pronouncements as discussed in Note 2—Accounting Changes and New Accounting Guidance, and to conform to current year presentations.

Our year consists of either 52 or 53 weeks, ending on the Sunday nearest April 30. The three and nine months ended January 31, 2010 consisted of 13 and 39 weeks, respectively. The three and nine months ended February 1, 2009 consisted of 14 and 40 weeks, respectively.

NOTE 2: ACCOUNTING CHANGES AND NEW ACCOUNTING GUIDANCE

In January 2010, the Financial Accounting Standards Board (FASB) issued authoritative guidance intended to improve disclosures about fair value measurements. The guidance requires entities to disclose significant transfers in and out of fair value hierarchy levels and the reasons for the transfers and to present information about purchases, sales, issuances and settlements separately in the reconciliation of fair value measurements using significant unobservable inputs (Level 3). Additionally, the guidance clarifies that a reporting entity should provide fair value measurements for each class of assets and liabilities and disclose the inputs and valuation techniques used for fair value measurements using significant other observable inputs (Level 2) and significant unobservable inputs (Level 3). The new guidance is effective for interim and annual periods beginning after December 15, 2009. Accordingly, we will adopt the new guidance in the fourth quarter of fiscal 2010.

In June 2009 and December 2009, the FASB issued guidance requiring an analysis to determine whether a variable interest gives the entity a controlling financial interest in a variable interest entity. This guidance requires an ongoing assessment and eliminates the quantitative approach previously required for determining whether an entity is the primary beneficiary. This guidance is effective for fiscal years beginning after November 15, 2009. Accordingly, we will adopt this guidance in fiscal year 2011. We are in the process of evaluating the potential impacts of such adoption.

In April 2009, the FASB issued new disclosure requirements about the fair value of financial instruments in interim financial statements. We adopted the new requirements in the first quarter of fiscal 2010. See Note 15—Fair Value

Measurements for required disclosures.

In September 2008, the Emerging Issues Task Force (EITF) issued guidance for determining whether an equity-linked financial instrument (or embedded feature) is indexed to an entity's own stock. The new guidance requires retrospective application with restatement of prior periods. We adopted the new guidance in the first quarter of fiscal 2010 and determined that it had no impact on our consolidated condensed financial statements.

In May 2008, the FASB issued new accounting guidance for convertible debt instruments that may be settled in cash upon conversion (including partial cash settlement). Under the new guidance, issuers of such instruments should separately account for the liability and equity components in a manner that will reflect the entity's nonconvertible debt borrowing rate when interest cost is recognized in subsequent periods. The amount allocated to the equity component represents a discount to the debt, which is amortized into interest expense using the effective interest method over the life of the debt. We adopted the new accounting guidance in the first quarter of fiscal 2010 and applied it retrospectively to all periods presented. Refer to Note 9—Debt for further discussion of the impact of this new accounting guidance on our consolidated condensed financial statements.

In December 2007, the FASB issued new accounting and disclosure guidance on how to recognize, measure and present assets acquired, liabilities assumed, noncontrolling interests and any goodwill recognized in a business combination. The objective of this new guidance is to improve the information included in financial reports about the nature and financial effects of business combinations. We adopted the new guidance in the first quarter of fiscal 2010, and will apply it prospectively to all future business combinations. The adoption did not have a significant impact on our consolidated condensed financial statements, and the impact on our consolidated condensed financial statements in future periods will depend on the nature and size of any future business combinations.

In December 2007, the FASB issued new accounting and reporting guidance for a noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This guidance clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity and should be reported as equity in the consolidated financial statements, rather than as a liability or in the mezzanine section between liabilities and equity. The new guidance also requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. We adopted the new accounting guidance in the first quarter of fiscal 2010, and are applying it prospectively, except for the consolidated condensed statements of income where income attributable to noncontrolling interests is immaterial for the periods presented. The new presentation and disclosure requirements have been applied retrospectively. The adoption of this guidance did not have a significant impact on our consolidated condensed financial statements.

In September 2006, the FASB issued new accounting and disclosure guidance that defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States, and expands disclosures about fair value measurements. It does not require any new fair value measurements. The new guidance was effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years for financial assets and liabilities, and for fiscal years beginning after November 15, 2008 for all nonrecurring fair value measurements of nonfinancial assets and liabilities. We adopted the new guidance for financial assets and liabilities in the first quarter of fiscal 2009 and for nonrecurring fair value measurements of nonfinancial assets and liabilities in the first quarter of fiscal 2010. The adoption did not have a significant impact on our consolidated financial statements. See Note 15— Fair Value Measurements for additional disclosures on fair value measurements.

NOTE 3: DISCONTINUED OPERATIONS

Smithfield Beef, Inc. (Smithfield Beef)

In March 2008 (fiscal 2008), we entered into an agreement with JBS S.A., a company organized and existing under the laws of Brazil (JBS), to sell Smithfield Beef, our beef processing and cattle feeding operation that encompassed our entire Beef segment. In October 2008 (fiscal 2009), we completed the sale of Smithfield Beef for $575.5 million in cash.

The remaining live cattle inventories of Smithfield Beef, which were excluded from the JBS transaction, were sold in the first quarter of fiscal 2010. Our results from the sale of the live cattle inventories that were excluded from the JBS transaction are reported in income from continuing operations in the Other segment.

We recorded an estimated pre-tax gain of $95.2 million ($51.9 million net of tax) on the sale of Smithfield Beef in income from discontinued operations in the second quarter of fiscal 2009. We recorded an additional gain of approximately $4.5 million ($2.4 million net of tax) in the third quarter of fiscal 2009 for the settlement of differences in working capital at closing from agreed-upon targets. These gains were recorded in income (loss) from discontinued operations.

The following table presents sales, interest expense and net income of Smithfield Beef for the fiscal periods indicated. Interest expense is allocated to discontinued operations based on specific borrowings by the discontinued operations.

These results are reported in income from discontinued operations.

	Three Months Ended		Nine Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(in millions)		(in millions)	
Sales	$ -	$ -	$ -	$ 1,699.0
Interest expense	-	-	-	17.3
Net income	-	-	-	0.9

Smithfield Bioenergy, LLC (SBE)

In April 2007 (fiscal 2007), we decided to exit the alternative fuels business and in May 2008 (fiscal 2009), we completed the sale of substantially all of the assets of SBE for $11.5 million. The results of SBE are presented in income from discontinued operations. The following table presents sales, interest expense and net loss of SBE for the fiscal periods indicated. These results are reported in income from discontinued operations.

	Three Months Ended		Nine Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(in millions)		(in millions)	
Sales	$ -	$ -	$ -	$ 3.8
Interest expense	-	-	-	1.3
Net loss	-	-	-	(2.7)

NOTE 4: INVENTORIES

Inventories consist of the following:

	January 31, 2010	May 3, 2009
	(in millions)	
Live hogs	$ 846.3	$ 838.4
Fresh and packaged meats	742.8	789.1
Manufacturing supplies	83.1	72.7
Grains and other	171.2	195.9
Total inventories	$ 1,843.4	$ 1,896.1

NOTE 5: DERIVATIVES AND HEDGING ACTIVITIES

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 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, and will in the future, avail ourselves of either acceptable method. We believe all of our derivative instruments represent economic hedges against changes in prices and rates, regardless of their designation for accounting purposes.

We do not offset amounts recognized for derivative instruments and amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from derivative instruments recognized at fair value executed with the same counterparty under a master netting arrangement. As of January 31, 2010, prepaid expenses and other current assets included $88.2 million representing cash on deposit with brokers to cover losses on our open derivative instruments. Changes in commodity prices could have a significant impact on cash deposit requirements under our broker and counterparty agreements. As of January 31, 2010, we had $14.0 million posted as collateral related to an interest rate swap. We have reviewed our derivative contracts and have determined that they do not contain credit contingent features which would require us to post additional collateral if we did not maintain a credit rating equivalent to what was in place at the time the contracts were entered into.

We are exposed to losses in the event of nonperformance or nonpayment by counterparties under financial instruments. Although our counterparties 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 counterparties with whom we maintain margin accounts that are settled on a daily basis, and therefore our credit risk is not significant. Determination of the credit quality of our counterparties is based upon a number of factors, including credit ratings and our evaluation of their financial condition. As of January 31, 2010, we had credit exposure of $4.8 million on non-exchange traded derivative contracts, excluding the effects of netting arrangements. As a result of netting arrangements, our credit exposure was reduced to $3.8 million. No significant concentrations of credit risk existed as of January 31, 2010.

The size and mix of our derivative portfolio varies from time to time based upon our analysis of current and future market conditions. The following table presents the fair values of our open derivative financial instruments in the consolidated balance sheets on a gross basis. All grain contracts, livestock contracts and foreign exchange 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. Interest rate contracts are recorded in accrued expenses and other current liabilities or other liabilities, as appropriate.

	Assets		Liabilities	
	January 31, 2010	May 3, 2009	January 31, 2010	May 3, 2009
	(in millions)		(in millions)	
Derivatives using the "hedge accounting" method:				
Grain contracts	$ 6.9	$ 10.4	$ 21.6	$ 17.7
Livestock contracts	11.6	-	2.0	-
Interest rate contracts	-	0.6	9.6	10.3
Foreign exchange contracts	2.1	2.8	0.1	14.4
Total	20.6	13.8	33.3	42.4
Derivatives using the “mark-to-market” method:				
Grain contracts	1.5	10.2	12.9	16.2
Livestock contracts	11.8	21.9	10.5	6.3
Energy contracts	0.1	-	3.9	13.0
Foreign exchange contracts	1.7	0.3	0.8	1.6
Total	15.1	32.4	28.1	37.1
Total fair value of derivative instruments	$ 35.7	$ 46.2	$ 61.4	$ 79.5

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 the forecasted purchase of corn and soybean meal. In addition, we enter into interest rate swaps to manage our exposure to changes in interest rates associated with our variable interest rate debt, and 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. We generally do not hedge anticipated transactions beyond twelve months.

During the nine months ended January 31, 2010, the range of notional volumes associated with open derivative instruments designated in cash flow hedging relationships was as follows:

	Minimum	Maximum	Metric
Commodities:			
Corn	-	79,035,000	Bushels
Soybean meal	78,900	551,200	Tons
Lean Hogs	-	264,800,000	Pounds
Interest rate	200,000,000	200,000,000	U.S. Dollars
Foreign currency (1)	37,993,270	106,247,277	

	U.S. Dollars

(1) Amounts represent the U.S. dollar equivalent of various foreign exchange contracts.

When cash flow hedge accounting is applied, derivative gains or losses from these cash flow hedges are recognized as a component of other comprehensive income (loss) (OCI) 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, interest expense for interest rate contracts, and selling, general and administrative expenses for foreign exchange contracts.

The following table presents the effects on our consolidated condensed financial statements of gains and losses on derivative instruments designated in cash flow hedging relationships for the fiscal periods indicated:

	Gain (Loss) Recognized in OCI on Derivative (Effective Portion)		Gain (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)		Loss Recognized in Earnings on Derivative (Ineffective Portion)	
	Three Months Ended		Three Months Ended		Three Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(in millions)		(in millions)		(in millions)	
Commodity contracts:						
Grain contracts	$ (12.7)	$ 14.1	$ (0.6)	$ (41.1)	$ 0.2	$ 3.4
Lean hog contracts	(3.8)	-	1.7	-	(0.3)	-
Interest rate contracts	(0.9)	(6.1)	(1.1)	(0.8)	-	-
Foreign exchange contracts	1.0	(8.1)	1.1	(1.3)	-	-
Total	$ (16.4)	$ (0.1)	$ 1.1	$ (43.2)	$ (0.1)	$ 3.4

	Nine Months Ended		Nine Months Ended		Nine Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(in millions)		(in millions)		(in millions)	
Commodity contracts:						
Grain contracts	$ (9.9)	$ (202.6)	$ (84.3)	$ (42.0)	$ (6.6)	$ (4.7)
Lean hog contracts	1.9	-	4.9	-	(0.4)	-
Interest rate contracts	0.5	(11.1)	(3.7)	(1.1)	-	-
Foreign exchange contracts	11.6	(9.1)	(3.5)	(0.8)	-	-
Total	$ 4.1	$ (222.8)	$ (86.6)	$ (43.9)	$ (7.0)	$ (4.7)

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 January 31, 2010, there were deferred net losses of $16.0 million, net of tax of $10.2 million, in accumulated other comprehensive loss. As of May 3, 2009, there were deferred net losses of $77.1 million, net of tax of $34.6 million, in accumulated other comprehensive loss. We expect to reclassify $2.5 million ($1.5 million net of tax) of the deferred net losses on closed commodity contracts into earnings within the next twelve months.

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. We also enter into interest rate swaps to manage interest rate risk associated with our fixed rate borrowings. When fair value hedge accounting is applied, derivative gains and losses from these fair value hedges 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 and interest expense for interest rate contracts.

During the nine months ended January 31, 2010, the range of notional volumes associated with open derivative instruments designated in fair value hedging relationships was as follows:

	Minimum	Maximum	Metric
Commodities:			
Corn	2,435,000	11,610,000	Bushels
Lean Hogs	-	726,160,000	Pounds
Interest rate	-	50,000,000	U.S. Dollars
Foreign currency (1)	16,051,549	24,836,547	U.S. Dollars

(1) Amounts represent the U.S. dollar equivalent of various foreign exchange contracts.

The following table presents 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:

	Gain (Loss) Recognized in Earnings on Derivative Three Months Ended		Gain (Loss) Recognized in Earnings on Related Hedged Item Three Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(in millions)		(in millions)	
Commodity contracts	$ 11.1	$ 0.1	$ (15.5)	$ -
Interest rate contracts	-	0.4	-	(0.4)
Foreign exchange contracts	(0.3)	(0.6)	0.3	-
Total	$ 10.8	$ (0.1)	$ (15.2)	$ (0.4)

	Nine Months Ended		Nine Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(in millions)		(in millions)	
Commodity contracts	$ 18.0	$ 13.6	$ (21.2)	$ (14.8)
Interest rate contracts	0.6	2.4	(0.6)	(2.4)
Foreign exchange contracts	2.8	(1.8)	(1.1)	-
Total	$ 21.4	$ 14.2	$ (22.9)	$ (17.2)

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 selling, general and administrative expenses for interest rate contracts and foreign exchange contracts.

During the nine months ended January 31, 2010, 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	9,000,000	872,160,000	Pounds
Corn	3,125,000	27,560,000	Bushels
Soybean meal	-	501,272	Tons
Soybeans	140,000	575,000	Bushels
Wheat	-	360,000	Bushels
Live cattle	-	6,000,000	Pounds
Pork bellies	-	1,920,000	Pounds
Natural gas	2,770,000	5,040,000	Million BTU's
Foreign currency (1)	60,029,232	152,462,490	U.S. Dollars

(1) Amounts represent the U.S. dollar equivalent of various foreign exchange contracts.

The following table presents the amount of gains (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:

	Three Months Ended		Nine Months Ended	
	January 31, 2010	February 1, 2009	January 31, 2010	February 1, 2009
	(in millions)		(in millions)	
Commodity contracts	$(8.1)	$22.7	$6.4	$74.0
Interest rate contracts	-	-	-	0.2
Foreign exchange contracts	(0.9)	5.3	(11.9)	6.3
Total	$(9.0)	$28.0	$(5.5)	$80.5

NOTE 6: IMPAIRMENT OF LONG-LIVED ASSETS

Hog Farms

In June 2009 (fiscal 2010), we decided to further reduce our domestic sow herd by 3%, or approximately 30,000 sows, which was accomplished by ceasing hog production operations and closing certain of our hog farms. In addition, in the first quarter of fiscal 2010, we began marketing certain other hog farms. As a result of these decisions, we recorded total impairment charges of $34.1 million, including an allocation of goodwill, in the first quarter of fiscal 2010 to write down the hog farm assets to their estimated fair values. The impairment charges were recorded in the Hog Production segment. See Note 15—Fair Value Measurements for further discussion.

Prior to the third quarter of fiscal 2010, we had classified certain hog farm assets that were being marketed as held for sale within prepaid expenses and other current assets in the consolidated condensed balance sheets. During the third quarter of fiscal 2010, it became apparent that a sale of these assets was not likely to be completed within twelve months. We have reclassified these assets, which consist primarily of property, plant and equipment, as assets held and used within property, plant and equipment, net in the consolidated condensed balance sheets. The carrying amount of these assets was $27.9 million as of January 31, 2010 and $33.1 million as of May 3, 2009.

RMH Foods, LLC (RMH)

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

In December 2009 (fiscal 2010), we completed the sale of RMH for $9.1 million, plus $1.4 million of liabilities assumed by the buyer.

Sioux City, Iowa Plant

In January 2010 (fiscal 2010), we announced that we will be closing our fresh pork processing plant located in Sioux City, Iowa in April 2010 (fiscal 2010). The Sioux City plant is one of our oldest and least efficient plants. The plant design severely limits our ability to produce value-added packaged meats products and maximize production throughput. A majority of the plant's production will be transferred to other nearby Smithfield plants.

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

NOTE 7: RESTRUCTURING

In February 2009 (fiscal 2009), we announced a plan to consolidate and streamline the corporate structure and manufacturing operations of our Pork segment (the Restructuring Plan). The Restructuring Plan included the closure of six plants, the last of which was closed in February 2010 (fiscal 2010).

The following table summarizes the balance of accrued expenses, the cumulative expense incurred to date and the expected remaining expenses to be incurred related to the Restructuring Plan by major type of cost. All of these charges were recorded in the Pork segment.

	Accrued Balance May 3, 2009	1st Quarter FY 2010 Expense	2nd Quarter FY 2010 Expense	3rd Quarter FY 2010 Expense	Payments	Accrued Balance January 31, 2010	Cumulative Expense-to-Date	Estimated Remaining Expense
Restructuring charges:				(in millions)				
Employee severance and related benefits	$ 11.9	$ (0.2)	$ 0.4	$ 0.2	$ (3.0)	$ 9.3	$ 12.7	$ 0.4
Other associated costs	0.5	6.5	3.0	3.1	(11.4)	1.7	14.3	8.5
Total restructuring charges	$ 12.4	$ 6.3	$ 3.4	$ 3.3	$ (14.4)	$ 11.0	27.0	$ 8.9
Impairment charges:								
Property, plant and equipment							69.9	
Inventory							4.8	
Total impairment charges							74.7	
Total restructuring and impairment charges							$ 101.7	

Employee severance and related benefits primarily include severance benefits and an estimated obligation for the partial withdrawal from a multiemployer pension plan. Other associated costs consist primarily of plant consolidation and plant wind-down expenses, all of which are expensed as incurred. Of the $13.5 million of restructuring and impairment charges recorded in fiscal 2010, $8.6 million was recorded in cost of sales with the remainder recorded in selling, general and administrative expenses. Substantially all of the estimated remaining expenses are expected to be incurred by the first half of fiscal 2011.

NOTE 8: INVESTMENTS

Investments consist of the following:

Equity Investment	% Owned	January 31, 2010	May 3, 2009
		(in millions)	
Campofrío Food Group (CFG) (1)	37%	$444.5	$417.8
Butterball, LLC (Butterball)	49%	96.3	78.2
Mexican joint ventures	Various	66.7	53.9
Other	Various	36.4	51.7
Total investments		$643.9	$601.6

(1) Prior to the third quarter of fiscal 2009, we owned 50% of Groupe Smithfield S.L. (Groupe Smithfield) and 24% of Campofrío Alimentación, S.A. (Campofrío). Those entities merged in the third quarter of fiscal 2009 to form CFG, of which we currently own 37%. The amounts presented for CFG throughout this Quarterly Report on Form 10-Q represent the combined historical results of Groupe Smithfield and Campofrío.

Equity in (income) loss of affiliates consists of the following:

Equity Investment	Segment	Three Months Ended January 31, 2010	Three Months Ended February 1, 2009	Nine Months Ended January 31, 2010	Nine Months Ended February 1, 2009
		(in millions)		(in millions)	
Butterball	Other	$(7.9)	$(3.9)	$(15.3)	$16.6
CFG (2)	International	5.3	0.6	(2.5)	4.2
Mexican joint ventures	Various	(4.4)	9.1	(11.3)	10.3
All other equity method investments	Various	0.2	11.8	(1.5)	10.5
Equity in (income) loss of affiliates		$(6.8)	$17.6	$(30.6)	$41.6

(2) 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.

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CFG

As of January 31, 2010, we held 37,811,302 shares of CFG common stock. The stock was valued at €6.48 per share (approximately $8.98 per share) on the close of the last day of trading before the end of our third quarter of fiscal 2010. Based on the stock price and foreign exchange rate as of January 31, 2010, the carrying value of our investment in CFG, net of the cumulative translation adjustment, exceeded the market value of the underlying securities by $79.9 million. We have analyzed our investment in CFG for impairment and have determined that the decline in value is temporary. We have based our conclusion on the historical prices and trading volumes of the stock, the impact of the movement in foreign currency translation, the duration of time in which the carrying value of the investment exceeded its fair value, our level of involvement with the entity, and our intent and ability to hold the investment long-term. Based on our assessment, no impairment was recorded.

In the third quarter of fiscal 2010, as part of a debt restructuring, CFG redeemed certain of its debt instruments and as a result, we recorded $10.4 million of charges in equity income in the third quarter of fiscal 2010.

During the first quarter of fiscal 2010, we received a cash dividend from CFG totaling approximately $16.6 million.

Sale of Farasia Corporation (Farasia)

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

NOTE 9: DEBT

2014 Notes

In July 2009 (fiscal 2010), we issued $625 million aggregate principal amount of 10% senior secured notes at a price equal to 96.201% of their face value. In August 2009 (fiscal 2010), we issued an additional $225 million aggregate principal amount of 10% senior secured notes at a price equal to 104% of their face value, plus accrued interest from July 2, 2009 to August 14, 2009. Collectively, these notes, which mature in July 2014, are referred to as the “2014 Notes.”

Interest payments are due semi-annually on January 15 and July 15. The 2014 Notes are guaranteed by substantially all of our U.S. subsidiaries. The 2014 Notes are secured by first-priority liens, subject to permitted liens and exceptions for excluded assets, in substantially all of the guarantors’ real property, fixtures and equipment (collectively, the Non-ABL Collateral) and are secured by second-priority liens on cash and cash equivalents, deposit accounts, accounts receivable, inventory, other personal property relating to such inventory and accounts receivable and all proceeds therefrom, intellectual property, and certain capital stock and interests, which secure the ABL Credit Facility (as defined below) on a first-priority basis (collectively, the ABL Collateral).

The 2014 Notes will rank equally in right of payment to all of our existing and future senior debt and senior in right of payment to all of our existing and future subordinated debt. The guarantees will rank equally in right of payment with all of the guarantors’ existing and future senior debt and senior in right of payment to all of the guarantors’ existing and future subordinated debt. In addition, the 2014 Notes are structurally subordinated to the liabilities of our non-guarantor subsidiaries.

We incurred offering expenses of approximately $22.8 million, which are being amortized, along with the discount and premium, into interest expense over the five-year life of the 2014 Notes. We used the net proceeds from the issuance of the 2014 Notes, together with other available cash, to repay borrowings and terminate commitments under our then existing $1.3 billion secured revolving credit agreement (the U.S. Credit Facility), to repay the outstanding balance under our then existing €300 million European secured revolving credit facility (the Euro Credit Facility), to repay and/or refinance other indebtedness and for other general corporate purposes. We cancelled the Euro Credit Facility, which was scheduled to mature in August 2010 (fiscal 2011), upon repayment of the outstanding balance. In the second quarter of fiscal 2010, in connection with the cancellation of the Euro Credit Facility, we recorded $3.0 million of charges primarily related to the write-off of unamortized costs associated with the facility as a loss on debt extinguishment.

Asset-Based Credit Facility

In July 2009 (fiscal 2010), we entered into a new asset-based revolving credit agreement totaling $1.0 billion that supports short-term funding needs and letters of credit (the ABL Credit Facility), which, along with the 2014 Notes, replaced the U.S. Credit Facility, which was scheduled to expire in August 2010 (fiscal 2011). Loans made under the ABL Credit Facility will mature and the commitments thereunder will terminate in July 2012. However, the ABL Credit Facility will be subject to an earlier maturity if we fail to satisfy certain conditions related to the refinancing or repayment of our senior notes due 2011. The ABL Credit Facility provides for an option, subject to certain conditions, to increase total commitments to $1.3 billion in the future.

The ABL Credit Facility requires an unused commitment fee of 1% per annum on the undrawn portion of the facility (subject to a stepdown in the event more than 50% of the commitments under the facility are utilized).

Obligations under the ABL Credit Facility are guaranteed by substantially all of our U.S. subsidiaries and are secured by a first-priority lien on the ABL Collateral. Our obligations under the ABL Credit Facility are also secured by a second-priority lien on the Non-ABL Collateral, which secures the 2014 Notes and our obligations under the Rabobank Term Loan (as defined below) on a first-priority basis.

Availability under the ABL Credit Facility is based on a percentage of certain eligible accounts receivable and eligible inventory and is reduced by certain reserves. After reducing the amount available by outstanding letters of credit issued under the ABL Credit Facility of $188.6 million and a borrowing base adjustment of $139.4 million, the amount available for borrowing, as of January 31, 2010, was $672.0 million, of which, we had no outstanding borrowings.

We incurred approximately $39.9 million in transaction fees which will be amortized into interest expense over the three-year life of the ABL Credit Facility. In the first quarter of fiscal 2010, we recognized a $7.4 million charge related to the write-off of amendment fees and costs associated with the U.S. Credit Facility as a loss on debt extinguishment.

Rabobank Term Loan

In July 2009 (fiscal 2010), we entered into a new $200 million term loan due August 29, 2013 (the Rabobank Term Loan), which replaced our then existing $200 million term loan that was scheduled to mature in August 2011. We are obligated to repay $25 million of the borrowings under the Rabobank Term Loan on each of August 29, 2011 and August 29, 2012. We may elect to prepay the loan at any time, subject to the payment of certain prepayment fees in respect of any voluntary prepayment prior to August 29, 2011 and other customary breakage costs. Outstanding borrowings under this loan will accrue interest at variable rates. Our obligations under the Rabobank Term Loan are guaranteed by substantially all of our U.S. subsidiaries on a senior secured basis. The Rabobank Term Loan is secured by first-priority liens on the Non-ABL Collateral and is secured by second-priority liens on the ABL Collateral, which secures our obligations under the ABL Credit Facility on a first-priority basis. Transaction fees for the Rabobank Term Loan were immaterial.

Convertible Notes

In July 2008 (fiscal 2009), we issued $400.0 million aggregate principal amount of 4% convertible senior notes due June 30, 2013 (the Convertible Notes) in a registered offering. The Convertible Notes are senior unsecured obligations. The Convertible Notes are payable with cash and, at certain times, are convertible into shares of our common stock based on an initial conversion rate, subject to adjustment, of 44.082 shares per $1,000 principal amount of Convertible Notes (which represents an initial conversion price of approximately $22.68 per share). Upon conversion, a holder will receive cash up to the principal amount of the Convertible Notes and shares of our common stock for the remainder, if any, of the conversion obligation.

The Convertible Notes were originally accounted for as a combined debt instrument as the conversion feature did not meet the requirements to be accounted for separately as a derivative financial instrument. In May 2008, the FASB issued new accounting guidance specifying that issuers of convertible debt instruments that may be settled in cash upon conversion (including partial cash settlement) should separately account for the liability and equity components in a manner that will reflect the ent