Maple Leaf Foods Inc. First Quarter 2014 Results Conference Call
Thursday, May 1, 2014 – 2:30 ET

CORPORATE PARTICIPANTS

Mr. Michael McCain
President and Chief Executive Officer

Mr. Michael Vels
Chief Financial Officer

Michael McCain, President and Chief Executive Officer
Thank you, and good afternoon, everyone. Thank you for joining us today. On today's webcast we will discuss Maple Leaf Foods' financial and operating results for the first quarter of 2014. The news release and today's webcast presentation are available at mapleleaf.com under the Investor section.

Some of the statements made on this call may constitute forward-looking information, and future results may differ materially from what we discuss. Please refer to our 2013 MD&A and other information on our website for a broader description of operations and risk factors that could affect the Company's performance.

I will begin today with an operating review, and then turn the call over to Michael Vels, our CFO, to provide other financial information. We'll then open up the phone lines for your questions. I'll begin on page two of the presentation.

In the first quarter, we experienced continued margin compression in our prepared meats business, as raw material prices increased rapidly due to the PED virus and the impact of lower currency. We previously announced pricing for March, catch up on last fall's raw material cost increases and inflation. However, in response to this unprecedented run-up, we and others in the industry have executed rapid adjustments to these increases effective mostly in May, targeted to restore margins. While we've established pricing to recover the margins fully, the second order impacts from these material price increases may cause some very short-term volatility or unpredictability for a few months ahead. We don't, however, expect it to impact our performance into 2015.

Startup phase of transition in our prepared meats business continues, and some key milestones were achieved during the quarter. We've had a successful startup of our wiener line in the new Heritage facility. This enables us to transfer volume out of our legacy wiener plant in Hamilton, Ontario, and in early April we were able to close this facility. Our remaining four legacy facilities are scheduled to close in the fourth quarter.

These achievements were significantly overshadowed by continued high costs tied to the direct overlap of a new and an old supply chain operating side-by-side. In Q1, we also benefited from improved commodity markets compared to the first quarter of last year, specifically in our primary processing and hog production businesses. Although these market factors have improved on a year-over-year basis, I would point out that they are still only neutral against the five-year average. Protein commodity markets continue to be highly volatile due in large part to the PED virus affecting the hog herd in the United States.

Finally, the sale of the bakery business to Grupo Bimbo is on track and expected to close in the second quarter. We've done a lot of work to prepare for the separation of our meat and bakery businesses, and Mike Vels will speak more about this in a moment.

Turning to slide number three, I want to highlight that, as of the first quarter of 2014, the bakery group is being accounted for as a discontinued operation, and therefore adjusted operating earnings, adjusted EPS, and adjusted EBITDA only include the results of the meat products and agri-business groups.

On that basis, adjusted operating earnings for the quarter was a loss of CAD29.9 million compared to a loss of CAD27.9 last year, and adjusted EPS was a loss of CAD0.24 per share in both periods. During the quarter, lower earnings in our prepared meats business, tied directly to the network transition and margin compression, was offset by improved results in our primary pork and hog production operations.

Adjusted EBITDA margin for the quarter was a negative 1.1% compared to a negative 1.4% last year and the trailing 12-month EBITDA margin of negative 1.3%. We still have a long way to go to our 2015 EBITDA margin target of 10%, and I will discuss the building blocks to that target in more detail shortly.

Turning to slide number four, here we provide a detailed breakout of the material factors in the year-over-year change in our adjusted operating earnings, consistent with how we've treated that analysis in the last few quarters. We realized a CAD15 million year-over-year gain from improved protein market conditions. We'll go into more detail on this shortly. Our network transition costs increased by CAD15 million versus a year ago, reflecting a much higher level of activity compared to Q1 last year.

Most of this was connected to the initial startup phase of our largest investment, the Heritage plant in Hamilton, Ontario. In absolute terms, these costs were CAD23 million in the quarter compared to CAD8 million in 2013. Network transition costs include three components - startup costs, incremental resources to support the significant additional work required, and, most significantly, the duplicate of overhead as we ran the four new plants and five legacy plants in parallel.

An increase in fresh and prepared meats volume contributed CAD4 million to earnings, although this is off a very, very low base in the first quarter of last year. Compared to the first quarter of last year, however, we experienced CAD14 million of margin compression in our prepared meat business. This is a reflection of sharply higher raw material and inflationary costs which we were not successful in passing through in pricing in the second half of 2013. This was exacerbated in the first quarter as pork input prices increased significantly from the prior year following a very material run-up in the live hog prices due to the impact of the PED virus on hog production volumes in the United States.

The weakening Canadian dollar also contributed to higher input prices. As I said previously, we have taken significant additional pricing across our portfolio in May to restore margins. Nonrecurring items includes a bucket of a number of smaller nonrecurring items, primarily costs, in the first quarter of 2013.

Turning to slide number five, we realized a CAD15 million year-over-year contribution from improvements in the protein market conditions over the prior year. CAD10 million of this was in the hog production business, driven by higher market prices for hogs and lower grain costs. Primary pork processing markets improved by CAD11 million over the prior year. The third and final element is margins on sales to Japan, which continued to be depressed. At the end of the first quarter, we were able to get substantial pricing in this market., but in the near-term we will just keep abreast of rising meat prices.

Our 2015 EBITDA margin target is based on five-year averages of domestic pork and poultry markets, long-term historical margins in Japanese pork markets, and break-even earnings in hog production. Hog production results were close to break-even in the first quarter, and we expect that this business unit will be profitable for at least the next couple of quarters. I want to highlight that, earlier in the year, we did lock in our profits for this business in forward hedging programs, and, as a result, our hog production business will not experience the full benefit of the recent spike in hog prices.

Pork margins were higher than five-year average in the first quarter of 2014. Therefore, to bridge to our 2015 margin target, we are actually allowing for a decline in primary pork processing margins of CAD5 million to return to the five-year average. As we discussed, margins to Japan are still under-performing. However, with our recent ability to get pricing in the market, we are confident there will be an improvement in this business when the fresh meat prices return to normal. Combining these two offsetting factors, we believe the commodity market impact in assessing the building blocks from the first quarter for a final end-stage run rate is essentially neutral.

Slide six highlights the continued cost pressure of running a parallel manufacturing network through the transition. The intense activity will continue through 2014 as we commission the new Heritage plant and transfer volume out of our subscale facilities by year-end. As I mentioned, we completed the closure of our Hamilton wiener plant on schedule. The remaining four plants are scheduled to close in the fourth quarter. A key goal in our execution planning is to mitigate any impact on our customers by gradually ramping up new plants and ensuring we continue to meet all production requirements through the process. While it's never perfect, we are largely delivering on this commitment through one of the most complex transformations in the North America food industry.

On slide number seven, you can see the steady progression upward of the transition costs as our activity level has increased. Transitional costs of CAD23 million in the quarter were higher than forecast as we incurred additional overhead costs at legacy plants due to extra weeks of production and costs to complete the commissioning at our Winnipeg and Saskatoon expansions that were higher than anticipated. This is in addition to the early startup stages of the Heritage plant.

We do not expect a material decrease in transition costs until Q3, followed by a further substantial decline in the fourth quarter. The triggers for reduction in each of the three buckets of transition costs are as follows - startup costs in 2014 will be primarily incurred at the new Heritage facility over the next two quarters, although the quantum and duration of these types of costs are difficult to precisely quantify. We do not expect that there will be a material reduction in duplicative overhead until the final four legacy plants close in Q4. Closure of the legacy wiener plant in April was an important milestone, but not financial material to the total. Final bucket of transition costs is the dedicated resources that we are deploying to execute the transition, and those will decline as we close plants and complete the transition.

Turning to slide number eight, margin compression in our prepared meats business impacted our results by approximately CAD14 million in the quarter, and this chart shows precisely why. Hog costs spiked 60% in Q1, which caused a 14% increase in pork prices from Q4 last year, including the impact of currency exchange. As we discussed in our last earnings call, we had already planned price increases for early 2014 to catch up on this margin compression.

This unexpected additional rise in the live hog markets due to PED and its associated increases in meat prices have been unprecedented in 50 years in this business. It has required us to pause and reset our pricing on short notice with customers, pricing, all of which will be rolled out across the business in May. We expect that these price increases will be sufficient enough to restore margins and cover higher costs. That said, the short-term and unpredictable risks attached to this action include demand responses from consumers, mix shifts, and unpredictable competitive responses. We are aggressively managing these risks, and we believe they're transitory, but they are real. We are reasonably confident that the entire market will react in similar ways in the first instance because the cost increases are an industry-wide issue.

One of the most important levers you can see on slide number nine is for us to engage consumers and protect volume for new product innovation that brings excitement and variety to the shopping and dining experience. We consciously accelerated the launch of a number of new products to the first half of 2014, supported by extensive in-store promotions. Building excitement without price is important to help consumers over this short-term hurdle of pretty significant inflation.

One of the big success stories has been the Maple Leaf prime brand, which grew 28% between 2011 and 2013, a really tremendous achievement. So, we’re keeping the momentum going in prime by launching several new categories, including frozen chicken strips, nuggets and wings, frozen entrees such as our Thai green curry chicken and turkey with home-style gravy, and finally, extending our fresh line of prime products to include marinated chicken breasts, individually portioned for easy use, as well as premium cuts of fresh pork, including ribs and tenderloins. We're very excited about all these launches, which we're confident will build on the already successful prime brand.

We've mentioned before that protein snacking is a huge marketing opportunity for us. Last year we began testing our first venture into this platform, with fresh, ready-to-eat oven roasted chicken strips paired with dried fruit. We call them Protinis, and we recently launched eight varieties at all major retailers nationwide. We've got a lot of support behind this launch, including Canada's own four-time Olympic gold medalist, Hayley Wickeheiser, and nutritionist Sue Mah. Keep an eye out for our new television campaign as well.

Another one of our platforms for growth is centered around marketing to the increasingly diverse population in Canada. The Mina brand aims to transform the halal food shopping experience at Canadian retailers by offering trusted poultry and meat products. The response has been terrific so far, and we have several initiatives planned to further increase brand awareness, including sponsorship at community events, product sampling, and contests.

The last item I'll mention in our product development side is our Raised Without Antibiotics, or RWA, pork programs, which is rapidly increasing demand from consumers. Maple Leaf is poised to be one of the largest suppliers of RWA pork due to our strong bio-security protocols.

Finally, we're rolling out a brand-new campaign behind the Maple Leaf brand, building on our equity with consumers. Maple Leaf is one of the best-known iconic brands in the country, and our goal is to migrate it from a liked brand to a loved brand. These new ads are airing nationally, supported by a robust digital media program.

As I said in my remarks this morning at our AGM, last year we faced a milestone, topping over one million Facebook fans and over six million video views on YouTube across our brands. We also designed and launched new mobile-friendly recipe platforms.

What I want to reinforce is that there is a lot going on to build our ongoing market share growth as Canada's leading consumer packaged meats company. It's an exciting future that is underpinned by some of the best marketing, product development, and sales talent in this country.

Turning to slide number 10, I'd like to take you through a current state of our network startups. Of all of our expansions, our Brampton plant is furthest along. All volume transfers were completed in the first quarter of 2014, which establishes this plant as the center of excellence of our fresh and frozen sausage production. We will continue to increase our return from this investment through the balance of 2014.

Our Winnipeg bacon and ham plant is the second largest facility in our network. All transfers of ham and bacon volume into this facility are now complete. In addition, we've achieved very significant gains in bacon and ham productivity and yields through the first quarter. Like Brampton, however, there is more upside to come.

Our Saskatoon plant has been the most challenging startup, primarily because of configuring different technologies together for the first time in a single facility. Our team is working through these issues, and we're making some steady improvements.

Our new Heritage plant is the largest in our prepared meats network and is dedicated to two categories, wieners and sliced meats. The ramp-up to date has focused on wiener production and has gone quite well. We are going to begin the commissioning of our sliced meats lines in the second quarter. While this is a more complex part of the commissioning process, we've dedicated significant and highly experienced in-house and third-party resources to achieve our work plan. We have a tight timeline of completing the commissioning by the fourth quarter, which involves transferring production through the remainder of the year from our four legacy plants. The risks would be the same as for any large-scale startup like this.

In the first quarter, we also transferred all of our volume out of the remaining warehouses into our eastern distribution center. This has been another milestone delivered. There are further savings to be realized through optimizing our shipping routes and strategies, including shipping direct to customer warehouses and eliminating VSD, which will be complete by the third quarter.

Turning to slide number 11, as we've discussed in the past, we believe the biggest question on the minds of analysts and our shareholders and other stakeholders is how we bridge the gap from our current performance to our margin target of 10%. We've been providing year-over-year analysis, but we found that it wasn't as helpful to you to understand the bridge to the end state. In fact, it's this bridge that gives us the confidence to feel that, notwithstanding the current financial results, we believe the targets are real and the targets are reasonable within a reasonable timeline.

Let's look at each one of the items in the building blocks on the page of slide 11. Starting at a baseline of negative 1.1%, which was the adjusted EBITDA margin in the first quarter, the largest contributor here is network transition, which represents half of the improvement at 5.5%, or roughly CAD165 million increase in operating earnings on an annualized basis completing that network transition. For those of you that have been modeling this and tracking it carefully, it's important to note this has two components - the elimination of transition costs combined with realizing the remaining benefits from running our business off a streamlined, low-cost manufacturing network. In essence, this is the delta between full-on added cost and contributing benefits from the enormous capital that we've spent.

The second bar is a 3.1 percentage point gain worth roughly CAD93 million on an annualized operating earnings basis from restoring our prepared meats margins to historic levels. As already discussed, we are taking pricing this month, which will restore our prepared meats margins.

The third bar on prepared meats volume, over the last few years we've shed some volume in our prepared meats business because it was either unprofitable or added unnecessary complexity to our plant network. We have concrete plans to recover this, some of which comes from eliminating instability in our network that has resulted from massive change. This represents 1% of the bridge, or a prize of approximately CAD30 million in operating earnings on an annualized basis.

And finally, during the last few quarters of the transition, we've incurred indirect costs in our legacy prepared meats facilities as we execute the transition. These costs are caused by disruptions to our manufacturing and distribution networks as production shifts and people transition to new facilities. We've introduced a significant amount of change to our supply chain in a very short period of time, and this is collateral damage. Although we've made some progress against these items, these costs, again representing 1.1% of our margin expansion worth roughly CAD33 million on an annualized basis, will not be entirely eliminated until the transition is complete. However, by definition, when these legacy plants close, this burden goes away.

Finally, we do have an "other" bucket that captures a variety of other smaller items, but none of them are significant.

We clearly understand the building blocks to our 2015 margin target. There are very specific actions and deliverables and milestones against each one. We believe that the margin restoration will occur largely in the third quarter, and the network transition impact will occur largely in the fourth quarter. Our financial tracking and compensation plans are embedded in ensuring we deliver these things. If we veer from schedule, and there's always risks in a network transition like this, the transition would shift by a quarter, not a year.

With that, I'll turn the call over to Michael Vels.

Michael Vels, Chief Financial Officer
Thanks, Michael. Turning to slide 12, a few comments on the balance sheet. First of all, the net debt at the end of the first quarter was CAD729 million. This looks as if it's increased from CAD452 million at the year-end. There are several factors affecting that increase. Firstly, on an operating basis, we have higher investment in working capital. We also recognized an early repayment premium as a result of the redemption of the Company's notes payable, and the debt was also impacted by investment in fixed assets during the quarter.

I want to point out for this quarter, the balance sheet has de-recognized the cash balances of Canada Bread, as Canada Bread is now reflected as a discontinued operation. And within the assets held for sale in the Canada Bread operations is a cash balance of CAD144 million, which would have been included had it not been accounted for as a discontinued operation.

As I mentioned, on March 14, Maple Leaf gave notice of redemption on CAD706 million of senior notes, which was subsequently repaid in April. As a result, the entire portion of the notes payable was classified as current debt on the March 31, 2013 balance sheet. On redemption of these notes on April 14, the total payment to note holders included CAD98.4 million in respect to settlements for early repayment premiums. We also paid out swap settlement amounts and other financing costs, all which were included in that amount.

As Michael said, the pending sale of the Company's 90% interest in Canada Bread is expected to close on the second quarter. Net cash proceeds to Maple Leaf at that time are expected to be approximately CAD1.65 billion. After closing, the Company will repay and cancel substantially all of its banking facilities with the exception of letter of credit facilities and CAD200 million of its existing bank revolving credit facility.

Moving to slide 13, we invested CAD69 million of capital in the quarter relating to continuing operations compared to CAD67 million last year. And of this amount, CAD58 million comprised strategic capital, primarily construction in our prepared meats network.

In 2014, we're estimating that net capital expenditures will be CAD255 million, including CAD140 million of strategic capital. That full-year estimate, however, includes CAD40 million in respect to the bakery business, the majority of which will not be reflected in the Maple Leaf financial statements, going forward, after sale of Canada Bread. In 2015, we estimate that capital expenditures for the protein business will be approximately CAD80 million, slightly below our historic base capital run rate.

On slide 14, I'd like to make a few comments on restructuring costs. In the first quarter, Maple Leaf reported CAD21.7 million in restructuring costs through the income statement. Approximately CAD16 million of that relates to costs that will be settled in cash in the future, and the remaining in noncash costs, such as accelerated depreciation. The charges for this quarter included CAD11 million of restructuring charges related to the prepared meats network transition, primarily employee retention and severance costs, and accelerated depreciation of facilities that are expected to be closed this year.

And recently, when we announced the bakery sale, we disclosed an estimate at that time of CAD160 million in associated cash expenditures that will arise as a result of this sale. During the quarter, the Company reported CAD10.6 million in restructuring charges primarily in respect of anticipated restructuring that'll be necessary to reduce the size of administrative and overheads to account for the sale of a substantial portion of the consolidated business. These expenses are included in the total estimate of CAD160 million. Further, we anticipate another approximate amount of CAD10 million to CAD15 million of similar restructuring expenses to be recorded in the second quarter. Again, these amounts also included in our initial estimate of CAD160 million in cash costs. We're now well through the complex business of separating the bakery business from the remaining operations in preparation for the closing of the Canada Bread transaction.

In addition to the separation work from bakery, we've also commenced and are at the front end of designing the new structure for Maple Leaf to accommodate the sale of Canada Bread. That will include right-sizing the remaining company to meet our ongoing needs as a focused consumer packaged meats company.

We have identified and will transfer almost 70 people from Maple Leaf to Canada Bread once the sale closes. We're also in the final stages of finalizing a transition services agreement with Grupo Bimbo, largely involving continuation of its information systems support for at least one, and potentially up to two years. Determining the optimal organizational end-state structure included first integrating our corporate and business unit managements into a single leadership team, which was announced in March. This new leadership team is now completing the designs to configure the new Maple Leaf in a manner that will meet our future requirements and establish a low-cost, efficient structure. These decisions will mostly be made by the end of the second quarter and implemented during the second half of 2014.

I'll now turn the call over to Michael for summary remarks.

Michael McCain, President and Chief Executive Officer
Thank you, Mike. Before I turn your attention to the summary of our presentation today, I just wanted to give you a status update on what the use of proceeds will be from the bakery transaction, as I know this is an important question for many of you. As I stated two months ago, the next key steps are to repay our debt, to assess the progress on the prepared meats transformation over the next few quarters, and assess the capital requirements for growth and appropriate capital structure for our residual protein business. While no decisions have been made, the Board certainly intends to be focusing on this issue, and these issues collectively, over the next few months and quarters.

Turning to slide number 15, we are currently experiencing unprecedented market conditions from the PED virus in the United States, and that's always challenging to manage, but I think we're managing it effectively and proactively, taking aggressive pricing action to respond to these rising raw material costs. And at the same time, our network transition is proceeding, but startup risks continue to exist.

The building blocks to our 10% EBITDA margin target are in place. We have great visibility and focus on those building blocks, with specific plans to deliver each one of them. And we're expecting positive trend lines for earnings in the second half of 2014. Alongside these efforts, we're driving our brand, our market leadership, our customer relationships with the most robust innovation and marketing program that we've ever executed in the history of the business.

I can certainly understand why this is a very trying period for investors, but I want to reinforce that we are in the final leg of a very long journey that will dramatically transform our cost structure, our competitiveness, our profitability, and our sustainability.

With that, I'll now turn over the call to your questions.

QUESTION AND ANSWER

Questioner
Hi, good afternoon. I guess a quickly question, hopefully, first on the price increase. So, just to clarify, the price increases that you are implementing in May, you believe that those will fully restore the profit based on the current futures outlook for hogs and pork?

Michael McCain, President and Chief Executive Officer
Yes, I do. I am highly confident that that they will restore the margin rate to our historic expectations and recover the cost of that raw material and currency inflation. I'm highly confident of that. However, it comes with a significant health warning, and it's imperative that you and others understand this health warning. And these are transitional remarks, not long-term structural remarks, but it is a short-term issue.

While we restored the margins in May, or expect to restore them in May, what we don't know and becomes highly unpredictable, is what the demand response will be from those new higher price. What we don't know is whether or not there'll be any mix shift as a result of that higher pricing. And what we don't know is what are the second and third-order marketplace-competitive behaviors to a potential demand shift as a result of that price increase.

Questioner
Right, that's understood. I mean, we've seen that in the past where the volumes get hit, but we've seen them come back, so not too concerned about that. But, I guess just at this stage, are you able to get any visibility as to whether the other private label players and the branded players have also ensued similar price increases in May?

Michael McCain, President and Chief Executive Officer
They did because everybody was affected, it's something of an economic crisis, given the magnitude. You had a 60% increase in the live hog markets, and it was reflected in meat values over a span of less than 60 days. And that's just unprecedented in 50 years. And so, that kind of a crisis was readily understood, readily accepted, and the same economic imperative for everybody in the industry. So, the answer is an unequivocal yes, but I wouldn't discount those risks that I articulate. They're very real.

Questioner
Understood.

Michael McCain, President and Chief Executive Officer
And we have a -- our perspective on that will be press on, and it's important in those types of situations to be steady in the wheel going through that and not to over-react to those second- and third-order impacts. But, it's a complicated marketplace, and with lots of stakeholders. And so, whether it's mix shift or demand response or second-third order competitive response, we have to manage through it. The important point to us is those are factors that affect us through this difficult period that is, according to the futures market -- not us, according to the futures market -- going to kind of normalize in the fall of 2014. We don't see this as a 2015 issue.

Questioner
And would prices typically go down if the futures go down, or do you just -- you have more room for promotional spend and things like that?

Michael McCain, President and Chief Executive Officer
A combination of both. I mean, at the end of the day, undoubtedly they will go down. Undoubtedly they will go down. But, we have -- there's lots of complexity in those costs. Some of it is with us, and when they go down, it won't go down all of which -- for example, the currency component. We priced for the currency component as well, and we also believe that that's going to stick with us today, probably closer to the CAD.90 level than the parity level with that -- a year ago. So, the short answer is yes, but we just have to manage that all very effectively. But, we do believe that we've got the fundamentals in place to restore long-term structural margins.

Questioner
Okay, and last question before I get back in the queue is, if we think back to the first few new lines that you put up -- put into some of your facilities that had trouble, I believe that what you're saying now is a lot of those are now running well and producing result -- much better results. Can you give us one, say, more detailed example of what was one of the major startup issues? I think bacon was one of the issues that were really bad, and how it was resolved, and how long it took?

Michael McCain, President and Chief Executive Officer
Yes, that was -- you went right to a really bad one. It was bad. I mean, I was very proud of how our management team responded to it. I think they handled it extraordinarily well. We've gone from a very slow speed, manual, very archaic, old equipment in our bacon slicing operations and processing operations in the

old world to a very high-speed, state-of-the-art technologically advanced line. And we had a litany of issues that are attached to that startup. Literally, the number of issues in a very complex startup that are measured in the thousands. You resolve them, and you resolve them at one level, and then you ramp up your production to a new level, and then you have a whole new round. It's every time you add a bit of load to the line, you likely get some new issues.

If I had to put them into themes, they were probably two primary themes in that -- or three, I'd say, actually. There was issues around the -- we are using technologies in that case that are new to North America in that particular line, and operating with those technologies at those speeds, with these ultra-high speeds, there was just -- there was a lot of debugging that had to go into the equipment. And so, there was a -- theme number one was just getting the equipment fully debugged operating at those line speeds.

The second theme would be dialing in the process, because the processes for cooking and cooling and equilibrating a belly prior to slicing in a line that is a very slow speed, manual line is very different than the process required to work efficiently on a very high-speed, high technology line, so we had to dial that in for a while. And then, the third component is just training the people on the line that do exist to both operate the equipment but, more importantly, how to respond to the -- rapidly, quickly, effectively to the performance gaps in the line.

So, those are some of the themes, but, I mean, that's the high level. There are thousands of lines that go into that, and I could give you anecdote after anecdote. I would tell you that I think our -- the bacon line itself peaked out -- actually, the Winnipeg peaked out in its worst -- at its worst was week 39 of last year, and the variances to our standards in week 39 were acute. And today, they're down to a nominal number. So, from week 39 last year to today. There's still some things that we need to do in that line to get the last little bit, but it's very manageable today.

So, these things are infinitely resolvable. It's just the -- you're relying on equipment manufacturers and their support systems, and training and debugging these technologies, and debugging technologies at such an advanced line speed, it just takes some time. And it's incredibly unpredictable.

But, that's going -- that's one of the worst ones. One of the better ones, just going along -- the more recent wiener facility in Hamilton actually is at the other end of the spectrum. That's going pretty well, actually. We met our first-stage production targets. It's not without issues. We had lots of issues, but we met our first-stage production targets. It's an incredible facility, incredible processing capacity and efficiency, and the technologies are just nothing short of impressive.

As I say to our people, we've gone from -- in some cases from the Smithsonian to intergalactic manufacturing in one step, and it's incredibly interesting to see. And in that particular facility, it went -- actually in the first stage, it went very, very well. So, the issue is not whether. It's when and timeline. And we've got a very experienced team of people that are working it, and they're working it hard, and they're working around the clock to get it done, and there are just a lot of variables that make the timelines unpredictable.

Questioner
That slide that you had where you do the bridge from EBITDA margin, from Q1 '14 to 2015, what would be the risk to that? It seems very much formality in terms of, like -- I don't want to say it's simple, because obviously it's not, but it seems so clear that it's just from here to there. And again, a quarter off, a quarter one way or the other way is no big deal. I don't think anybody's going to care about that.

But, what type of risk is there to that 10%, I guess is kind of what I'm trying to get at? Because it seems very methodical and doable, but at the same time slides are good, but -- the execution of it?

Michael McCain, President and Chief Executive Officer
Yes. Well, let me take them one at a time. First of all, I can assure you that our management team is not looking at a quarter here or a quarter there and saying it's no big deal. We're looking at every day -- our management team's attitude is every day is a big deal. So, we have a very high sense of urgency throughout the organization. That's not to say that it won't happen, that there isn't risk that could move it a quarter or two one way or the other. But, at the end of the day, our urgency is measured in days, not in quarters. So, we do view it as a big deal.

Let me take it bar by bar. The first one, the 5.5%, there are three things that have to be done in there. The first is getting the new plants to run as planned. The second is moving production, or SKUs, of which there are roughly 400 SKUs that have to move from the old plants to the new ones. And then, the final bar is -- or the final component is closing the old facility. 65% of that bar, 65% of it, is just the overhead connected to closing those old plants. So, it's very much a timeline-based component.

The risks of a particular line getting 95% of the targeted productivity is actually the smallest component of that. It's -- the biggest component of that bar is the duplicative overhead, and 65% of it is eliminating the old overheads from those now-four remaining legacy plants.

So -- but I would say the risk factor attached to that one is predominantly timeline-related. And while we do have a sense -- an urgency measured in days, I would tell you that it -- could it slip by weeks or a month or two, or quarter? It's so unpredictable that the answer is yes, it could do that.

The second bar is margin restoration. And as someone asked earlier, he asked can we do the math to say we've restored our margins in that marketplace, and the answer is yes. I mean, I could tell you with some degree of assurance that that -- that as of May 4, that bar is in place. Having said that, what I can't tell you is what the second order impacts are to that, and the second and third order impacts are demand implications in the short-term, mix shifts in the short-term, and competitive response to either demand or mix shifts in the short-term.

And so, those are the risks attached to that one, but we feel pretty good about it. We're tracking it daily, and there's a high level of urgency across the entire industry, north and south of the border, to recover those margins. And I think we've been all over that one.

Now, the volume progression is one that we've -- it's half -- I wouldn't say half, but it's partially designed in that we've shed volume that we didn't want. It was either unprofitable or it just didn't suit our manufacturing ability. But, on the other hand, we've given up some volume, or some volume softness in the quarter, in the last six months, because of some customer service issues and the like.

Biggest part is volume that we've shed deliberately. But, there are tremendous volume opportunities opening up to us in places like the United States now with the CAD.90 dollar, with covering that volume in the Canadian marketplace post-transition, and some new innovation that we have. So, we're -- we actually feel very comfortable that we can get that piece, and-or more, over the course of the next year, year and a half.

And then the last one, which is 1.1% of the legacy, 1.1 percentage points in the legacy piece, that's an unfortunate component. That's -- as I said in my AGM remarks today, I mean, we are managing through that transition in the best we can, but we're not -- our precision in operating our legacy facilities is not where we would like it to be, or you would like it to be, largely because we're diffusing our managerial talent over two plant networks, not one. And you just don't operate them as well as you should in that market. But, the good news is, is that once we close those legacy facilities, that ineffectiveness goes away. So, that's sort of connected to the first part.

So, it's all reasonable. I said this morning in my remarks at the AGM, I think the -- I feel very comfortable in the end state. I think the risk factors tend to be mostly timelines and dealing with the second order impacts of these price moves. Is that helpful?

Questioner
Yes, that's very helpful. And compensation is directly tied to them hitting these numbers by a certain date?

Michael McCain, President and Chief Executive Officer
Yes. Short answer is they -- yes.

Questioner
Great. I appreciate it.

Questioner
Hey, good afternoon. As you look ahead to 2015 and beyond, can you just talk about the potential for Maple Leaf to expand its export business, either to more countries beyond where you're exporting now, or perhaps with a broader product base, potentially including your Canadian brands?

Michael McCain, President and Chief Executive Officer
I think there's some opportunities today opening up to fill in the gaps in the United States, in contiguous territory or in the United States, particularly in value-added areas. We are doing, I think, a marvelous job at using our advantage particularly in specialty products like Raised Without Antibiotics in the US market. And with the CAD .90 dollar, and now great assets, we have an opportunity to do that.

However, I'd caution you that that's not -- we did not build this capacity in Canada to build enormous excess capacity. This is filling in the gaps on some volume at a few select facilities, and then finding a way to sell that at a high margin into an adjacent territory. We did not make this investment with significant excess goods. In fact, we made it with no additional capacity, for the most part. Across the network, it's designed basically to be hyper-efficient and low cost in servicing the Canadian market.

So, I think the export opportunities beyond the fill-in-the-gaps component of this, which is illustrated in the bridge to 10%, is probably limited. Having said that, we will be looking, as I -- over time, not short-term but, if you look beyond 2015, at some point we will look for footprint expansion outside of Canada because that will be the prudent thing to do. We have very high market shares in this country and limited to 30 million people. So, at some point we'll look to do that, but it would be outside the scope of what we have in front of us now.

Questioner
Okay, thanks. And when you spoke about the use of proceeds, going forward, proceeds from the Canada Bread sale, and you talked about assessing your capital needs for growth, could you just talk a bit more about what that would look like and what kind of areas, or what you would be targeting in terms of growth?

Michael McCain, President and Chief Executive Officer
I can't because we've not formally -- we have ideas, but we've not reviewed all those opportunities with the Board and really vetted them to the degree that they need to be vetted. And so, I'd really rather not speculate on what that outcome is. Suffice to say the themes are basically filling in the gaps in our Canadian portfolio, of which there are many. I alluded to three this morning in my remarks in the AGM. The poultry industry, dry-cured meats, and snacking are three great examples of that.

Number two, driving organic growth in our current portfolio, leveraging our brands. Number three is possibly looking for opportunities some day in the future to expand footprint, but that's -- we'll be very cautious about that and unclear on the timelines. And so, once those capital needs are identified in the business -- and I should point out completing the capital needs for the existing initiatives and transformations which will carry through to the second half of 2014.

So, when you add that all up, the Board will be very deliberate and disciplined and cautious about it all, but when they add it all up, they'll then determine what the appropriate answer is, and approach it with some degree of resolve. So, I'm sure that's not as precise as you'd like at this moment, but it's largely a reflection that the work hasn't been done.

Questioner
No, it's very helpful. Thank you very much.

Questioner
So, thank you. So, the return on invested capital that you're expecting to get from the strategic CapEx, is that mostly in that network transition bar of 5.5%?

Michael Vels, Chief Financial Officer
Yes.

Questioner
Okay. Looking at the volumes, and the hog shortages seems to be out there in many countries because of the PEDv, how are you dealing with it? Are you seeing any -- has the virus hit your farms at all, and do you see any signs yet of farmers looking at expanding supply in Canada, given the higher profits that are coming this year?

Michael McCain, President and Chief Executive Officer
In Canada -- the US industry, by and large, Michael, has not done a great job of containing the virus, which is reflective of the -- its spread throughout the countryside there. There's a wide variation of what the impact will be in the hog herd in the US, a very wide variation, which I think is a reflection of the fact that there's a lot of just unpredictability.

The Canadian market, on the other hand, I think has done a pretty remarkable job to date of protecting itself in bio-security. The Ontario region has had quite a few positive results in PED virus, so maybe that's a little less successful, but certainly still nowhere near the United States. But, Manitoba has only had less than a handful of positive results in a very isolated location, and the operators, including the processors, have an incredibly vigilant bio-security regime in place that's been invested in at some cost, at a very material cost, actually, material to them, anyway, not to our whole company but to them, to help protect its potential spread.

Having said that, the risk is, is that this is a highly virulent virus that, for instance, has -- I've been told by some scientists has the capacity to travel even by air up to 16 kilometers. So, it's quite virulent, and it's a risk factor in front of us. But, to date, it hasn't impacted us.

Questioner
So, where are you seeing volume shortages? I mean, I know you've cut back your prepared meat volumes, but in your primary processing facility, where are you now versus I think the 4.5 million, 4.4 million that you were processing before?

Michael McCain, President and Chief Executive Officer
We're on an annualized basis of about 3.6 million, 3.7 million at Brandon, I think. Including our facility in Lethbridge it is over 4 million.

Questioner
And so, this is impacting, I guess, more of your fresh meat sales?

Michael McCain, President and Chief Executive Officer
No, that's had nothing to do with PED, and it does. It impacts our fresh meat sales, yes. It has nothing to do with PED. That's largely a reflection of the economics of hog processing over the course of the last five years and contraction in the Canadian supply.

Questioner
So, what -- have you seen any signs that farmers in Canada are going to start expanding their herds again?

Michael McCain, President and Chief Executive Officer
No, it's too early to tell, but I suspect we will also see that over the course of the next six months to a year.

Questioner
And do you need it -- that volume to come back to get to that 10%? Because I don't see that anywhere in this chart.

Michael McCain, President and Chief Executive Officer
No, we don't. We do not. Short answer is we don't.

Questioner
Okay. I think that's it. Thank you. Actually, no. Just on the plant closures, are these expected to all come right at the end of Q4, or are they going to be staggered throughout the quarter? How should we expect -- what's your current planning on that, given that it's still far away?

Michael McCain, President and Chief Executive Officer
Of course we plan it through the quarter, but I would model it near the end of the quarter.

Questioner
Thank you.

Michael McCain, President and Chief Executive Officer
Okay. Well, thank you very much. We appreciate everybody's attention here today. This is a long story. It's a long journey. It's been a seven-year journey, and we feel like -- for those of you that have built a house, we feel like we're focused on the move-in date. We still have a lot of work to do. It's a foot race, as you can see from those building blocks, and there's no shortage of obstacles. So, it's been quite an adventure, but we can see the finish line, and we're really focused on it.

We're very excited about what we're doing. We're very excited about the transition for the vision of the business from an integrated food company to a monoline protein business. And we look forward to continue to update you quarter-over-quarter on our progress, and certainly appreciate the support that we've gotten from all of our shareholder and analyst base and their interest in our activities.

So, thank you, and I'll look forward to the next quarter.