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## CQB - Q2 2012 Chiquita Brands International, Inc. Earnings Conference Call

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**OVERVIEW:**

CQB reported 2Q12 GAAP net income of $6m or $0.12 per diluted share.





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## CORPORATE PARTICIPANTS

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**Brian Kocher** *Chiquita Brands International Inc - CFO*

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## PRESENTATION

**Operator**

Good day, and welcome to the Chiquita Brands second-quarter 2012 earnings call. As a reminder, today's conference is being recorded. You'll have the opportunity to ask questions following the presentation.

(Operator Instructions)

At this time, for opening remarks and introductions, I would like to turn the conference over to Mr. Steve Himes, Director of Investor Relations. Please go ahead, sir.

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**Steve Himes** - *Chiquita Brands International Inc - Director, IR*

Thank you, Kevin. Welcome, everyone, to Chiquita Brand International's second-quarter 2012 earnings conference call. On the call today are Fernando Aguirre, Chairman and Chief Executive Officer; and Brian Kocher, Chief Financial Officer. After today's prepared remarks, we will take questions as time allows. A copy of today's press release is available on the Company's website at www.Chiquita.com, and you may also contact Chiquita's Investor Relations department at 980-636-5637 to receive a copy. Our press release includes reconciliations to US GAAP of any non-GAAP financial measures that we mention today. This call contains forward-looking statements regarding operating performance or industry development and any such statements are intended to fall within the Safe Harbor provided under the securities laws. Factors that could cause results to differ materially are described in the Forward-Looking Statements section of today's press release and in Chiquita's SEC filings, including its annual report on Form 10-K and quarterly reports on Form 10-Q. And now, I will turn the call over to Fernando.

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**Fernando Aguirre** - *Chiquita Brands International Inc - Chairman and CEO*

Thank you, Steve, and good afternoon, and thank you for joining us today. We have several items which we would like to cover this afternoon. First, we will review Chiquita's second-quarter performance. Second, formally launch our transformation strategy, which we began laying out on the year-end call in February and is intended to increase shareholder value by singularly focusing on driving profitability in our core businesses of bananas and salads. Third, we will frame the earnings power of Chiquita going forward, quantify our long-term financial goals, and provide additional detail on the actions we are taking to support the achievement of these long-term financial goals. Last, I will also discuss my future plans with the Company. To put this in context, the actions we are announcing today are a series of initiatives which began with the move to Charlotte and the decision to expand our salads business by offering private label salads and will result in a continued restructuring of our current Organization. The move, together with the changes we are announcing, will lower our fixed cost base and are expected to increase Chiquita's profitability in the next six months by reducing expenses and allowing us to focus on our core businesses, bananas and salads. I'm going to ask Brian to take us through our second-quarter results and expand on the plans to improve our profitability short-term. Brian?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Thank you, Fernando. Regarding the second quarter, you will remember that on the last couple of calls, we indicated that 2012 would be a challenging year for Chiquita. Although many of the external factors impacting our Business have not changed, our results reflect improvements and in some instances, even exceed our expectations, particularly with regard to many of the controllable aspects of our Business. The second-quarter 2012 net income on a comparable basis was $12 million, or $0.27 per diluted share, versus $34 million or $0.73 per diluted share in 2011. US GAAP results for Q2 2012 were net income of $6 million, or $0.12 per diluted share, versus net income of $78 million, or $1.68 per diluted share, in 2011. The adjustments between comparable results and GAAP results are included in the table in the press release.

Looking at bananas, sales were 4% lower at $533 million. Comparable operating income was $29 million, or 5.5% of sales, and was impacted by the absence of a product supply surcharge in North America, the weakening euro in European markets, and slightly higher delivered fruit costs. Local pricing gains in Europe partially offset these impacts. Our North American banana business faced difficult comparisons to last year, because of the product supply surcharge that was in effect through the end of the second quarter 2011. Banana pricing was 8% lower on essentially the same unit volume. In Europe, although local prices were 5% higher than in 2011, the increase was not enough to offset the large and rapid decline in the value of the euro. The euro decline alone negatively impacted our year-over-year quarterly comparison by $26 million. In fact, excluding the impact of currency, our European operating income approximately doubled year-over-year.

In our core European market, dollar equivalent prices were 6% lower, and volumes were 5% lower as we rationalized volume in areas where we could not generate a profit. Despite difficult market conditions and some of the variables that we could not control, our banana business's underlying performance exceeded our internal forecast, as we effectively managed the parts of the business that we could control. Without the unprecedented move in the euro, which we just discussed, comparable income in bananas was essentially flat. If not for the 2011 surcharge in North America, comparable income for bananas would have increased year-over-year. Disciplined marketing spends, shipping savings, maximizing utilization of our fixed infrastructure, and the allocation of banana volume to the most efficient markets help drive the underlying business performance.

In our salads and healthy snacks segment, second-quarter net sales were steady at $252 million. On our first quarter call, we indicated that retail salad volume comparisons could be as much as 15% below the second quarter of 2011. Salad volumes were better than expected this quarter, and the quarter ended about 8% below 2011 levels. Increasing sales, retail sales velocity on a same-store basis, the benefits of improved salad quality, and more effective promotion planning strategies led to the velocity increase. Average pricing of retail salads was up slightly from the second quarter of 2011. Increased sales volume in both our foodservice and healthy snacking business offset the revenue effect of lower retail salad volumes. For the quarter, the salad segment delivered $11 million in operating income on a comparable basis versus income of $4 million a year ago. The improved results reflect manufacturing cost improvements, which eliminated certain salad-quality costs incurred in 2011. We also benefited from improved pricing and reduced marketing spend in the salad segment. I want to comment on two important highlights related to the second quarter, which will provide us important flexibility in executing our transformation strategy.

First, in June, you saw the announcement that we successfully received the amendment to our credit agreement. In our current environment, the amendment provides the Company with more operating flexibility to execute its strategy and to manage the volatility inherent in its businesses. The amendment period extends through September of 2013, at which point the terms of the credit agreement largely revert to the original agreement. This support from our lending group highlights their confidence in our Business and their understanding that results from this year uniquely reflect some unprecedented issues, such as the weak euro. Secondly, the relocation of our corporate headquarters and consolidation of our other corporative and administrative functions in Charlotte, North Carolina, is ongoing. We recognized $7 million of costs related to the relocation, $4 million net of tax, in the second quarter 2012, primarily related to severance, and we expect to record an additional $8 million of relocation costs during the second half of 2012. Recall that the cost of the move is essentially offset with the local incentives. Separately, and in addition, Chiquita will realize ongoing operating cost savings of more than $4 million annually from more efficient staffing, consolidation of locations, lower rent, and reduced travel costs.

I would like to provide a little color on the balance of 2012 during which Chiquita will continue to face challenges from some of the headwinds that we've seen in the first half of the year. In our banana business, we continue to expect that supply will outpace demand. The euro will continue to negatively impact Chiquita with comparisons to 2011 in particular. In the third and fourth quarters of 2011, Chiquita realized revenues at levels of $1.41 per euro and $1.40 per euro respectively. These levels are comparison to the spot price today of approximately $1.24 a euro. In June and July, however, we entered into various hedging instruments in order to protect from the downside risk of further devaluation of the euro. Our hedges cover 85% of Chiquita's expected euro cash flow below $1.23 per euro for the balance of 2012. In 2013, our hedges cover 50% of the expected euro cash flow below $1.20 and 35% of the Chiquita's expected euro exposure at a rate below $1.23. Lastly, in terms of our salad business, we expect to see our volumes slightly down in the third quarter and improving in Q4 with the launch of several new items, continued quality improvement, and potential new branded and private label customer contracts that may add to existing volumes. By the end of the year, volumes should be down only slightly to 2011 volumes.

Now, let me turn to laying out how we are looking at the Business over the next few years, starting with specific profit targets. We do not believe the Company's recent performance is indicative of the earnings potential of our business. We are implementing a strategy to enable Chiquita to adapt and compete in the current and future marketplace. For clarity, we are solely focused on increasing shareholder value. Our number one financial goal is to increase cash flow and pay down debt, which in turn, increases shareholder value. While we mentioned earlier in the year that we would at least like to explore alternative uses of cash that may be more accretive than debt reduction, given the current need to adjust our cost structure and change our strategic model, we have decided to focus on increasing cash flow to reduce debt and maximize our asset utilization on our core banana and salads businesses. In other words, we are not looking to acquire any business in the foreseeable future. Given macroeconomic conditions, changes in our own industry, and to quantify the impact of our new strategy, we wanted to take this opportunity to provide our stakeholders with an understanding of Chiquita's earnings potential. To do this, we have today announced long-term operating margin targets for each of our business units.

These operating margins are EBIT margins, earnings before interest and taxes, and exclude certain unallocated corporate costs that are separately disclosed in our corporate segment. While these targets are announced today, and depending upon executing our transformation strategy to drive increased profitability in our core markets, we are focusing on a two to three-year time horizon to achieve these results. In terms of specific targets, for our global banana business, our goal is to average approximately 4% operating income or EBIT margins. While we cannot control the euro, our long-term financial goal is based on a euro at the current $1.24 current euro rate. We believe that a 4% target EBIT margin is achievable by focusing on things that we can control. Additionally, a 4% EBIT margin would rank favorably with our normalized performance over the last four years. To put this in context, on $2 billion of annual banana sales, we are targeting approximately $80 million of operating income in the segment. For salads, we believe we can achieve 7% to 8% operating margins in the next 24 to 36 months. Similarly put, on $1 billion of salad sales, we are targeting $70 million to $80 million of operating income. After subtracting the corporate segment, based on today's revenue and assuming no movement in the euro, that would equate to approximately $110 million of consolidated comparable operating income and approximately $175 million of consolidated EBITDA on an annual basis.

The changes we have outlined will result in sustainable cost reductions beginning immediately of at least $60 million after a one-time charge of approximately $15 million in the second half of 2012, primarily related to severance. The restructuring plan that we're announcing today should -- is in effect immediately and we should start seeing at least $8 million in savings as early as the fourth quarter of 2012, and $60 million on an annualized basis. More than 0.5 of the savings come from streamlining Chiquita's operating and overhead structure, including the elimination of more than 300 positions and related reductions in overhead and newly gained efficiency. Eliminated positions include current vacancies and extend to Senior Management of the Company. We are reducing staff levels, not just to save money, but we are doing so to strategically change our operating model. Again, we must continue to streamline our overhead and operating functions to meet or exceed the ways our competitors operate. We employ many functions and positions, which they do not. Let me now turn it over to Fernando, who will outline some of the strategies we are using to reach these financial targets. Fernando?

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**Fernando Aguirre** - *Chiquita Brands International Inc - Chairman and CEO*

Thank you, Brian. We believe these targets, the targets that Brian has laid out, are aggressive, but achievable. In fact, we've operated this Business with those margins in the recent past. In order to reach these targets, you can expect our Business to make strategic decisions to focus our efforts in increasing profitability in our core bananas and salads business; to drive costs out of our supply chain to be more competitive in our core markets;

to minimize our overhead structure to the bare essentials of supporting our core bananas and salads business; to evaluate non-core unprofitable businesses and minimize investment in diversification and innovation; and to limit our consumer marketing investments to certain European geographies in support of our pricing premium. The entire Management team has participated in the development of these long-range targets and strategic changes, and everybody is committed to executing the strategy and our compensation is directly tied to the future financial success of the Company. To be more specific, here are more details on what is included in this new transformation strategy.

In bananas, we will continue driving costs from all areas of the supply chain. We already have projects identified to further reduce our shipping, our sourcing infrastructure, and direct input costs. We will not invest a significant amount in our banana innovation efforts and will reduce the R&D investments in bananas to the core areas of quality improvement and cost reduction. We will reduce the corporate structure to the appropriate size, in light of the reduced investments noted above. We will reduce our consumer marketing investments to those geographies in Europe where we achieve a price premium. In salads, the most important action that we can undertake is to grow volume. We announced as a first step in our new strategy the decision to offer private label salads and expand into whole head lettuce and organic salads. Higher volume would not only increase revenues, but it will also allow us to maximize the utilization of our plants, which will increase profit margins.

We are also reducing manufacturing costs by using reverse auctions for commodity direct materials; by reducing unprofitable SKUs and eliminating associated overhead; by introducing new salad SKUs in a low-investment R&D model; and by enlarging our available pool of salad growers to promote competition. As you will recall, in June, we broke ground on our new Midwest facility, which will replace three existing facilities in the region. The new facility will provide annual cost savings of at least $7 million, as well as operating flexibility for the salad business. Production will begin in early 2013. While we will maintain trade-oriented marketing programs that have proven to help us to improve shelf velocity, we will reduce our overall marketing investments in consumer messaging. In order to achieve our long-term goals, which we expect to significantly improve profitability and increase shareholder value, we must also change our asset allocation decisions, as well as streamline our costs. In the past, we have invested heavily in diversification, innovation, and new business lines. At this point, we will [de-fair] any diversification efforts outside bananas and salads.

Diversification may be important to us in the long-term, but it will not be the focus over the next two years. Our priority is to eliminate the structural cost disadvantage we have today versus our major competitors. Going forward, we will also ensure our structure is consistently sized to operate competitively. Our plan is to reduce global SG&A levels to no more than 8% of net sales, which is in line with industry benchmarks. To get there, we will simplify our Organization, eliminate jobs in areas dedicated to diversification and reduce additional staff levels by continuing our consolidation efforts to Charlotte. We have made some important strategic and operational decisions towards these goals. These include reducing European headquarters operations to focus support on core businesses; realigning sales and retail operations functions to support profitable value-added customer service; refocusing marketing resources to support only retailer-focused trade marketing; and evaluating non-core, unprofitable business. In short, we plan to limit future investments to areas where customers and consumers see value and pay us a profitable price. It is important to note that the two recent long-term investments in the consolidation of salad facilities in the Midwest and the relocation of the headquarters in Charlotte included major annual savings and financial incentives that are in line with our new strategic model.

We are dedicated to fulfilling commitments made to these projects. These changes are much more than cost savings. They are a fundamental strategic model change. As such, they are designed to maintain high-quality customer service and best-in-class quality products. Importantly, for those Chiquita employees affected by the changes worldwide, we will treat them fairly and consistent with our core values. Their restructuring is expected to be completed by the end of third quarter 2012. To summarize a few points, we are focusing our strategy to drive profitability of our core businesses, bananas and salads. We want to take advantage of economy sub-scale to increase our consolidated cash flows, reduce debt, and create volume for our shareholders. To that end, we are reaffirming debt reduction as the number one priority for any excess cash. We do not believe our current period results are indicative of our long-term earnings power and we set forth long-term financial targets to clarify our belief of the earnings power of our businesses over the next 24 to 36 months. In order to achieve those long-term financial objectives, we have deferred, reduced, or eliminated many of the diversification non-core innovation and consumer marketing investments, reduced the cost and infrastructure in our businesses in both SG&A, as well as cost of goods sold.

We anticipate these efforts will increase consolidated earnings of the business and drive long-term shareholder value. Given this new strategic direction and the completion of the Charlotte relocation, both the Board and I believe that now is the right time to transition the role of Chairman and CEO. The Board has put in place a committee and hired a firm to do an external search. While the search is under way, I will continue in my current capacity and will work with the Board and Management team to ensure a seamless transition. We are following a clear and smooth transition plan and I have great confidence in the team that is in place to execute our turnaround plans. We have accomplished many important things, and while I won't list them all, I'm most proud of how resilient and courageous we have been to sustain many of the headwinds.

Some were inherited and some external factors we cannot control. But as shareholders, you should know that we have always tried to do the right thing to create value in the right manner. At the end of the day, I am one of the largest shareholders in the Company, and as such, I want to get us back to being fairly valued in the market and a smooth transition will help do that. It has been my honor and pleasure to lead Chiquita almost nine years and I look forward to ensuring the next few months we focus on executing our plans and a smooth transition to a new CEO who can help us build and generate shareholder value. I will continue to dedicate my heart and soul and every ounce of energy within me to deliver the results that we all want. This concludes our prepared remarks. Operator, if you can please open the call for questions.

## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions)

Scott Mushkin, Jefferies & Company.

**Scott Mushkin** - *Jefferies & Co. - Analyst*

Hello, guys. Thanks for taking my questions. And I do, Fernando, really appreciate your words and all your hard work. The next two quarters look like they are going to be particularly difficult with the euro where it is and I was just wondering if you can -- maybe, Brian, you could give us a little thought process on is $50 million of EBITDA enough to keep this Company going through the end of the year? Is that even a fair question, I would put out there. Because it seems like that's a possibility here, before we get into next year. And then the second question I have, there seems to be a lot of -- I don't want to say a lot riding, but some riding in the salads business on winning of new contracts to get the volume, and I was wondering if you could tell us what the volume will be if that does not happen.

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Scott, let me answer a couple of those questions, and let's talk a little bit about the go-forward and the next couple of quarters. We do anticipate, as we've said, that 2012 will be a tough year, but we also know that we were able to deliver better than our internal expectations in the second quarter and that the bank amendment, the credit facility amendment, provided us some flexibility and operating room to withstand the challenges that we face and some of the volatility that we face. In addition, subsequent to that, we went ahead and hedged substantially all, 85%, of our euro risk going forward, so we know that -- we don't face any more exposure or relatively little exposure, less than $1.23. So I think as we look over the course of the next couple of months, we're in line, actually a little bit ahead of our estimates and forecasts that we were expecting and certainly that we contemplated in the bank agreement.

Let me also move to the next question you had about salad volumes -- retail salad volumes in particular. And remember a couple of things. We mentioned during the last call that our retail volumes were expected to hit the low point in the second quarter and be down15% year-over-year. Those came in at 8% lower, so we improved our retail salad velocities better than we expected. That came with essentially no new distribution, so that's based on what I'll call the retained business or the incumbent business. And even as we look out in the second half of the year, we anticipate gaining some volume, but I think I mentioned in the first call, even when we were chasing private, and our focus being on private label volume and expanding our retail salads volume, we did not anticipate that making a significant impact to the P&L, at least at that time, 9 to 12 months, now it would be 6 to 9 months. So I hope that, although not giving you specific guidance, I hope it frames some of the questions you may be alluding to.

**Scott Mushkin** - *Jefferies & Co. - Analyst*

Yes, that's perfect. I really appreciate it. And just for clarity, because you guys are going through stuff fast. It's been a long day. And I'm sure it has been for you guys, too. But the hedging, what do you hedge the next two quarters? It's at $1.23. Is it 50%, is that what it is--?

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

85% hedge--

**Scott Mushkin** - *Jefferies & Co. - Analyst*

85%.

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

85% of our euro cash flow is hedged at $1.23. That's what I mean. From a hedging standpoint, we're -- have essentially hedged most of our downside risk below $1.23.

**Scott Mushkin** - *Jefferies & Co. - Analyst*

And the $26 million hit to EBIT that you reference in the second quarter, is that the size we will see in the third and fourth, too? Or is it not -- you don't want to draw that out?

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Well, we gave you what we had last quarter, or in 2011. In the third quarter 2011, we had $1.41 in the fourth quarter. Excuse me, third quarter, we had $1.41. In the fourth quarter, we had $1.40. And if you look at a spot rate right now of $1.24, you can see the difference.

**Scott Mushkin** - *Jefferies & Co. - Analyst*

And in the second quarter of '11, what was it? What was your average during the second quarter of '12? If it's in the release, I apologize.

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

The second quarter of '11 was around $1.44. And our second quarter of '12 was around $1.29.

**Scott Mushkin** - *Jefferies & Co. - Analyst*

So similar, okay. That's really great.

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Similar, yes.

**Scott Mushkin** - *Jefferies & Co. - Analyst*

I'll get back in the queue.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Scott, the thing that I want to take away is, is in spite of the pressure we had from the euro, the underlying business was able to offset a lot of that and ultimately achieve more than we expected. And I think that sometimes gets lost when you talk about the euro impact and particularly in an unhedged environment, the euro impact. I just want to make sure that that comes through clearly.

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**Scott Mushkin** - *Jefferies & Co. - Analyst*

No, I mean, absolutely. And I think that's your work that you did over in Europe and I think a lot of that work is coming through. It's a shame the euro is blowing up. But if you're covered 85%, it does seem to mitigate some of it, but it looks like EBITDA could go negative in the third and fourth quarter and then I'll officially yield. Is that wrong to think it could be negative?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

I don't see it going negative, no.

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**Scott Mushkin** - *Jefferies & Co. - Analyst*

Okay, okay.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

It's not going negative, no.

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**Scott Mushkin** - *Jefferies & Co. - Analyst*

No, okay. That's -- I appreciate that. I'm going to get back in the queue because I actually have a few more, but I'm sure other people are dying to ask questions. Thanks.

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**Operator**

Heather Jones, BB&T Capital Markets.

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**Heather Jones** - *BB&T Capital Markets - Analyst*

A few questions on the cost restructuring. You talk about sourcing and logistic changes in the press release and non-recurrence of quality issues in salads and all. Does the $60 million include the non-recurrence of quality issues in the back half for salads? Or is it--?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

No, that's not -- yes, let me explain that. So one of the reasons that we had better year-over-year performance in the salad segment from '11 to '12 was the result that we had better quality performance. We had better manufacturing procedures and therefore, we had both better sales velocities, as well as lower costs, all right? So put that aside and that's an explanation, part of the explanation, for year-over-year improvement in the salad segment, second quarter of '11, the second quarter of '12. Okay?

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**Heather Jones** - *BB&T Capital Markets - Analyst*

Okay.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

As you look at our cost reduction plan, we will achieve at least $60 million of annualized savings year-over-year. I think the way that I would look at that, is you probably have somewhere in the range of $25 million or so that's SG&A-related, maybe a little -- $25 million to $30 million that's SG&A related, let's call it some programs that might be SG&A related. And that includes people, obviously, in terms of taking out the structure. And then you also -- the rest are what I would describe as more cost of goods sold related items. So remember, we still have [offered] some ships that are coming off of lease. We'd still have some other projects in place to drive cost out of the supply chain, and that's an area that we believe we can become more competitive and we have events that are happening in 2012 or before 2013, like ships coming off charter to help us achieve those savings. So there are events that come up that force us to make a decision and we have the opportunity to make a decision that drives costs out of the supply chain. So I hope that explains the difference between year-over-year performance and then also the cost savings program.

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**Heather Jones** - *BB&T Capital Markets - Analyst*

It does. As far as -- I was shocked that salads were better in Q2 versus Q2 '11, given lower volumes already on depressed base. You mentioned the quality issues, and I know those were called out last year, but I didn't get the sense they were that large. So did you dramatically reduce marketing spend, or what else -- how else were you able to drive that year-on-year improvement, given the lower volumes?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Sure, sure. There are a couple of things that helped us in this picture. Certainly, we had some pricing that helped. We also had a little bit of volume pick-up that came from our foodservice business and our healthy snacking business. Remember, and it was a short phrase in the script, but although we were down in retail salads, we were up in foodservice. And that helps offset some of the volume that we lost in retail, drives manufacturing efficiencies, dilutes overhead, and helps us in that area. And then we did have about $3 million of marketing that was -- $3 million less in 2012 than in 2011. And so those are the real components. It's a little bit of price. Certainly -- the other areas are production overhead. You'll remember last year we took some cost out and we've just been very aggressive in driving savings in our production overhead arena and that helped the salad business in the second quarter as well.

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**Heather Jones** - *BB&T Capital Markets - Analyst*

Okay. Well, let's just segue to a broader question I have. I don't -- may be -- but I'm looking at your volumes in this quarter, and they are down, call it 30% or so since '09. And so I estimate your utilization is probably running around 60%. And so is part of your plan to grow salad volumes, which is part of your long-term plan to achieve 7% to 8% EBIT margins, am I right in thinking that you're breakeven at this lower utilization rate is higher than some of your competitors, and so just trying to get a sense of how you're planning on addressing that.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Yes, I'm not sure that I can comment on what the breakeven of our competitors are. But here's the way that I would look at that, I think, Heather. As we have over the last several years, we've continued to take cost out of our business. And I think I told -- we talked about this even two years ago, where we were more profitable with less capacity and less volume. We were more profitable than we ever have been because of the work that we did on the cost side. We've continued to get some benefit from the cost side and continue to be focused on making our manufacturing environment the most efficient that it can. We do want more volume. When you have plant with some capacity, volume helps drive profits and that's one of the reasons that we elected to offer private label. It's one of the reasons that we want to do whole head lettuce. It's one of the reasons we want to expand organics, because we can do that without any real significant expenditures in plants, in manufacturing, and we might add a line or two here or there, but more or less, we can do that with our existing infrastructure. So yes, we do want to add volume. Yes, adding volume will be on the margin, certainly a profit-accretive effort. But we've done a very good job in driving fixed cost out so that we can have some quarters like this quarter where we actually drove profits even with less volume.

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**Heather Jones** - *BB&T Capital Markets - Analyst*

Okay, and that's good. And the $60 million plan is excellent sounding. I guess one final question, though. And it's related to this whole transition, the restructuring, et cetera. But we've heard some anecdotes here in the US about Chiquita becoming more aggressive bidding for some banana contracts with relatively large retailers. Just wonder if you could speak to that. Is that -- because this is your best market on a global perspective. So I don't know if that's a function of just the internal transition going on or -- if you could speak to that?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Well, I'm not sure that I can speak to any of the rumors you are hearing and what source they are, or anything of that nature. But what I will tell you is we continue to try to drive volume in the right spots where it's profitable for us and we can maximize some of our fixed infrastructure. So we'll continue to -- in certain areas and then we've mentioned before on the call sometimes we're underrepresented in certain geographies and we'll continue to drive profits where they make the most sense for us and volume where we can take the best advantage of our infrastructure.

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**Heather Jones** - *BB&T Capital Markets - Analyst*

Okay, and then my final question is I took from your press release that you are expecting margins in the back half to be up in your salad business. Am I understanding that correctly, as far as up year-on-year in your salad business?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Did you say margins or volumes -- retail volumes?

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**Heather Jones** - *BB&T Capital Markets - Analyst*

I thought -- I can't find it now. No, margins. Let me see -- I can't find it now, but I thought I had read in the second half that -- yes, here it says operating margins should improve year-on-year. So you're expecting higher salad margins in Q3 and Q4?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

We are.

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**Heather Jones** - *BB&T Capital Markets - Analyst*

Year-on-year?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

And that's mostly, again, that's where you get into a lot of the quality-related costs. So if you look at last year, and I think the number last year, we had somewhere in the range of $13 million or $15 million of quality-related costs in 2011. And those were some in the second quarter, but mostly in the third and the fourth quarter of 2011. So all other things being normal, or excuse me, all other things being the same, you would expect us to at least get back that type of profitability.

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**Heather Jones** - *BB&T Capital Markets - Analyst*

Okay, okay. All right. Thank you so much.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Does that make sense?

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**Heather Jones** - *BB&T Capital Markets - Analyst*

It does, it does. Very helpful. Thank you.

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**Operator**

Reza Vahabzadeh, Barclays.

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**Reza Vahabzadeh** - *Barclays Capital - Analyst*

Just on supply and demand for bananas, I don't know if you've addressed this or not, but would you anticipate gradual improvement in the next six months and into 2013? Do you have much visibility in that?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

We disclosed, Reza, that we believe that at least for the balance of the year that supply would outpace demand.

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**Reza Vahabzadeh** - *Barclays Capital - Analyst*

Got it. And is there any -- so even into 2013, you don't think there's going to be any moderation in supply?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

We didn't really disclose any outlook on 2013, but again, you think of all things remaining equal, then we would expect a similar type of supply situation.

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**Reza Vahabzadeh** - *Barclays Capital - Analyst*

All right, and is this supply from Latin America still being up or is it from the African countries?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

We see -- in all -- we see very little impact from ACP countries in our market. Now, from time to time, you'll see some flow up and flow down and that may ripple through, but the majority of the European market is dependent upon the Latin American supply, the dollar bananas.

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**Reza Vahabzadeh** - *Barclays Capital - Analyst*

Got it. And then as far as the salad business is concerned, are you seeing any more rational competition, given your pricing realization, or is it still fairly intense?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

I won't comment on particularly what our competitors are doing and rational or irrational or whatever adjective someone can describe. But again, I think our approach, we've tried to maintain and be very simple. We would like to grow volume. We would like to use the assets and the fixed infrastructure that we have, and we believe we can do so in a value-creating way. And that's how our sales people compete.

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**Reza Vahabzadeh** - *Barclays Capital - Analyst*

Appreciate it, thank you.

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**Operator**

Carla Casella, JPMorgan.

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**Carla Casella** - *JPMorgan Chase & Co. - Analyst*

Hello, one question on just the capital structure. As it relates to both the restructuring and your potential to exit some of your lease fleet capacity, as well as the bonds coming due not too far in the future, what do you think makes sense as an optimal capital structure? Does it make sense to have high yield bonds? Is it something to do with bank debt? Anything else that we're not thinking of?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

We always are evaluating our capital structure. We just went through a period with a very supportive bank group where they helped us on the credit facility amendment and gave us a vote of confidence to do that and when we talked at the end of the first quarter and certainly when we talked with the bank group, we talked about being opportunistic with respect to the Capital Markets. And I think that's the same place we are now. Our number one focus is to increase cash flows, use the excess proceeds to pay down debt, and then at the same time, we'll look to opportunistically enter the Capital Markets when it makes sense for us and could create some value for us.

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**Carla Casella** - *JPMorgan Chase & Co. - Analyst*

Okay, great. And then when you look at the ships, can you give us an update on number of ships that you chartered today and number that you -- if everything is on charter, and how that could change over the next three years as you get to the restructuring. Do you have excess capacity that you can move out of?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Well, here's what I'll tell you about the shipping configuration. Remember a couple of years ago, we sold the ships, captured that balance sheet value, and then paid down debt to do that. And so our portfolio is now 100% in either charter or leases or something of that nature. So some type of in-between, midterm to long-term lease arrangement and charter arrangement. We constantly, and again, last year, we evaluated taking some ships out of the charter pool and replacing those with container vessels, and so we did that and we're able to leverage a cost advantage there. And at least five of our ships will roll off lease at the end of this year. And that's where I would like at least lead the discussion.

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**Carla Casella** - *JPMorgan Chase & Co. - Analyst*

Okay, great. And then just one last question, on the salad business, can you talk of any major wins or losses in the quarter or for the back half, not specific customers if you're not comfortable giving that, but it sounds like you may be moving more towards a focus on foodservice and away from retail. Is there a margin differential between the two, or are you having more wins in foodservice than in retail?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

I would not read into the volume figures any discussion about or belief that we're emphasizing now foodservice over retail. What I would say we're emphasizing is profitable volume. And we like the retail market. We believe we have an advantage over competition in the retail market with respect to things like quality and sales velocity and shrink, and we like the retail grocery market. At the same time, we have been in foodservice for a long, long time and have some very good customers in foodservice. And to the extent we have opportunities to profitably add volume in foodservice, we'll do that as well. But I would not read -- I mentioned some of the volume we had in retail and foodservice, but I would not read into that at all some strategic shift towards foodservice or away from retail, not at all.

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**Carla Casella** - *JPMorgan Chase & Co. - Analyst*

Okay, great. Thank you.

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**Operator**

Bryan Hunt, Wells Fargo Securities.

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**Bryan Hunt** - *Wells Fargo Securities, LLC - Analyst*

Brian, just to understand maybe the opportunity of savings on R&D, as well as marketing, would you happen to have your annual spend on R&D and marketing handy?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

The way I would look at that, Bryan, is that's already included in the $60 million that we gave you.

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**Bryan Hunt** - *Wells Fargo Securities, LLC - Analyst*

Okay.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

That's a component of the at least $60 million we anticipate saving as a result of these changes. And if you remember, I'd described it $25 million of SG&A, people-related costs, some more programs. Maybe that's another $10 million or so, and then cost of goods sold on top of that. So that's the breakout, if it helps you.

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**Bryan Hunt** - *Wells Fargo Securities, LLC - Analyst*

That does. That definitely does. And then, if I look at your current debt level and layer on the $175 million of EBITDA target that you all believe you can get to on a normalized basis, that implies that the Company is roughly 3.4 or 3.5 times leveraged, given today's debt levels. Is that a reasonable capital structure for this business, given the earnings volatility, or do you think -- and you'll obviously generate free cash flow if you get to that level and pay down debt -- but what do you think the target leverage level is for the Business before you can switch gears and think about increasing R&D and diversity and maybe M&A?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Yes, here's what I'll say. We reiterate that our number one priority for excess cash is to pay down debt. Deleveraging helps with a volatile business environment, deleveraging helps with some of the variables that we -- withstanding some of the changes in the variables that we can't exercise direct control over. So make no mistake about it, we're very clear. Utilizing excess cash to pay down debt is our goal and focus. In the past, we've talked about 3 times, net debt at 3 times EBITDA as a target level. I think what you'll see us stick to is we're going to generate, increase our cash flow with all of the excess cash, we'll pay down debt. And then we'll take an opportunity to decide later if we want to go lower than three times.

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**Bryan Hunt** - *Wells Fargo Securities, LLC - Analyst*

Well looking out into next year, do you all believe at this point that you'll contract for fewer bananas than you did this year?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

It's a process we go through every year, where we evaluate sales volume, owned fruit, purchased fruit, and then try to make the best mix of that so that we minimize the excess fruit and we maximize available fruit when we need it and can price it the most. So it's a process that we're going through all the time.

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**Bryan Hunt** - *Wells Fargo Securities, LLC - Analyst*

Is it more of like a Q4 event, then?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Well, typically that's the timing where you start getting into your purchased fruit contracts, your shipping contracts, those types of things, but I will tell you it's not something that we take our eyes off any quarter. We're constantly trying to evaluate our fruit position.

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**Bryan Hunt** - *Wells Fargo Securities, LLC - Analyst*

And then lastly, just to look fundamentally maybe at -- and no one asked the question they usually do. There's parts of the world that are definitely experiencing the droughts that we're experiencing here in North America and my understanding is the availability of fruit in certain markets -- competing fruit that would normally be there on a seasonal basis is unavailable in many markets. How are banana prices performing in a local currency quarter-to-date in parts of the Middle East and in Europe, relative to normal seasonal patterns?

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Well, our -- let me give you the Europe business, because that's certainly more significant to us. We see pricing up on a US dollar basis in the Middle East and the Med, but Europe is more significant to us. And as we look through July, our local currency pricing is up. Let's call it the high single-digits.

**Bryan Hunt** - *Wells Fargo Securities, LLC - Analyst*

Thank you for your time and the depth of the detail. Best of luck.

**Operator**

And we have time for one more question. Mary Gilbert, Imperial Capital.

**Mary Gilbert** - *Imperial Capital - Analyst*

On the question surrounding the salads business and getting into private label, the whole head lettuce, can you give us an idea of the timing? Is this where you're going to have some contracts, major contracts coming up in the fourth quarter, and then also in the first quarter or at the end of the first quarter? So is this really a 2013 benefit that we'll start to see private label, organics, and whole head lettuce flowing in?

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Yes, it's a great question. When we talked about this at the end of the first quarter, we talked about this being meaningful. So some of the customer contracts coming open for renewal and available for bid in the end of the year, first part of the next year, and that in a meaningful basis -- at that time, we thought it would be meaningful in the financial statements in 9 to 12 months and we're 3 months later, so now that's 6 to 9 months before we see a meaningful impact.

**Mary Gilbert** - *Imperial Capital - Analyst*

Got it, yes. So it's really not going to impact 2012 is the bottom line, right?

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Now, look, let me -- we have not, we have not projected and set expectation that there's a meaningful impact in 2012. I will tell you that every day we send our sales people out hitting the streets to go find profitable, meaningful volume.

**Mary Gilbert** - *Imperial Capital - Analyst*

Okay. Okay. That's helpful. All right. Okay. I think -- how should we look at working capital year-over-year, with a lot of the initiatives that we're looking at for this year and also I'm assuming for next year we'll see some increases. How should we look at that?

**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Well, I would look at -- I think so far this year, we're about right around free cash flow breakeven. And more or less, that's our expectation for the balance of the year. As we improve operations, free cash flow goes up and as we improve operations, I think we've got an opportunity to continue driving working capital efficiencies. But I would look at it and right now we're about free cash flow breakeven through the second quarter -- for the second quarter, as well as year to date through June.

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**Mary Gilbert** - *Imperial Capital - Analyst*

Okay. The other thing -- this is just a housekeeping item, but wanted to find out what your stock comp expense was in the quarter. And I'm assuming that the ship amortization is the same as it was a year ago in the quarter and year-to-date?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

When you say ship amortization, you mean amortization--?

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**Mary Gilbert** - *Imperial Capital - Analyst*

The gain.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

-- of the deferred gain, right?

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**Mary Gilbert** - *Imperial Capital - Analyst*

Correct.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Yes, that's right. It's about the same. And stock option compensation is--

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**Mary Gilbert** - *Imperial Capital - Analyst*

Yes.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Right around $2 million or so.

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**Mary Gilbert** - *Imperial Capital - Analyst*

$2 million for the quarter?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

For the quarter.

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**Mary Gilbert** - *Imperial Capital - Analyst*

Okay, perfect. Okay, great. Is there any cash restructuring costs that flowed through year-to-date?

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

There is. We've disclosed -- and I encourage you to look through the earnings release as well. We disclosed the charges we have for the relocation to Charlotte. We've got certainly some non-cash charges for some exit activities, but all of that is detailed in our reconciliation from comparable to US GAAP figures in the press release.

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**Mary Gilbert** - *Imperial Capital - Analyst*

Okay, yes. I saw the total charge that flowed through the income statement, but just wondered if there was a difference in terms of the cash component.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

Yes--

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**Mary Gilbert** - *Imperial Capital - Analyst*

I think it was $7 million.

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**Brian Kocher** - *Chiquita Brands International Inc - CFO*

There are some timing differences, of course, but I wouldn't say it's meaningful to think of it in terms of huge swings.

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**Mary Gilbert** - *Imperial Capital - Analyst*

Okay, great. That's helpful. Thank you.

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**Operator**

And ladies and gentlemen, that does conclude our question-and-answer session. I would now like to turn the call back over to Fernando Aguirre for any additional or closing remarks.

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**Fernando Aguirre** - *Chiquita Brands International Inc - Chairman and CEO*

Thank you. And thank you very much for your questions today, and thank you all to our shareholders for the support you've given us over the years and we certainly are looking forward to continuing to rebound the Company's results. Thank you very much.

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**Operator**

And ladies and gentlemen, once again, that does conclude today's call. We do appreciate everyone's participation.

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