

Hillshire Brands Company (HSH-\$35.78-NYSE)

Alternatives to a Pinnacle Acquisition

Year 6/30 :	EPS	P/E	PMV	Dividend: \$0.70	Current Return: 2.0%
2016P	\$2.15	16.6x	\$53	Shares O/S: 122.6 million	52-Week Range: \$38.01 – \$30.35
2015P	1.95	18.4	48		
2014E	1.75	20.6	45		
2013A	1.72	20.8	---		

COMPANY OVERVIEW

Hillshire Brands Company headquartered in Chicago, Illinois was renamed from the Sara Lee Corporation following the tax-free spin-off to shareholders on June 28, 2012 of the international coffee and tea company, D.E MASTER BLENTERS 1753. Hillshire generates over \$4 billion in annual revenue of which nearly 90% is generated from meat-based products under leading brands, such as *Jimmy Dean*, *Hillshire Farms*, *Ballpark*, *Aidells* and *Gallo*.

On May 12, 2014 Hillshire announced an agreement to acquire Pinnacle Foods (PF-NYSE) for nearly \$6.8 billion or \$18 per share in cash and one-half Hillshire share for each Pinnacle share owned. As a result, the combined company is expected to generate approximately \$6.9 billion in revenue, \$1.1 billion of EBITDA and earnings of \$2.00 per share in fiscal 2015, accretive to our current estimate of \$1.95. Alternatively, there may be other options for Hillshire to consider in order to unlock shareholder value, including a sale of the company to a strategic buyer. Protein suppliers, such as JBS SA (JBSS3-BR), Hormel (HRL-NYSE) or Tyson (TSN-NYSE) may be interested in Hillshire's strong brands and the higher, more consistent profitability of the packaged food business.

JBS SA, the Brazilian protein company may still be interested. On May 20, JBS SA issued a press release stating it requested registration of primary and secondary common shares for a public offering of its subsidiary, JBS Foods, which includes the JBS poultry business in Brazil and Seara, which was acquired in September 2013. The segment has annualized revenue of approximately BRL 11 billion (\$5.0 billion) and EBITDA of between BRL 1.2-1.5 billion (\$540-685 million) based on management's previous guidance and 1Q results. Assuming a 10x multiple on the division similar to BRF Brasil Foods (BRFS3-BR), no debt and the sale of nearly half of its stake, JBS SA may raise nearly \$2.7-3.4 billion. At the end of the first quarter, JBS SA leverage ratio was estimated at 3.3x, which would consequently be reduced to approximately 2.5x following the offering.

Hillshire competes today in mostly meat-centric categories, such as breakfast and smoked sausages, frozen breakfast meals, hot dogs and lunchmeat with retail sales totaling \$13.8 billion. The company is increasing innovation and has recently announced the expansion of several of its brands into adjacent categories, including frozen dinners/entrées, a category worth an additional \$9 billion in retail sales. This fits the strategy that JBS has laid out previously for its US pork business, which includes expanding its value-added products, case ready products and improving its converted product volume and margin. As recently as September 2013, in a *Bloomberg Business Week* article when asked about possibly acquiring Hillshire, CEO Wesley Mendonça Battista commented, "Maybe at the right time, at the right price." Hillshire shares remain a Buy; valuation is attractive as Hillshire shares trade at 9.5x June 2015 projected EBITDA and 18.4x earnings. We calculate a PMV of \$47 based on 2015 estimates, a 24% discount to the current market price, not including the acquisition of Pinnacle Foods and including a break-up fee of \$163 million (or \$1.33 per share).

Table 1

Hillshire Brands Company Earnings Model

	2012 - 2018P							
Fiscal year end 6/30	2012	2013	2014E	2015P	2016P	2017P	2018P	CAGR
(\$ in millions, except per share)								'13-'18P
Revenue	\$ 3,958	\$ 3,920	\$ 4,003	\$ 4,234	\$ 4,386	\$ 4,561	\$ 4,745	3.9 %
% Growth	-1.5%	-1.0%	2.1%	5.8%	3.6%	4.0%	4.0%	
EBITDA	501	498	513	543	577	606	637	5.0
Margin	12.7%	12.7%	12.8%	12.8%	13.1%	13.3%	13.4%	
EPS, cont ops		\$ 1.72	\$ 1.75	\$ 1.95	\$ 2.15	\$ 2.35	\$ 2.55	8.2
% Growth			0.5%	11.9%	11.1%	9.0%	8.8%	
TEV/EBITDA Multiple		10.0x	9.7x	9.5x	8.9x	8.5x	8.1x	
P/E Multiple		20.8	20.6	18.4	16.6	15.2	14.0	
CapEx		139	130	133	137	141	145	

Source: Company data and Gabelli & Company estimates.

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Table 2

Hillshire Brands Company
Private Market Value Analysis
2012 - 2018P

Fiscal year ends 6/30
(\$ in millions, except per share)

Retail

	2012	2013	2014E	2015P	2016P	2017P	2018P
Hillshire Farm (estimated)	\$ 1,055	\$ 1,023	\$ 1,034	\$ 1,085	\$ 1,129	\$ 1,174	\$ 1,221
Jimmy Dean	971	1,029	1,049	1,112	1,168	1,226	1,288
Ball Park	406	410	418	433	448	464	480
State Fair	142	131	131	134	137	141	144
Aidells	102	111	121	130	140	151	163
Sara Lee	60	55	56	58	59	60	62
Gallo	30	32	34	36	37	39	40
Sara Lee Bakery	118	104	111	177	187	195	204
Revenue	2,884	2,894	2,954	3,165	3,304	3,449	3,601
EBITDA	402	417	422	460	498	530	563
Valuation Multiple	12.0x	12.0x	12.0x	12.0x	12.0x	12.0x	12.0x
Segment Value	\$ 4,824	\$ 5,004	\$ 5,060	\$ 5,521	\$ 5,981	\$ 6,355	\$ 6,756

Foodservice/Other

Bakery (estimated)	\$ 382	\$ 343	\$ 340	\$ 348	\$ 357	\$ 366	\$ 375
Meat	698	683	710	721	725	746	769
Revenue	1,080	1,026	1,050	1,069	1,081	1,112	1,144
EBITDA	116	99	112	124	121	121	121
Valuation Multiple	10.0x	10.0x	10.0x	10.0x	10.0x	10.0x	10.0x
Segment Value	\$ 1,160	\$ 990	\$ 1,116	\$ 1,240	\$ 1,213	\$ 1,211	\$ 1,209

Australian Bakery

Segment Value	\$ 85	\$ 85					
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Corporate

	(21)	(18)	(20)	(41)	(43)	(45)	(47)
Total Private Market Value	6,069	6,079	6,175	6,761	7,194	7,566	7,965
Less: Net Debt	(699)	(551)	(538)	(750)	(686)	(672)	(690)
Less: Options Payments (a)	(79)	(116)	(83)	(97)	(120)	(135)	(151)
Equity Private Market Value	5,291	5,412	5,555	5,913	6,387	6,758	7,125
Shares Outstanding	120.6	123.2	123.8	122.3	120.8	119.3	117.8
PMV per share	\$ 44	\$ 44	\$ 45	\$ 48	\$ 53	\$ 57	\$ 60
Current Market - Discount to PMV	18.4%	18.5%	20.2%	26.0%	32.3%	36.8%	40.8%

(a) After-tax payments to buy out options holders at Private Market Value.

Source: Company data and Gabelli & Company estimates.

Other Companies Mentioned:

BRF SA	(BRFS3-BR)
Hormel Foods Corporation	(HRL-NYSE)
JBS SA	(JBSS3-BR)
Pinnacle Foods Inc.	(PF - NYSE)
Tyson Foods, Inc.	(TSN-NYSE)

I, **Sarah Donnelly**, the Research Analyst who prepared this report, hereby certify that the views expressed in this report accurately reflect the analyst's personal views about the subject companies and their securities. The Research Analyst has not been, is not and will not be receiving direct or indirect compensation for expressing the specific recommendation or view in this report.

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Important Disclosures

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A **Buy** rated stock is one that in our view is trading at a meaningful discount to our estimated PMV. We could expect a more modest private market value to increase at an accelerated pace, the discount of the public stock price to PMV to narrow through the emergence of a catalyst, or some combination of the two to occur.

A **Hold** is a stock that may be trading at or near our estimated private market value. We may not anticipate a large increase in the PMV, or see some other factors at work.

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