SANDERSON FARMS INC
Form 10-K
December 21, 2007

**Table of Contents**

**UNITED STATES**
**SECURITIES AND EXCHANGE COMMISSION**
**Washington, D.C. 20549**
**FORM 10-K**
(Mark One)

þ **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended October 31, 2007**

o **Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from __________ to __________**

**Commission file number: 1-14977**

**SANDERSON FARMS, INC.**
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Mississippi<br>(State or other jurisdiction of<br>incorporation or organization) | 64-0615843<br>(IRS Employer<br>Identification No.) |
| 127 Flynt Road<br>Laurel, Mississippi<br>(Address of principal executive offices) | 39443<br>(Zip Code) |

Registrant s telephone number, including area code: (601) 649-4030

Securities registered pursuant to Section 12(b) of the Act:

| Title of each Class: | Name of exchange on which registered: |
|---|---|
| Common stock, $1.00 par value per share | The NASDAQ Stock Market LLC |

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

o Yes þ No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

o Yes þ No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

þ Yes o No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K o.

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

o Yes þ No

Aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant computed by reference to the closing sales price of the common equity in The NASDAQ Stock Market on the last business day of the Registrant s most recently completed second fiscal quarter: $677,129,214.

Number of shares outstanding of the Registrant s common stock as of December 20, 2007: 20,239,111 shares of common stock, $1.00 per share par value.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s definitive proxy statement filed or to be filed in connection with its 2008 Annual Meeting of Stockholders are incorporated by reference into Part III.

**TABLE OF CONTENTS**

## INTRODUCTORY NOTE

**Definitions.** This Annual Report on Form 10-K is filed by Sanderson Farms, Inc., a Mississippi corporation. Except where the context indicates otherwise, the terms Registrant, Company, Sanderson Farms, we, us, or our to Sanderson Farms, Inc. and its subsidiaries and predecessor organizations. The use of these terms to refer to Sanderson Farms, Inc. and its subsidiaries collectively does not suggest that Sanderson Farms has abandoned their separate identities or the legal protections given to them as separate legal entities. Fiscal year means the fiscal year ended October 31, 2007, which is the year for which this Annual Report is filed.

**Presentation and Dates of Information.** Except for Item 4A herein, the Item numbers and letters appearing in this Annual Report correspond with those used in Securities and Exchange Commission Form 10-K (and, to the extent that it is incorporated into Form 10-K, the letters used in the Commission s Regulation S-K) as effective on the date hereof, which specifies the information required to be included in Annual Reports to the Commission. Item 4A ( Executive Officers of the Registrant ) has been included by the Registrant in accordance with General Instruction G(3) of Form 10-K and Instruction 3 of Item 401(b) of Regulation S-K. The information contained in this Annual Report is, unless indicated to be given as of a specified date or for the specified period, given as of the date of this Report, which is December 21, 2007.

## PART I

### Item 1. Business

### (a) GENERAL DEVELOPMENT OF THE REGISTRANT S BUSINESS

The Registrant was incorporated in Mississippi in 1955, and is a fully-integrated poultry processing company engaged in the production, processing, marketing and distribution of fresh and frozen chicken products. In addition, the Registrant is engaged in the processing, marketing and distribution of processed and prepared food items through its wholly-owned subsidiary, Sanderson Farms, Inc. (Foods Division).

The Registrant sells ice pack, chill pack and frozen chicken, in whole, cut-up and boneless form, primarily under the Sanderson Farms® brand name to retailers, distributors, and casual dining operators principally in the southeastern, southwestern and western United States. During its fiscal year ended October 31, 2007 the Registrant processed 343.6 million chickens, or approximately 2.0 billion dressed pounds. According to 2007 industry statistics, the Registrant was the 4th largest processor of dressed chickens in the United States based on estimated average weekly processing.

The Registrant s chicken operations presently encompass 7 hatcheries, 6 feed mills and 8 processing plants. The Registrant has contracts with operators of approximately 528 grow-out farms that provide it with sufficient housing capacity for its current operations. The Registrant also has contracts with operators of 173 breeder farms.

Through its Foods Division subsidiary, the Registrant sells over 100 processed and prepared food items nationally and regionally, primarily to distributors, national food service accounts and retailers. These food items include further processed chicken products and frozen entrees, such as chicken and dumplings, lasagna, seafood gumbo, shrimp creole and other specialty products.

Since the Registrant completed the initial public offering of its common stock in May 1987, the Registrant has significantly expanded its operations to increase production capacity, product lines and marketing flexibility. Through 1995, this expansion included the expansion of the Registrant s Hammond, Louisiana processing facility, the construction of new waste water facilities at the Hammond, Louisiana and Collins and Hazlehurst, Mississippi processing facilities, the addition of second shifts at the Hammond, Louisiana, Laurel, Hazlehurst, and Collins, Mississippi processing facilities, expansion of freezer and production capacity at its prepared foods facility in Jackson, Mississippi, the expansion of freezer capacity at its Laurel, Mississippi, Hammond, Louisiana and Collins, Mississippi processing facilities, the addition of deboning capabilities at all of the Registrant s poultry processing facilities, and the construction and start-up of its Pike County (McComb), Mississippi production and processing

Table of Contents

facilities, including a hatchery, a feed mill, a processing plant, a waste water treatment facility and a water treatment facility. In addition, since 1987, the Registrant completed the expansion and renovation of the hatchery at its Hazlehurst, Mississippi production facilities.

In 1997, the Registrant began initial operations at a new poultry processing complex in Brazos County, Texas. The complex consists of a feed mill, hatchery, processing plant and wastewater treatment facility. This plant operates at full capacity of 1.25 million head of chicken per week.

In the fourth quarter of fiscal 2005, the Registrant began initial operations at a new poultry processing complex in southern Georgia. The complex consists of a feed mill, hatchery, processing plant and wastewater treatment facility. This plant reached its full capacity of 1.25 million head of chicken per week during October 2006.

During fiscal 2006, the Company announced the construction of a new poultry complex in Waco, Texas. The completed complex consists of an expansion of the feedmill in Robertson County, Texas, hatchery, processing plant and wastewater treatment facility, and will process 1.25 million head per week at full capacity. Operations at the new Waco, Texas complex began during August 2007 and will reach full capacity during the summer of 2008.

Since 1997, the Company has also changed its marketing strategy to move away from the small bird markets serving primarily the fast food markets and into the retail and big bird deboning markets serving the retail and food service industries. This market shift has resulted in larger average bird weights of the chickens processed by the Company, and has substantially increased the number of pounds processed by the Company. In addition, the Registrant continually evaluates internal and external expansion opportunities to continue its growth in poultry and/or related food products.

Capital expenditures for fiscal 2007 were funded by working capital and borrowings under the Registrant s revolving credit agreement. Effective April 27, 2007, the Registrant amended its revolving credit facility to, among other things, change the covenant requiring a minimum debt to total capitalization ratio of 55% during fiscal 2008 and 2009, increase the available credit to $225.0 million and extend the expiration date until April 1, 2012. As of October 31, 2007, the Company was in compliance with all covenants and had $180.0 million available to borrow under the revolving credit facility. The Registrant anticipates that capital expenditures for fiscal 2008 will be funded by internally generated working capital and, if needed, borrowings under the revolving credit agreement.

**(b) FINANCIAL INFORMATION ABOUT INDUSTRY SEGMENTS**

Not applicable.

**(c) NARRATIVE DESCRIPTION OF REGISTRANT S BUSINESS**

**General**

The Registrant is engaged in the production, processing, marketing and distribution of fresh and frozen chicken and the preparation, processing, marketing and distribution of processed and prepared food items.

The Registrant sells chill pack, ice pack and frozen chicken, both whole and cut-up, primarily under the Sanderson Farms® brand name to retailers, distributors and casual dining operators principally in the southeastern, southwestern and western United States. During its fiscal year ended October 31, 2007, the Registrant processed approximately 343.6 million chickens, or approximately 2.0 billion dressed pounds. In addition, the Registrant purchased and further processed 9.1 million pounds of poultry products during fiscal 2007. According to 2007 industry statistics, the Registrant was the 4th largest processor of dressed chicken in the United States based on estimated average weekly processing.

The Registrant conducts its chicken operations through Sanderson Farms, Inc. (Production Division) and Sanderson Farms, Inc. (Processing Division), both of which are wholly-owned subsidiaries of Sanderson Farms, Inc.

Table of Contents

The production subsidiary, Sanderson Farms, Inc. (Production Division), which has facilities in Laurel, Collins, Hazlehurst and Pike County, Mississippi, Bryan, Waco, and Robertson County, Texas and Adel, Georgia, is engaged in the production of chickens to the broiler stage. Sanderson Farms, Inc. (Processing Division), which has facilities in Laurel, Collins, Hazlehurst and Pike County, Mississippi, Hammond, Louisiana, Bryan and Waco, Texas and Moultrie, Georgia, is engaged in the processing, sale and distribution of chickens.

The Registrant conducts its processed and prepared foods business through its wholly-owned subsidiary, Sanderson Farms, Inc. (Foods Division), which has a facility in Jackson, Mississippi. The Foods Division is engaged in the processing, marketing and distribution of over 100 processed and prepared food items, which it sells nationally and regionally, principally to distributors, national food service accounts and retailers.

**Products**

The Registrant has the ability to produce a wide range of processed chicken products and processed and prepared food items that allow it to take advantage of marketing opportunities as they arise.

Processed chicken is first saleable as an ice packed whole chicken. The Registrant adds value to its ice packed whole chickens by removing the giblets, weighing, packaging and labeling the product to specific customer requirements and cutting the product based on customer specifications. The additional processing steps of giblet removal, close tolerance weighing and cutting increase the value of the product to the customer over whole ice packed chickens by reducing customer handling and cutting labor and capital costs, reducing the shrinkage associated with cutting, and ensuring consistently sized portions.

The Registrant adds additional value to the processed chicken by deep chilling and packaging whole chickens in bags or combinations of fresh chicken parts in various sized individual trays under the Registrant s brand name, which then may be weighed and pre-priced, based on each customer s needs. This chill pack process increases the value of the product by extending shelf life, reducing customer weighing and packaging labor, and providing the customer with a wide variety of products with uniform, well designed packaging, all of which enhance the customer s ability to merchandise chicken products.

To satisfy some customers merchandising needs, the Registrant freezes the chicken product, which adds value by meeting the customers handling, storage, distribution and marketing needs and by permitting shipment of product overseas where transportation time may be as long as 25 days.

Value added products usually generate higher sale prices per pound, exhibit less finished price volatility and generally result in higher and more consistent profit margins over the long-term than non-value added product forms. Selling fresh chickens as a prepackaged brand name product has been a significant step in the development of the value added, higher margin consumer business.

The following table sets forth, for the periods indicated, the contribution, as a percentage of sales of chicken products, of value added and non-value added chicken products.

| | Fiscal Year Ended October 31, | | | | |
|---|---|---|---|---|---|
| | **2003** | **2004** | **2005** | **2006** | **2007** |
| Value added | 99.5% | 99.6% | 99.5% | 99.7% | 99.7% |
| Non-value added | .5 | .4 | .5 | .3 | .3 |
| Total Registrant chicken sales | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

Table of Contents

The following table sets forth, for the periods indicated, the contribution, as a percentage of net sales dollars, of each of the Registrant s major product lines.

| | Fiscal Year Ended October 31, | | | | |
|---|---|---|---|---|---|
| | **2003** | **2004** | **2005** | **2006** | **2007** |
| Registrant processed chicken: | | | | | |
| Value added: | | | | | |
| Chill pack | 34.4% | 32.5% | 33.6% | 31.0% | 28.5% |
| Fresh bulk pack | 42.5 | 47.5 | 44.4 | 45.1 | 44.3 |
| Frozen | 10.3 | 10.0 | 12.4 | 14.1 | 17.2 |
| Subtotal | 87.2 | 90.0 | 90.4 | 90.2 | 90.0 |
| Non-value added: | | | | | |
| Ice pack | .3 | .3 | .3 | .3 | .3 |
| Frozen | .1 | .1 | .1 | .0 | .0 |
| Subtotal | .4 | .4 | .4 | .3 | .3 |
| Total Company processed chicken | 87.6 | 90.4 | 90.8 | 90.5 | 90.3 |
| Processed and prepared foods | 12.4 | 9.6 | 9.2 | 9.5 | 9.7 |
| Total | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

**Market Segments and Pricing**

The three largest market segments in the chicken industry are big bird deboning, chill pack and small birds.

The following table sets forth, for each of the Company s poultry processing plants, the general market segment in which the plant participates, the weekly capacity of each plant at full capacity expressed in number of head processed, and the average industry size of birds processed in the relevant market segment.

| **Plant Location** | **Market Segment** | **Capacity Per Week*** | **Industry Bird Size** |
|---|---|---|---|
| Laurel, Mississippi | Big Bird Deboning | 625,000 | 7.45 |
| Hazlehurst, Mississippi | Big Bird Deboning | 625,000 | 7.45 |
| Hammond, Louisiana | Big Bird Deboning | 625,000 | 7.45 |
| McComb, Mississippi | Chill Pack Retail | 1,250,000 | 5.60 |
| Bryan, Texas | Chill Pack Retail | 1,250,000 | 5.60 |
| Collins, Mississippi | Big Bird Deboning | 1,250,000 | 7.45 |
| Moultrie, Georgia | Chill Pack Retail | 1,250,000 | 5.60 |
| Waco, Texas | Big Bird Deboning | 1,250,000 | 7.45 |

* At full capacity.

Those plants that target the big bird deboning market grow a relatively large bird. The dark meat from these birds is sold primarily as frozen leg quarters in the export market or as fresh whole legs to further processors. This dark meat is sold primarily at spot commodity prices, which prices exhibit fluctuations typical of commodity markets. The white meat produced by these plants is generally sold as fresh deboned breast meat and whole or cut wings, and is likewise sold at spot commodity market prices for wings and boneless breast meat. The Company as of October 31, 2007 processes 3.45 million head per week in its big bird deboning plants (the Waco, Texas plant, which began operations in August 2007, was not yet operating at full capacity), and its results are materially impacted by fluctuations in the commodity market prices for leg quarters, boneless breast meat and wings.

Table of Contents

The Urner Barry spot market price for leg quarters, boneless breast meat and whole wings for the past five calendar years is set forth below:

Those plants that target the chill pack retail market grow a medium sized bird and cut and package the product in various sized individual trays to customers specifications. The trays are weighed and pre-priced primarily for customers to resell through retail outlets. While the Company sells some of its chill pack product under store brand names, most of its chill pack production is sold under the Company s Sanderson Farms® brand name. While the Company has long term contracts (one to four years) with most of its chill pack customers, the pricing of this product is based on a formula that uses the Georgia Dock whole bird price as its base. The Georgia Dock whole bird price is issued each week by the Georgia Department of Agriculture and is based on its survey of prices during the preceding week. The Company as of October 31, 2007 has 3.75 million head per week dedicated to the chill pack market, and its results are materially impacted by fluctuations in the Georgia Dock price.

The Georgia Dock price for whole birds as issued by the Georgia Department of Agriculture for the last five calendar years is set forth below:

Those companies with plants dedicated to the small bird market grow and process a relatively small chicken and market the finished product primarily to fast food and food service companies at negotiated flat prices, cost plus formulas or spot market prices. Based on bench marking services used by the industry, this market segment has been the least profitable of the three primary market segments over the last ten years. The Company has no product dedicated to the small bird market.

**Sales and Marketing**

The Registrant s chicken products are sold primarily to retailers (including national and regional supermarket chains and local supermarkets) and distributors located principally in the southeastern, southwestern and western United States. The Registrant also sells its chicken products to casual dining operators and to customers who resell the products outside of the continental United States. This wide range of customers, together with the Registrant s product mix, provides the Registrant with flexibility in responding to changing market conditions in its effort to maximize profits. This flexibility also assists the Registrant in its efforts to reduce its exposure to market volatility.

Sales and distribution of the Registrant s chicken products are conducted primarily by sales personnel at the Registrant s general corporate offices in Laurel, Mississippi and by customer service representatives at each of its eight processing complexes and through independent food brokers. Each complex has individual on-site distribution centers and uses the Registrant s truck fleet, as well as contract carriers, for distribution of its products.

Generally, the Registrant prices much of its chicken products based upon weekly and daily market prices reported by the Georgia Department of Agriculture and by private firms. Consistent with the industry, the Registrant s profitability is impacted by such market prices, which may fluctuate substantially and exhibit cyclical characteristics. The Registrant will adjust base prices depending upon value added, volume, product mix and other factors. While base prices may change weekly and daily, the Registrant s adjustment is generally negotiated from time to time with the Registrant s customers. The Registrant s sales are generally made on an as-ordered basis, and the Registrant maintains few long-term sales contracts with its non-chill pack customers.

The Registrant uses television, radio and newspaper advertising, point of purchase material and other marketing techniques to develop consumer awareness of and brand recognition for its Sanderson Farms® products. The Registrant has achieved a high level of public awareness and acceptance of its products through television advertising. Brand awareness is an important element of the Registrant s marketing philosophy, and it intends to continue brand name merchandising of its products. During calendar 2004, the Company launched an advertising campaign designed to distinguish the Company s fresh chicken products from competitors products. The campaign noted that the Company s product is a natural product free from salt, water and other additives that some competitors inject into their fresh chicken. The campaign was well received, and the Company plans to continue the campaign in the future.

The Registrant s processed and prepared food items are sold nationally and regionally, primarily to distributors and national food service accounts. Sales of such products are handled by independent food brokers located throughout the United States, primarily in the southeast and southwest United States, and by sales personnel of the Registrant. Processed and prepared food items are distributed from the Registrant s plant in Jackson, Mississippi, through arrangements with contract carriers.

**Production and Facilities**

**General.** The Registrant is a vertically-integrated producer of fresh and frozen chicken products, controlling the production of hatching eggs, hatching, feed manufacturing, growing, processing and packaging of its product lines.

**Breeding and Hatching**. The Registrant maintains its own breeder flocks for the production of hatching eggs. The Registrant s breeder flocks are acquired as one-day old chicks (known as pullets or cockerels) from primary breeding companies that specialize in the production of genetically designed breeder stock. As of October 31, 2007, the Registrant maintained contracts with 44 pullet farm operators for the grow-out of pullets (growing the pullet to

Table of Contents

the point at which it is capable of egg production, which takes approximately six months). Thereafter, the mature breeder flocks are transported by Registrant s vehicles to breeder farms that are maintained, as of October 31, 2007, by 129 independent contractors under the Registrant s supervision. Eggs produced by independent contract breeders are transported to Registrant s hatcheries in Registrant s vehicles.

The Registrant owns and operates seven hatcheries located in Mississippi, Texas and Georgia where eggs are incubated and hatched in a process requiring 21 days. Once hatched, the day-old chicks are vaccinated against common poultry diseases and are transported by Registrant s vehicles to independent contract grow-out farms. As of October 31, 2007, the Registrant s hatcheries were capable of producing an aggregate of approximately 8.6 million chicks per week.

**Grow-out.** The Registrant places its chicks on 528 grow-out farms, as of October 31, 2007, located in Mississippi, Louisiana, Texas and Georgia where broilers are grown to an age of approximately seven to nine weeks. The farms provide the Registrant with sufficient housing capacity for its operations, and are typically family-owned farms operated under contract with the Registrant. The farm owners provide facilities, utilities and labor; the Registrant supplies the day-old chicks, feed and veterinary and technical services. The farm owner is compensated pursuant to an incentive formula designed to promote production cost efficiency.

Historically, the Registrant has been able to accommodate expansion in grow-out facilities through additional contract arrangements with independent growers.

**Feed Mills.** An important factor in the grow-out of chickens is the rate at which chickens convert feed into body weight. The Registrant purchases on the open market the primary feed ingredients, including corn and soybean meal, which historically have been the largest cost components of the Registrant s total feed costs. The quality and composition of the feed are critical to the conversion rate, and accordingly, the Registrant formulates and produces its own feed. As of October 31, 2007, the Registrant operated 6 feed mills, 4 of which are located in Mississippi, one in Texas and one in Georgia. The Registrant s annual feed requirements for fiscal 2007 were approximately 2,594,000 tons, and it has the capacity to produce approximately 3,713,000 tons of finished feed annually under current configurations.

Feed grains are commodities subject to volatile price changes caused by weather, size of harvest, transportation and storage costs and the agricultural policies of the United States and foreign governments. On October 31, 2007, the Registrant had approximately 2,052,000 bushels of corn storage capacity at its feed mills, which was sufficient to store all of its weekly requirements for corn. Generally, the Registrant purchases its corn and other feed supplies at current prices from suppliers and, to a limited extent, directly from farmers. Feed grains are available from an adequate number of sources. Although the Registrant has not experienced, and does not anticipate problems in securing adequate supplies of feed grains, price fluctuations of feed grains can be expected to have a direct and material effect upon the Registrant s profitability. Although the Registrant attempts to manage the risk from volatile price changes in grain markets by sometimes purchasing grain at current prices for future delivery, it cannot eliminate the potentially adverse effect of grain price increases.

**Processing.** Once the chicks reach processing weight, they are transported to the Registrant s processing plants. These plants use modern, highly automated equipment to process and package the chickens. The Registrant s Pike County, Mississippi processing plant, which currently operates two processing lines on a double shift basis, is currently processing approximately 1,250,000 chickens per week. The Registrant s Collins, Mississippi processing plant, which currently operates two processing lines on a double shift basis, is currently processing approximately 1,250,000 chickens per week. The Registrant s Brazos County, Texas processing plant, which currently operates two processing lines on a double shift basis, is currently processing approximately 1,250,000 chickens per week. The Registrant s Laurel and Hazlehurst, Mississippi and Hammond, Louisiana processing plants, which currently operate on a double shift basis, are collectively processing approximately 1,875,000 chickens per week. The Registrant s Moultrie, Georgia processing plant, which currently operates two processing lines on a double shift basis, is currently processing 1,250,000 chickens per week. The Registrant s Waco, Texas processing plant, which began initial operations during the fourth quarter of fiscal 2007, currently is operating one processing line on a partial double shift basis. The Registrant also has the capabilities to produce deboned product at eight processing facilities.

At October 31, 2007, these deboning facilities were operating on a double shifted basis, except for the new Waco complex which will not reach full capacity until the summer of 2008, resulting in a combined capacity to process approximately 21.4 million pounds of boneless, skinless breast meat per week.

**Sanderson Farms, Inc. (Foods Division).** The facilities of Sanderson Farms, Inc. (Foods Division) are located in Jackson, Mississippi in a plant with approximately 75,000 square feet of refrigerated manufacturing and storage space. The plant uses highly automated equipment to prepare, process and freeze food items. The Registrant could increase significantly its production of processed and prepared food items without incurring significant capital expenditures or delays.

**Executive Offices; Other Facilities.** The Registrant s corporate offices are located in Laurel, Mississippi. As of October 31, 2007, the Registrant operated 9 automotive maintenance shops which service approximately 699 Registrant over-the-road and farm vehicles. In addition, the Registrant has one child care facility located near its Collins, Mississippi processing plant, currently serving over 155 children.

During fiscal 2005, the Company began construction of a new 90,000 square feet corporate office building in Laurel, Mississippi. Construction was completed in February 2006. The office building houses the Company s corporate offices, meeting facilities and computer equipment and constitutes the corporate headquarters.

**Quality Control**

The Registrant believes that quality control is important to its business and conducts quality control activities throughout all aspects of its operations. The Registrant believes these activities are beneficial to efficient production and in assuring its customers wholesome, high quality products.

From its company owned laboratory in Laurel, Mississippi, the Director of Technical Services supervises the operation of a modern, well-equipped laboratory which, among other things, monitors sanitation at the hatcheries, quality and purity of the Registrant s feed ingredients and feed, the health of the Registrant s breeder flocks and broilers, and conducts microbiological tests of live chickens, facilities and finished products. The Registrant conducts on-site quality control activities at each of the eight processing plants and the prepared food plant.

**Regulation**

The Registrant s facilities and operations are subject to regulation by various federal and state agencies, including, but not limited to, the Federal Food and Drug Administration ( FDA ), the United States Department of Agriculture ( USDA ), the Environmental Protection Agency, the Occupational Safety and Health Administration and corresponding state agencies. The Registrant s chicken processing plants are subject to continuous on-site inspection by the USDA. The Sanderson Farms, Inc. (Foods Division) processing plant operates under the USDA s Total Quality Control Program, which is a strict self-inspection plan written in cooperation with and monitored by the USDA. The FDA inspects the production of the Registrant s feed mills.

Compliance with existing regulations has not had a material adverse effect upon the Registrant s earnings or competitive position in the past and is not anticipated to have a materially adverse effect in the future. Management believes that the Registrant is in substantial compliance with existing laws and regulations relating to the operation of its facilities and does not know of any major capital expenditures necessary to comply with such statutes and regulations.

The Registrant takes extensive precautions to ensure that its flocks are healthy and that its processing plants and other facilities operate in a healthy and environmentally sound manner. Events beyond the control of the Registrant, however, such as an outbreak of disease in its flocks or the adoption by governmental agencies of more stringent regulations, could materially and adversely affect its operations.

Table of Contents

**Competition**

The Registrant is subject to significant competition from regional and national firms in all markets in which it competes. Some of the Registrant s competitors have greater financial and marketing resources than the Registrant.

The primary methods of competition are price, product quality, number of products offered, brand awareness and customer service. The Registrant has emphasized product quality and brand awareness through its advertising strategy. See Business Sales and Marketing . Although poultry is relatively inexpensive in comparison with other meats, the Registrant competes indirectly with the producers of other meats and fish, since changes in the relative prices of these foods may alter consumer buying patterns.

No customer accounted for more than 10.0% of consolidated sales for the years ended October 31, 2007, October 31, 2006, or October 31, 2005. The Company does not believe the loss of any customer would have a material adverse effect on the Company.

**Sources of Supply**

During fiscal 2007, the Registrant purchased its pullets and cockerels from two (2) major breeders. The Registrant has found the genetic breeds or cross breeds supplied by these companies to produce chickens most suitable to the Registrant s purposes. The Registrant has no written contracts with these breeders for the supply of breeder stock. Other sources of breeder stock are available, and the Registrant continually evaluates these sources of supply.

Should breeder stock from its present suppliers not be available for any reason, the Registrant believes that it could obtain adequate breeder stock from other suppliers.

Other major raw materials used by the Registrant include feed grains, cooking ingredients and packaging materials. The Registrant purchases these materials from a number of vendors and believes that its sources of supply are adequate for its present needs. The Registrant does not anticipate any difficulty in obtaining these materials in the future.

**Seasonality**

The demand for the Registrant s chicken products generally is greatest during the spring and summer months and lowest during the winter months.

**Trademarks**

The Registrant has registered with the United States Patent and Trademark Office the trademark Sanderson Farms®, which it uses in connection with the distribution of its prepared foods, frozen entree products and premium grade chill pack products. The Registrant considers the protection of this trademark to be important to its marketing efforts due to consumer awareness of and loyalty to the Sanderson Farms® label. The Registrant also has registered with the United States Patent and Trademark Office eight other trademarks that are used in connection with the distribution of chicken and other products and for other competitive purposes.

The Registrant, over the years, has developed important non-public proprietary information regarding product related matters. While the Registrant has internal safeguards and procedures to protect the confidentiality of such information, it does not generally seek patent protection for its technology.

**Table of Contents**

**Employee and Labor Relations**

As of October 31, 2007, the Registrant had 9,705 employees, including 1,059 salaried and 8,646 hourly employees. A collective bargaining agreement with the United Food and Commercial Workers International Union covering 580 hourly employees who work at the Registrant s processing plant in Hammond, Louisiana expired on December 1, 2007, and a new agreement has been negotiated. The new agreement will expire December 1, 2010. This collective bargaining agreement has a grievance procedure and no strike-no lockout clauses that should assist in maintaining stable labor relations at the Hammond plant.

A collective bargaining agreement with the Laborers International Union of North America, Professional Employees Local Union #693, AFL-CIO, covering 568 hourly employees who work at the Registrant s processing plant in Hazlehurst, Mississippi was renegotiated and signed effective January 1, 2006 and has an expiration date of December 31, 2008. This collective bargaining agreement has a grievance procedure and no strike-no lockout clauses that should assist in maintaining stable labor relations at the Hazlehurst plant.

A collective bargaining agreement with the Laborers International Union of North America, Professional Employees Local Union #693, AFL-CIO, covering 1,238 hourly employees who work at the Registrant s processing plant in Collins, Mississippi was renegotiated and signed effective January 11, 2007 and has a termination date of January 10, 2010. This collective bargaining agreement has a grievance procedure and no strike-no lockout clauses that should assist in maintaining stable labor relations at the Collins plant.

On June 9, 1999, the production, maintenance and clean-up employees at the Company s Bryan, Texas poultry processing facility voted to be represented by the United Food and Commercial Workers Union Local #408, AFL-CIO. A collective bargaining agreement was renegotiated effective January 1, 2006, with an expiration date of December 31, 2008. This collective bargaining agreement has a grievance procedure and no strike-no lockout clause that should assist in maintaining stable labor relations at the Bryan, Texas processing facility.

On November 30, 2001, live haul drivers at the Company s McComb, Mississippi production division voted to be represented by United Food and Commercial Workers Union Local #1529 AFL-CIO in collective bargaining. A collective bargaining agreement was reached with an expiration date of December 31, 2006. That agreement was renegotiated and signed effective January 1, 2007, and has an expiration date of December 31, 2009. The union demonstrated during 2004 by signed authorization cards that it had been chosen as the bargaining representative of the loader-operators, and at their request loader operators were included in the bargaining unit with the live-haul drivers.

On September 13, 2001, production, maintenance and truck driver employees at the Company s McComb, Mississippi Feed Mill facility voted to be represented in collective bargaining by United Food and Commercial Workers Union Local #1529 AFL-CIO. Negotiations were completed on a new contract in February 2005, and the current agreement expires December 31, 2007. A new agreement is currently being negotiated, but scheduling constraints on the part of the union s representative prevent the next meeting from occurring until after the current agreement expires.

**(d) FINANCIAL INFORMATION ABOUT GEOGRAPHIC AREAS**

All of the Company s operations are domiciled in the United States. All of the products sold to the Company s customers for the Company s fiscal years 2007, 2006 and 2005 were produced in the United States and all long-lived assets of the Company are domiciled in the United States.

The Company exports certain of its products to foreign markets, primarily Mexico, Russia, China, Puerto Rico, and the Caribbean. These exports sales for fiscal years 2007, 2006 and 2005 totaled approximately $164.4 million, $69.5 million, and $69.1 million, respectively. The Company s export sales are facilitated through independent food brokers located in the United States and the Company s internal sales staff. For fiscal 2007, 2006 and 2005, the Company made no sales of products produced in a country other than the United States.

**(e) AVAILABLE INFORMATION**

Our address on the world wide web is http://www.sandersonfarms.com. The information on our web site is not a part of this document. Our annual reports on Form 10-K, our quarterly reports on Form 10-Q, our current reports on Form 8-K, and all amendments to those reports and the Company s corporate code of conduct are available, free of charge, through our web site as soon as reasonably practicable after they are filed with the SEC. Information concerning corporate governance matters is also available on the website.

**Item 1A. Risk Factors**

**Before making an investment in our common stock, investors should consider carefully the following risks.**

*Industry cyclicality can affect our earnings, especially due to fluctuations in commodity prices of feed ingredients, chicken and alternative proteins.*

Profitability in the poultry industry is materially affected by the commodity prices of feed ingredients, chicken and alternative proteins. These prices are determined by supply and demand factors. As a result, the poultry industry is subject to wide fluctuations that are called cycles. Typically we do well when chicken and beef prices are high and feed prices are low. We do less well, and sometimes have losses, when chicken and beef prices are low and feed prices are high. It is very difficult to predict when these cycles will occur. All we can safely predict is that they do and will occur.

Various factors can affect the supply of corn and soybean meal, which are the primary ingredients of the feed we use. In particular, global weather patterns, the global level of supply inventories and demand for feed ingredients, currency fluctuations and the agricultural policies of the United States and foreign governments all affect the supply of feed ingredients. Weather patterns often change agricultural conditions in an unpredictable manner. A sudden and significant change in weather patterns could affect supplies of feed ingredients, as well as both the industry s and our ability to obtain feed ingredients, grow chickens or deliver products. More recently, demand for corn from ethanol producers has resulted in sharply higher costs for corn and other grains. Increases in the prices of feed ingredients will result in increases in raw material costs and operating costs. Because our chicken prices are related to the commodity prices of chickens, we typically are not able to increase our product prices to offset these increased grain costs. We periodically enter into contracts to purchase feed ingredients at current prices for future delivery to manage our feed ingredient costs. This practice reduces but does not eliminate the risk of increased operating costs from commodity price increases.

*Outbreaks of avian disease, such as avian influenza, or the perception that outbreaks may occur, can significantly restrict our ability to conduct our operations.*

We take reasonable precautions to ensure that our flocks are healthy and that our processing plants and other facilities operate in a sanitary and environmentally sound manner. Nevertheless, events beyond our control, such as the outbreak of avian disease, even if it does not affect our flocks, could significantly restrict our ability to conduct our operations or our sales. An outbreak of disease could result in governmental restrictions on the import and export of fresh chicken, including our fresh chicken products, or other products to or from our suppliers, facilities or customers, or require us to destroy one or more of our flocks. This could result in the cancellation of orders by our customers and create adverse publicity that may have a material adverse effect on our business, reputation and prospects. In addition, world wide fears about avian disease, such as avian influenza, has, in the past, depressed, demand for fresh chicken, which adversely impacted our sales.

Over the last two years there has been substantial publicity regarding a highly pathogenic strain of avian influenza, known as H5N1, which has affected Asia since 2002 and which has been found in Eastern Europe. It is

**Table of Contents**

widely believed that H5N1 is spread by migratory birds, such as ducks and geese. There have also been some cases where H5N1 is believed to have passed from birds to humans as humans came into contact with live birds that were infected with the disease.

Although the highly pathogenic H5N1 strain has not been identified in North America, there have been outbreaks of low pathogenic strains of avian influenza in North America, including in the U.S. in 2002 and 2004 and in Mexico in previous years, including 2005. In addition, low pathogenic strains of the avian influenza virus were detected in wild birds in the United States in 2006. Although these low pathogenic outbreaks have not generated the same level of concern, or received the same level of publicity or been accompanied by the same reduction in demand for poultry products in certain countries as that associated with the highly pathogenic H5N1 strain, they have nevertheless impacted our sales. Accordingly, even if the H5N1 strain does not spread to North America, we cannot assure you that it will not materially adversely affect domestic or international demand for poultry produced in North America, and, if it were to spread to North America, we cannot assure you that it would not significantly affect our operations or the demand for our products, in each case in a manner having a material adverse effect on our business, reputation or prospects.

*A decrease in demand for our products in the export markets could materially and adversely affect our results of operations.*

We export frozen chicken products overseas to Russia and other former Soviet countries, China and Mexico, among other countries. Any disruption to the export markets, such as trade embargos, import bans or quotas could materially impact our sales or create an over supply of chicken in the United States. This, in turn, could cause domestic poultry prices to decline. Any quotas or bans in the future could materially and adversely affect our sales and our results of operations.

*Competition in the poultry industry with other poultry companies, especially companies with greater resources, may make us unable to compete successfully in these industries, which could adversely affect our business.*

The poultry industry is highly competitive. Some of our competitors have greater financial and marketing resources than we have.

In general, the competitive factors in the U.S. poultry industry include:

- price;
- product quality;
- brand identification;
- breadth of product line and
- customer service.

Competitive factors vary by major market. In the foodservice market, competition is based on consistent quality, product development, service and price. In the U.S. retail market, we believe that competition is based on product quality, brand awareness, price and customer service. Our success depends in part on our ability to manage costs and be efficient in the highly competitive poultry industry.

*The loss of our major customers could have a material adverse effect on our results of operations.*

Our sales to our top ten customers represented 47.6% of our net sales during the 2007 fiscal year. Our non-chill pack customers, with whom we generally do not have long-term contracts, could significantly reduce or cease their purchases from us with little or no advance notice, which could materially and adversely affect our sales and results of operations.

*We must identify changing consumer preferences and develop and offer food products to meet their preferences.*

Consumer preferences evolve over time and the success of our food products depends on our ability to identify the tastes and dietary habits of consumers and to offer products that appeal to their preferences. We introduce new products and improved products from time to time and incur significant development and marketing cost. If our products fail to meet consumer preference, then our strategy to grow sales and profits with new products will be less successful.

*Inclement weather, such as excessive heat or storms, could hurt our flocks, which could in turn have a material adverse affect on our results of operations.*

Extreme weather in the Gulf South region where we operate, such as excessive heat, hurricanes or other storms, could impair the health or growth of our flocks or interfere with our hatching, production or shipping operations due to power outages, fuel shortages, damage to infrastructure, or disruption of shipping channels, among other things. Any of these factors could materially and adversely affect our results of operations.

*We rely heavily on the services of key personnel.*

We depend substantially on the leadership of a small number of executive officers and other key employees. We do not have employment agreements with these persons and they would not be bound by non-competition agreements or non-solicitation agreements if they were to leave us. The loss of the services of these persons could have a material adverse effect on our business, results of operations and financial condition.

*We depend on the availability of, and good relations with, our employees and contract growers.*

We have approximately 9,700 employees, 2,642 of which are covered by collective bargaining agreements or are members of labor unions. In addition, we contract with over 700 independent farms in Mississippi, Louisiana, Texas and Georgia for the grow-out of our breeder and broiler stock and the production of broiler eggs. Our operations depend on the availability of labor and contract growers and maintaining good relations with these persons and with labor unions. If we fail to maintain good relations with our employees or with the unions, we may experience labor strikes or work stoppages. If we do not attract and maintain contracts with our growers, our production operations could be negatively impacted.

*Immigration Legislation and Enforcement*

Immigration reform continues to attract significant attention in the public arena and the United States Congress. If new immigration legislation is enacted at the federal level or in states in which we do business, such legislation may contain provisions that could make it more difficult or costly for us to hire United States citizens and/or legal immigrant workers. In such case, we may incur additional costs to run our business or may have to change the way we conduct our operations, either of which could have a material adverse effect on our business, operating results and financial condition. Also, despite our past and continuing efforts to hire only United States citizens and/or persons legally authorized to work in the United States, increased enforcement efforts with respect to existing immigration laws by governmental authorities may disrupt a portion or our workforce or our operations at one or more of our facilities, thereby negatively impacting our business.

*If our poultry products become contaminated, we may be subject to product liability claims and product recalls.*

Poultry products may be subject to contamination by disease-producing organisms, or pathogens, such as Listeria monocytogenes, Salmonella and generic E. coli. These pathogens are generally found in the environment and, as a result, there is a risk that they, as a result of food processing, could be present in our processed poultry products. These pathogens can also be introduced as a result of improper handling by our customers, consumers or third parties after we have shipped the products. We control these risks through careful processing and testing of our finished product, but we cannot entirely eliminate them. We have little, if any, control over proper handling once the product has been shipped. Nevertheless, contamination that results from improper handling by our customers, consumers or third parties, or tampering with our products by those persons, may be blamed on us. Any publicity regarding product contamination or resulting illness or death could adversely affect us even if we did not cause the contamination and could have a material adverse effect on our business, reputation and future prospects. We could be required to recall our products if they are contaminated or damaged and product liability claims could be asserted against us.

14

**Table of Contents**

*We are exposed to risks relating to product liability, product recalls, property damage and injuries to persons, for which insurance coverage is expensive, limited and potentially inadequate.*

Our business operations entail a number of risks, including risks relating to product liability claims, product recalls, property damage and injuries to persons. We currently maintain insurance with respect to certain of these risks, including product liability and recall insurance, property insurance, workers compensation insurance and general liability insurance, but in many cases such insurance is expensive and difficult to obtain. We cannot assure you that we can maintain on reasonable terms sufficient coverage to protect us against losses due to any of these events.

*We would be adversely affected if we expand our business by acquiring other businesses or by building new processing plants, but fail to successfully integrate the acquired business or run a new plant efficiently.*

We regularly evaluate expansion opportunities such as acquiring other businesses or building new processing plants. Significant expansion involves risks such as additional debt and integrating the acquired business or new plant into our operations. In evaluating expansion opportunities, we carefully consider the effect that financing the opportunity will have on our financial condition. Successful expansion depends on our ability to integrate the acquired business or efficiently run the new plant. If we are unable to do this, expansion could adversely affect our operations, financial results and prospects.

*Governmental regulation is a constant factor affecting our business.*

The poultry industry is subject to federal, state, local and foreign governmental regulation relating to the processing, packaging, storage, distribution, advertising, labeling, quality and safety of food products. Unknown matters, new laws and regulations, or stricter interpretations of existing laws or regulations may materially affect our business or operations in the future. Our failure to comply with applicable laws and regulations could subject us to administrative penalties and civil remedies, including fines, injunctions and recalls of our products. Our operations are also subject to extensive and increasingly stringent regulations administered by the Environmental Protection Agency, which pertain to the discharge of materials into the environment and the handling and disposition of wastes. Failure to comply with these regulations can have serious consequences, including civil and administrative penalties and negative publicity.

*Our stock price may be volatile.*

The market price of our common stock could be subject to wide fluctuations in response to factors such as the following, many of which are beyond our control:

- market cyclicality and fluctuations in the price of feed grains and chicken products, as described above;
- quarterly variations in our operating results, or results that vary from the expectations of securities analysts and investors;
- changes in investor perceptions of the poultry industry in general, including our competitors and
- general economic and competitive conditions.

In addition, purchases or sales of large quantities of our stock could have an unusual effect on our market price.

*Anti-takeover provisions in our charter and by-laws may make it difficult for anyone to acquire us without approval of our board of directors.*

**Table of Contents**

Our articles of incorporation and by-laws contain provisions designed to discourage attempts to acquire control of our company without the approval of our board of directors. These provisions include a classified board of directors, advance notification requirements for stockholders to nominate persons for election to the board and to make stockholder proposals, special stockholder voting requirements and a poison pill that discourages acquisitions of shares that could increase ownership beyond 20% of our total shares. These measures may discourage offers to acquire us and may permit our board of directors to choose not to entertain offers to purchase us, even offers that are at a substantial premium to the market price of our stock. Our stockholders may therefore be deprived of opportunities to profit from a sale of control of our company.

**Item 1B. Unresolved Staff Comments.**

Not applicable.

**Item 2. Properties.**

The Registrant s principal properties are as follows:

| Use | Location (City, State) |
|---|---|
| Poultry complex, including poultry processing plant, hatchery and feedmill | Laurel, Mississippi |
| Poultry complex, including poultry processing plant, hatchery and feedmill | Pike County, Mississippi |
| Poultry complex, including poultry processing plant, hatchery and feedmill | Hazlehurst and Gallman, Mississippi |
| Poultry complex, including poultry processing plant, hatchery and feedmill | Brazos and Robertson Counties, Texas |
| Poultry complex, including poultry processing plant, hatchery and feedmill | Moultrie and Adel, Georgia |
| Poultry complex, including poultry processing plant and hatchery | Waco and McLennan County, Texas |
| Poultry processing plant | Hammond, Louisiana |
| Poultry processing plant, hatchery, child care facility and feedmill | Collins, Mississippi |
| Prepared food plant | Jackson, Mississippi |
| Corporate general offices and technical laboratory | Laurel, Mississippi |

The Registrant owns substantially all of its major operating facilities with the following exceptions: one processing plant and feed mill complex is leased on an annual renewal basis through 2063 with an option to purchase at a nominal amount at the end of the lease term. One processing plant complex is leased under four leases, which are renewable annually through 2061, 2063, 2075 and 2073, respectively. Certain infrastructure improvements associated with a processing plant are leased under a lease that expires in 2012 and is thereafter renewable annually through 2091. All of the foregoing leases are capital leases.

There are no material encumbrances on the major operating facilities owned by the Registrant, except that the plant of Sanderson Farms, Inc. (Foods Division) is encumbered by a mortgage which collateralizes a note with an outstanding principal balance of $328,000 on October 31, 2007, which bears interest at the rate of 5.0% per annum and is payable in equal annual installments through 2009. In addition, under the terms of the Company s revolving credit agreement, the Registrant may not pledge any additional assets as collateral other than fixed assets up to 15.0% of its tangible assets.

Management believes that the Company s facilities are suitable for its current purposes, and believes that current renovations and expansions will enhance present operations and allow for future internal growth.

**Item 3. Legal Proceedings**

**Table of Contents**

On June 6, 2006, Annie Collins, a former employee of the processing division subsidiary, on behalf of herself and as representative of a class of individuals who are similarly situated and who have suffered the same or similar damages filed a complaint against the Company s processing and production subsidiaries in the United States District Court for the Eastern District of Louisiana.
Plaintiffs allege that the Company s subsidiaries violated the Fair Labor Standards Act by failing to pay plaintiffs and other hourly employees for the time spent donning and doffing protective and sanitary clothing and performing other alleged compensable activities, and that Sanderson automatically deducted thirty minutes from each worker s workday for a meal break regardless of the actual time spent on break. Plaintiffs also allege that they were not paid overtime wages at the legal rate. Plaintiffs seek unpaid wages, liquidated damages and injunctive relief.
On July 31, 2006, following various procedural motions, the Company filed its Answer to the plaintiffs Complaint.
On July 20, 2006, ten current and former employees of the processing division subsidiary filed an action in the United States District Court for the Eastern District of Louisiana nearly identical to the one described above. Approximately 3,700 individuals purportedly have given their consent to be a party plaintiff to both this action and the action described above. Since the filing of these two complaints, six other substantially similar lawsuits were filed in United States District Courts for the Jackson and Hattiesburg divisions of the Southern District of Mississippi. Unlike the two suits referenced above filed in Louisiana (which suits were consolidated into one action), these complaints are specific to individual processing locations of the processing division subsidiary of the Company.

On March 26, 2007, the parties to the consolidated Louisiana action filed a Joint Motion for Preliminary Approval of Collection Action Settlement and Appointment of Plaintiff s Counsel as Class Counsel. Although not a party to the Louisiana matter, the plaintiffs in the Mississippi suits agreed to be bound by the settlement reached in the Louisiana suit, and the Mississippi suits have been stayed pending approval of the settlement motion before the Louisiana Court. On April 11, 2007, the Court denied the joint motion on two grounds: (1) The motion was premature because no motion to certify a collective action had been filed in the case, and (2) certain contingencies contained in the settlement agreement gave rise to concerns about whether the settlement agreement was in accordance with the Fair Labor Standards Act. The parties filed a Joint Motion for Reconsideration of this order of the Court, which was granted in part and denied in part by order dated May 3, 2007. In the order, the Court stated it would permit notice to the class to proceed. The Court also stated that if certain contingencies agreed to by the parties in the settlement agreement concerning class participation were met, it would consider the reasonableness of the proposed settlement at a fairness hearing The parties agreed to proceed in this manner, and the Court authorized the distribution of notice to the class. At the joint request of the parties, the Court extended the August 1, 2007 deadline for class members to opt into the lawsuits to September 14, 2007. On November 15, 2007, following the completion of notice to the class, the Company voided the settlement agreement because the contingencies in the agreement concerning class participation were not met. The Court held a settlement conference with the parties on December 5, 2007. At that conference, the parties agreed to a new tentative settlement on terms substantially similar to the earlier settlement, but proportionate to the participation elected by the plaintiff group. The parties agreed to an abbreviated notice period, and are seeking Court approval in order to finalize the settlement agreement. Even if approved, the settlement will still be subject to a fairness hearing to be held at the end of the notice period. In the Mississippi cases, the Company is seeking an extension of the stay currently in effect pending the Court s approval of the settlement.
The Company is also involved in various other claims and litigation incidental to its business. Although the outcome of the matters referred to in the proceeding sentence cannot be determined with certainty, management, upon the advice of c