

Q2 2007 Earnings Call

Company Participants

- Andre Dorf, Head of Paper Business Unit
- Antonio Maciel Neto, CEO
- Bernardo Szpigel, IR

Other Participants

- Marcos Assumpcao, Analyst
- Tereza Mello, Analyst
- Verena Wachnitz, Analyst

Presentation

Operator

There will be a replay facility for this call on the website. We inform you that all participants will be able to listen to the conference during the Company's presentation. (Operator Instructions).

Today's speakers will be Mr. Antonio Maciel Neto CEO, Mr. Bernardo Szpigel CFO and Investor Relations Officer, Mr. Rogerio Ziviani Head of Pulp & Paper Business Unit, Mr. Andre Dorf Head of Paper Business Unit and Mr. Ernesto Pousada Mucuri Project Officer.

We also would like to inform that statements during this conference may constitute forward-looking statements. Such statements are subject to known and unknown risks and uncertainties that could cause the Company's actual results to differ materially from those set forward in forward-looking statements. I will now pass the floor to Mr. Antonio Maciel Neto, CEO, who will start today's conference call. Thank you.

Antonio Maciel Neto {BIO 16703850 <GO>}

Hello. Good morning everyone, thank you very much for your participation this morning on this call, Suzano Pulp and Paper call. It's a pleasure to have this opportunity. I will start with a short presentation about the key highlights that we experienced during the last quarter. And just after Bernardo, or CFO and Investor Relations Officer, will go through a short presentation. And will have time just after with our other officers here to answer your questions.

I will start with the first slide two with the key highlights, I think you have this shown; or read, we are going to show you our key ten highlights for the quarter. Firstly, I'm going to start with the net profit. We reached \$172R million of net profit in the Second Quarter,

66.5% higher than in the Second Quarter of last year. We had strong operations in the quarter and we have some benefits coming from also the valuation of the Real.

Going to the EBITDA, we had also a strong EBITDA, \$279R.3 million, margins at 34%. And we would like to underline that this is under a very strong Real. So a combination of price increase and cost reduction led us to achieve this 34% margin in EBITDA in the Second Quarter.

Talking about the Pulp cash-cost, Mucuri pulp cash-cost, we have a good increase of this number. We achieved \$446R per ton in the Second Quarter, which is \$226 per ton. This was a good result. And Bernardo is going to a little bit more about these numbers as we move forward. Market pulp price, we experienced a \$20US increase per ton in June. And now we are with a price increase coming in August. Rogerio Ziviani will have the chance with you to talk about this as we move.

Pulp, market pulp inventories down to 27 days of shipments in June. So it's one of the lowest levels of inventories of market pulp in the last years, which is very good for us as we approach the start-up of our line 2 in Mucuri. It is a good time to start a new plant, a new line with a huge big volume when we have our inventories at one of the lowest levels in the last ten years at least.

Mucuri project, Ernesto Pousada is going to talk a little bit about that. But we are very happy to announce that we are on schedule and within budget. On time, on budget, nowadays we are working just following a list of issues to be solved. So October 1 continues to be our key deadline to start the project, to start the line 2. Also we have started, as we announced before, the Suzano Pulp and Paper Asia.

This is our office that is already helping us a lot in our relationship with our customers in that region, mainly with commercial and technical assistance to our customers in that region. We had also the start-up of the third turbine of the Amador Aguiar mill. We were before calling this Capim Branco, now after the inauguration we changed the name to Amador Aguiar.

This is the final completion of this project. So now this new mill is working at full capacity and is very good for our energy hedging. We are also very happy to mention that we have a new Chief of Forestry Business Unit Officer, Mr. Joao Comerio, who joined us some weeks ago and is working -- bring a very good experience of the forest business in Brazil and in the US as well.

And Joao is a good add to our team and he is starting his job with the Company during this month. Market capitalization reached \$4US.2 billion at the end of June. So it's a not a big record for our Company value and this is a good thing to communicate as well.

So as I mentioned before, now Bernardo Szpigel is going to go through the presentation, after that we have the Q&A. Thank you.

Bernardo Szpigel {BIO 2080745 <GO>}

Good morning. So proceeding with the presentation and moving to slide three, on the Mucuri project we have completed our civil works, erection assembly is almost completed, commissioning is already on its final phase. On the recovery boiler we had an excellent result with was a record in terms of construction times and equipment of this type, it is 20.5 months this completion.

The boiler is already operating. It is already helping to produce pulp in line 1. We brought down the existing recovery boiler for retrofitting, it's already underway. So it's fully operational. You can see in the photo in the middle of this slide the boiler already functioning, you steaming coming out of it.

On slide four on the Pulp Business Unit now. The highlights. The average net selling price for pulp in the export market was \$594US per ton in the Second Quarter '07, compared with \$588US in the First Quarter '07 and \$558US in Second Quarter '06. So an evolution in terms of increase of net realized prices for pulp over these quarters. We saw again growth in world demand. And this, combined with some reduction of high-cost producers that happened in '05 and '06.

This enhances an optimistic outlook for the start-up of this mill, as Maciel already pointed out. The production of this quarter in terms of market pulp was 167,400 tons. And we have cash-cost of \$225US per ton in the Second Quarter, which is a very good result. We have a reduction in terms of cost in Real per ton to 446. And an appreciation in terms of the Real in cash-cost in dollars to 225.

Moving now to slide five, we have some data in there comparing sales volumes in the three quarters and also net sales. We have been operating at this level of 175, roughly, thousand tons per quarter of market pulp, which is our sales capacity. In terms of exports, Europe continued to be our main export destination with 62% of our exports and Asia with essentially 25%.

Moving now to the Paper Business Unit on slide six, the average net selling price was \$2R,179 per ton for all markets. Of the sales, 60% of the volumes sold in the quarter was to the domestic market, which is an improvement compared with the previous quarter, due to the seasonal evolution. Paper sales volume in the domestic market was 12.7% higher than in the First Quarter '07 and 2.8% higher than in Second Quarter '06.

And a highlight for paperboard sales, which was 16% higher than a year ago than any other paper market and the performance over year. On slide seven, in terms of paper sales we had a very good quarter, 282,000 tons of paper sold in the Second Quarter '07 compared with 266,000 in First Quarter '07 and 262,000 in Second Quarter '06. Of our exports, remember that 40% of paper sales were exported, of this 40%, 45% went to Latin America.

Moving now to slide eight, some figures on the results and comparing the three quarters of Second Quarter '07 against First Quarter '07. And Second Quarter '06 and the

percentage basis also. It was a mostly positive -- very positive quarter, sales volumes were up by 4%, paper volumes, as I mentioned already, 12.8% up against the First Quarter and 2.8% against a year ago.

Pulp volume this is a normal valuation of quarter-on-quarter, not very significant, we haven't been increasing capacity in the last quarters. Net revenue following the evolution, in terms of the prices, which moved quite well in this quarter compared with the others. And also suffering now the negative affect of the appreciation of the Real in our exports.

Net income showing a very good result of 62% to 66% increase over previous quarters, not only the operational performance but also very significant. We had in this quarter a further appreciation of the currency from the beginning to the end of the quarter, which impacted the dollar exposure on our balance sheet.

Cash cost of 446 was already mentioned, a very good result, 3.5% below First Quarter '07, a very positive evolution, especially compared at the end of last year we were having higher cash costs for market pulp. EBITDA at \$279R million showed an increase of 1.7% against the First Quarter and 6.2% against a year ago. In dollar terms we reached \$141US million.

We are running right now at, considering the last 12 months, at \$540 million of EBITDA, which is a very good result. Of course this also has an impact on the further appreciation of the currency that we had shown.

EBITDA margin increased to 34percentage points against 33.9 in the First Quarter and 33.4 a year ago. A very good note also on the net debt to EBITDA ratio, we are of course implementing the Mucuri project, a very large investment being performed in the recent quarters. And we have maintained our net debt to EBITDA ratio at 3.7 times, which is a very good result for the Company as a whole.

So with this we complete the presentation. And we will open to the question-and-answer session. Thank you.

Questions And Answers

Operator

Thank you. (Operator Instructions). Our first question is coming from Marcos Assumpcao of Merrill Lynch.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Hi good morning, gentlemen. My first question goes to Mr. Antonio Maciel, it is regarding the potential reduction in cash-cost per ton of pulp after the learning curve of the Mucuri project. I don't know, Maciel, if you could quantify a little bit what could be the reduction of cash-cost per ton of Suzano overall after the learning curve of Mucuri project, assuming a flat FX rate.

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A - Antonio Maciel Neto {BIO 16703850 <GO>}

Marcos, first to thank you for your question, I'd like to say that we experienced this reduction of our cash-cost this quarter, as we have -- or anticipated before in the last call, several actions that we are taking to reduction these specific costs. Now in the next quarter, going from now to the end of the year, we will have some variations in these costs, because we will have a maintenance period in Mucuri for about ten days.

We are going to also to fit the whole -- full integration of line 2 into the site and making the connections and the links between the line 2 and line 1. So we have a very interesting period, a lot of excitement going around there with this period where we have this maintenance period, we have the completion of all the connections and links and this like. So we will see a variation in the coming next quarter and probably some improvement at the end of the year.

As we have the learning curve completed that we are expecting that is going to happen in between six to nine months from the start-up, we are going really to see a whole reduction in the cash-cost of our pulp producing in Mucuri. Our initial estimates are considering from 5% to 10% of the current levels that we have. 5% to 10% this is what we are considering that are going to be possible considering the new technology that we are using there, a lot of usage of microelectronics, this is a new equipment and new technologies.

And this is going to provide a lower cost than we had before. It is important to underline that our line 1 is very good as well, it's one of the newest in the world. And now we are adding really the newest technology in the newest line. So we consider 5% to 10% to be a good number after the learning curve.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Okay, perfect. And a second question maybe for Bernardo is regarding the maintenance CapEx for Suzano after the pulp expansion project. What will be the next level for maintenance CapEx now?

A - Bernardo Szpigel {BIO 2080745 <GO>}

I think, total for all the mills on a consolidated basis we are working with \$150 million maintenance CapEx.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

I'm sorry, can you repeat that?

A - Bernardo Szpigel {BIO 2080745 <GO>}

\$150 million per year for all mills after we reach -- with the second line included.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

FINAL

Okay. Thank you. And my last question goes to Andre Dorf. I would like to hear from you if you have any comments on the recent announced merger between Bowater and Abitibi in the U.S.. And if this could have any impact in terms of prices for paper in the uncoated segment or any other segments in the U.S. market. And actually, if this could potentially impact your sales as well?

A - Andre Dorf {BIO 15460232 <GO>}

Yes, hi Marcos. Both players are more focused on newsprint and low weighted coated, rather than printing and writing coat size or paperboard, which are the grades that we export to those markets. We've seen the U.S. markets strengthening a little bit after the countervailing tariffs and antidumping tariffs against the Asians. And causing less pressure, especially on the coated side. So we expect the second half of the year is better than we have in the first one for the printing and writing grades.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Okay. Then just to clarify here, do you still -- are you still suffering pressure in terms of prices in the domestic market coming from imports from the Third Quarter?

A - Andre Dorf {BIO 15460232 <GO>}

Yes. Apparently the degree that suffers more pressure against the imports is the coated one. And apparently the imports stabilized in the level of 40% of our domestic market. So we don't expect any increase or further increase in these levels in terms of imports. And we expect to sustain our current prices looking forward.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Okay. Great. Thank you very much.

Operator

Thank you. (Operator Instructions). Our next question comes from Tereza Mello of Citi.

Q - Tereza Mello {BIO 6448187 <GO>}

Hi. Good afternoon, -- good morning. A quick question regarding your long-term outlook for leverage. After the conclusion of the Mucuri mill, you don't have any (inaudible) projects starting in the next few years. What's your leverage target? And what do you think it -- do you think you are going to be unlevered, or are your plans to pay higher dividends with this additional cash that you are going to be generating in the next few years? Thank you.

A - Antonio Maciel Neto {BIO 16703850 <GO>}

This is Antonio Maciel. I'd like to say that we are going to have this deleveraging in a very quick, very fast due to the cash generation that we are going to experience with the second line launch. So this is why we also have mentioned that before year-end, we are

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going to announce our growth strategy or at least a growth project regarding to -- pulp, the market pulp.

So we are considering a new cycle of growth. We are finishing a cycle that we have some debottlenecking. We have the acquisition of Ripasa. And we have this big project Mucuri. This -- as we conclude this cycle, we are going to -- we are working now that is in the next cycle of the growth.

We have this -- we have to see -- we are not committing, that is to say a firm commitment, with this number of net debt ratio versus EBITDA, mainly because we would like to consider new projects, new opportunities to have some acquisition opportunities to work. In -- we are at 373 now off of this number, which is going to grow a little bit during the year and then it's going to go down. We think that three is a good number for a company like this for --

Q - Tereza Mello {BIO 6448187 <GO>}

Okay.

A - Antonio Maciel Neto {BIO 16703850 <GO>}

Okay? Investment grade has been achieved with two or 1.5. So we are considering -- three is a good number for us. Three or less than three is a good number. But we are not setting a firm commitment because we would like to consider the new opportunities for acquisition or new projects coming.

And also just to conclude, this statement is we have now a much better condition to play a good role in the capital market. So we are not going to have only the best markets to -- for the growth. We can have all the, if you want, some of the other alternatives related to the capital market.

Q - Tereza Mello {BIO 6448187 <GO>}

Okay. But just -- do you have any level that you consider to be unlevered then at that point, you would then to remain for a very long time? What do you consider your optimal capital structure? Or, if you don't have any projects or it takes too long to announce this project, would you go to a net debt to EBITDA of one?

A - Antonio Maciel Neto {BIO 16703850 <GO>}

It's, I think, 1.5 we say is a good number. From one to 1.5 is the number that we have. In the market, we have seen the companies without these big projects who are very well analyzed, is a good number from one to 1.5.

As we move, we have very fast going below three and this is -- but we will have projects and we are going to consider that and the capital market. I'll ask Bernard to come to talk a little bit about this though.

Q - Tereza Mello {BIO 6448187 <GO>}

Thank you.

A - Bernardo Szpigel {BIO 2080745 <GO>}

It is just completely what Maciel just said. If we don't have projects, then of course we need to go down to one to one and a half times. So this is a very comfortable level in terms of capital structure for the Company.

For a company like ours where you have sometimes large projects like the Mucuri project. And you can leverage the projects with very good funding as we have done in the case of this Mucuri, then we may go up with a project above these levels, provided that we have a good funding and we are providing a good return to shareholders.

We know that with the leverage the funding that we obtained for the project we are leveraging shareholders' money significantly, funding the project with 78% of very good debt. A project like the one that you see in terms of the new mill will also have an impact that in the first years, it's just the formation of a FOREX base. Not a very large CapEx in the initial years.

Q - Tereza Mello {BIO 6448187 <GO>}

Yes.

A - Bernardo Szpigel {BIO 2080745 <GO>}

Only when you enter the construction of the mill itself, an investment growth above \$1 billion, then net debt to EBITDA would go up. This is the case, you have seen for Suzano ourselves, we were running by the time we -- before we acquired, Ripasa one and a half times net debt to EBITDA. And getting ready for the Mucuri mill and also with the acquisition of Ripasa we went up to something like two, two and a half times net debt to EBITDA. So the optimal net debt to EBITDA ratio of course depends on the kind of projects that you can have.

Q - Tereza Mello {BIO 6448187 <GO>}

Okay. Thank you very much. If I may ask just another question regarding your -- what pulp prices are you currently using to analyze projects in the long term? I ask that because of this change in the Brazilian currency dues over the last few years and what you believe. Do you believe you are now in a -- we are going to have a higher pulp price in the long term? Have you already moved to a higher pulp price or not?

A - Bernardo Szpigel {BIO 2080745 <GO>}

Well in terms of -- I'm -- our outlook for the market continues to be one in which we see room for new capacity, very competitive capacity in Brazil and we ourselves, we are considering projects that continue to have cash costs, which are competitive worldwide. And we should continue to see the growth in the market for eucalyptus for example, it grows -- those growth rates of 6 -- of 5% to 7% a year in the current year.

Prices that we have been using to -- for our studies have moved up from recent years. By the time that you are performing the feasibility studies for the Mucuri projects, you are looking at normalized prices of below \$500 per ton, 480 (inaudible) prices. Now I think that most everybody -- almost everybody would agree that we're talking about 550 or more on a normalized base.

Of course this also reflects some weakness of the dollar. But our relative competitive position is not only against the dollar. But against the dollar and the other currencies. And some of our competitors and our main customers as well. So projects, new projects, at these levels continue in our case to show feasibility an adequate return, compared to our weighted average cost of capital.

Q - Tereza Mello {BIO 6448187 <GO>}

Okay. Thank you very much.

A - Bernardo Szpigel {BIO 2080745 <GO>}

Sure.

Operator

Thank you. Our next question is coming from Verena Wachnitz of T. Rowe Price.

Q - Verena Wachnitz {BIO 5955218 <GO>}

Hi. Good morning. My question is regarding SG&A expenses. We saw a reduction in your G&A expenses in this quarter both year-on-year and quarter-on-quarter, can you comment on what that growth -- that reduction. And if that is the run rate going forward? Then selling expenses did increase. And if you could also commented on that. Thank you very much.

A - Bernardo Szpigel {BIO 2080745 <GO>}

Well Verena. Good morning. We saw a reduction in S -- in G&A expenses more than (S). And G&A is slowing efforts in terms of cutting costs, administrative and fixed costs. We are working to get some improvements. We would expect to continue to move on -- reduction as we move ahead.

On sales expenses, we had a non-recurring item, which was bad debt, increasing bad debt provision of \$5R million, which increased our costs on a non-recurring basis. In general, we are also -- we also increased the S table simply because of volumes sold, which were higher in this quarter.

But in general we also, we would expect to have some improvements on that side as well. As we obtain larger volumes in our business, we are also negotiating some improvement in the costs, transportation costs that impact our selling expenses.

Q - Verena Wachnitz {BIO 5955218 <GO>}

All right. Thank you.

A - Bernardo Szpigel {BIO 2080745 <GO>}

Sure.

Operator

Thank you. (Operator Instructions). There appear to be no further questions. This concludes the question and answer session. At this time, I would like to turn the floor back to Mr. Antonio Maciel Neto for any closing remarks.

A - Antonio Maciel Neto {BIO 16703850 <GO>}

Okay. Thank you very much for the participation in this call this morning. We are very happy with these results and very excited with -- for the coming quarter where we have the start-up of Mucuri and several channels coming in. We will be always ready to answer questions through our investor relations department or direct with us, with the officers here. Thank you very much for the participation and a good morning.

Operator

Thank you. This does conclude today's presentation. You may disconnect your lines at this time and have a wonderful day.

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