

Q4 2016 Earnings Call

Company Participants

- Guilherme Setubal Souza e Silva, Executive Manager-Investor Relations

Other Participants

- Paulo Guimaraes Valaci, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen, and welcome to the Audio Conference Call of Duratex. Thank you for standing by. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions to participate will be given at that time. As a reminder, this conference is being recorded.

I would now like to turn the conference over to Mr. Guilherme Silva, Investor Relations Manager. Please go ahead, sir.

Guilherme Setubal Souza e Silva {BIO 20114864 <GO>}

Good morning, everybody. Thanks for joining this Duratex final quarter presentation. My name is Guilherme Silva. I am the IR Manager of the company. So, first of all, please turn to page number 2 and the idea here is to discuss the highlight of the final quarter 2016.

Let's start with the Wood Division. First point, volumes grew in both domestic market and exports, however, with a less profitable mix of products; point number two, sales of land and timber during the fourth quarter, with a positive cash generation; and last one, on the Wood Division, EBITDA increase that has offset the negative trend in the first quarter.

So let's move to the Deca Division. Highlight number one, Deca Division has outperformed the industry average. Again, I'd like to reinforce that when you compare Deca's performance with the ABRAMAT index, Deca had a better performance than the average of the segment. Second one, more favorable mix of products in this last quarter 2016.

So let's move to the financial performance. First one, recurrent EBITDA margin of 21.1%, the best margin in the last year, right, and the average margin of 2015. Second one, and very, very important one, the net debt/EBITDA, the ratio net debt/EBITDA equaled 2.99 times, below 3 times, right. So it's important to mention here that in the third quarter 2016, this ratio was 3.3% (sic) [3.3 times] (02:32), as one of our targets over the last

quarter was to reduce this ratio. This was the result of the focus on working capital reduction, investment control and liquidation of idle assets.

So right now, please turn to the next page, page number 3, and here, we will discuss the consolidated financial figures. The consolidated net revenues in this final quarter 2016 was around BRL 1 billion. This amount was 6.4% higher than the third quarter 2016, and around 8% higher than the same period of 2015.

Recurrent EBITDA increased from BRL 186 million to BRL 217 million, right. The recurrent EBITDA margin increased from 19.2% to 21.1%. As I said before, right now, the EBITDA margin of the final quarter 2016 was in the same level of the average of 2015. Recurrent net profit reduced from BRL 9 million to BRL 6 million, but it's important to mention that during the all year, the net profit was around BRL 30 million.

In the pie chart below, we have the net revenue breakdown. 50% of the revenues in this final quarter 2016 came from the Wood Division in Brazil; 11% came from the Wood Division in Colombia; and the rest 34% came from Deca Division.

In the chart beside, you have the relation between foreign market and the total revenues of the company. It's important to mention that the average of 2016, the foreign market represents around 20% of the revenues, basically through exports plus Wood Division in Colombia. I'd like to reinforce part of our targets to reach around 30% of our revenues comes from out of Brazil Tablemac with the Wood Division in Colombia, plus exports over the next few years.

So right now, please turn to next page, page number 4. And the idea here is to discuss the CapEx, the investment of the company over the last years. So in the first chart, you have the maintenance and projects, basically, our industrial CapEx, right. As you can see, we finalized important high core (05:12) investment between 2013 and 2014. After that, our maintenance CapEx is very focused on the sustaining of the business, right.

Right now in 2016 and our idea for over the next years is to have CapEx industrial only to the sustaining business around BRL 200 million. The chart beside you have our forest OpEx. This is more focused in our long run strategy, right. So when we are doing this investment right now, we are focusing six years ahead. As you can see, we are keeping this investment in the same level over the last years. Last year, in 2016, our forest OpEx was around BRL 191 million.

And the chart beside, we have the merger and acquisitions. Basically in 2016, we did the tender offer of Tablemac, right. So in the beginning of the last year, we had 80% of the shares, and right now, we're close to a 100% of the shares. We're considering this business in Colombia, Tablemac, as the delisted company.

So right now, please turn to page number 5. And the idea here is to disclose the corporate debt, amortization schedule and debt composition. First of all, I would like to raise as a main highlight of this slide the reduction in our net debt. We reduced our net

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debt around BRL 87 million, basically due to sales of land, sales of timber, very focused on our working capital, right, and extended tenure to pay the suppliers.

In addition to that, we increased EBITDA quarter-on-quarter, right and given that, we could reduce the ratio net debt/EBITDA from 3.3 times to below 3 times this year. It's very important, this part of the strategy of the company for the year of 2017 to keep this trend to reduce the ratio net debt/EBITDA.

In the chart below, we have the amortization schedule, right. So our cash position BRL 1.4 billion. Our total debt BRL 3.4 billion. But as you can see, we have enough money to pay off all of our debt in 2017 and 2019 (07:49). So we can see that we are very comfortable right now with our cash position.

In the pie chart beside, we have our debt composition. Around 70% of our debt are in domestic currency, basically, working capital in BRL and BNDES loans and the rest 30% of our debt are in foreign currency basically Resolution 4121, but it's important to mention that we did a swap, we did the hedge of all of our debt. So we don't have any exposure in other currency than BRL in our debts.

So right now, please move to page number 7, and we will start the discussion about the Wood Division. The first slide lies in page number 7, we have the MDF market and MDP market. As we can see year-on-year, the MDF market, as a whole, not only Duratex, but all industry in Brazil, decreased 3.7%, but I'd like to mention that quarter-on-quarter, so last quarter 2015 against last quarter 2016, the MDF increased 12%. This is an important indicator that economy can recover next year. I'm not saying that the economy will recover, but it's important sign to measure the potential to recover the economy next year.

Regarding MDP, the market last year was flat year-on-year, and when compared with the last quarter 2015 against last quarter 2016, the MDP decreased only 1.6%.

So right now, please turn to page number 8, and here we will discuss the operational performance of the Wood Division in Duratex. So regarding the shipment, the volumes. As a main highlight of this quarter, the volumes increased 10% quarter-on-quarter, and 7.2% last quarter 2015 against last quarter 2016, right. The volumes in this fourth quarter 2016 was 639,000 cubic meters. However, year-on-year, the volumes in Duratex has decreased 2.6%, reaching 2.433 million cubic meters in 2016.

In the chart beside, you have the occupancy rate of Duratex in the next last quarter 2016. MDF, including Itapetininga 60%, without Itapetininga 79%. MDP, 53% including Itapetininga, without Itapetininga 67%. Hardboard was the same, because there is no hardboard line in Itapetininga, was the same 80% in this final quarter 2016.

Right now, please move to page number 9. And here, we should discuss the financial performance of the Wood Division. The net revenues in this fourth quarter 2016 increased 10%, the same amount when compared to the final quarter 2015, basically due to the

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better volume that we had in this last quarter. However, year-on-year, the net revenue was quite stable. The net revenue of the Wood Division reached BRL 2.6 billion in 2016.

In the chart beside, you have the recurrent EBITDA. The recurrent EBITDA in this fourth quarter 2016 increased from BRL 135 million to BRL 175 million, basically due to the sales of timber that we did to Fibria in last December, the amount was BRL 38 million. And given that the margins in the third quarter increased from 21.5% to 25.3% in this final quarter 2016. However, year-on-year, the EBITDA in the Wood Division decreased around 15% which is BRL 104 million (12:11), basically due to a lower volume and unfavorable mix of products, okay.

So let's move to the last slide about the Wood Division. And here, the idea is to discuss the Wood Division in Colombia. So as you can see, the performance of the Wood Division in this final quarter 2016, Colombia was very similar of the third quarter 2016. I'd like to reinforce here that the Wood Division in Colombia is going very well, running full capacity and we're improving our results, and our forecast is very favorable for 2016, 2017 again. So that's it from the Wood Division.

Please turn to next page, page number 12 and here we'll discuss about Deca Division. In the first slide about ABRAMAT index. ABRAMAT index measures the growth in the revenues of building materials in domestic market. In 2016, this index decreased 11.5%. As I mentioned before, the net revenues of Deca decreased only 4% last year. What you can conclude here is probably Deca is gaining market share against our competitors.

And finally, regarding the forecast about ABRAMAT in 2017, the forecast is flat 2017 against 2016. This shows that we can see a positive year in 2017 when compared with last year that we saw a huge decrease in terms of revenues in this segment.

Right now, move to page number 13, and here we have the operational performance in Deca Division in this final quarter 2016. Regarding the shipment, the volume decreased 10% quarter-on-quarter, when compared third 2016 against final quarter 2016, and 4.4% last quarter 2015 against last quarter 2016. It's important to mention that year-on-year the volume in Deca Division decreased 5.3%. The chart beside, you have the occupancy rate in the Deca Division in this final quarter 2016, Sanitary Wares 60%, Metal Fittings 72%.

And finally, please turn to the last slide regarding Deca, slide number 14. And here, we have the financial performance of Deca Division. The net revenues in this fourth quarter 2016 was BRL 337 million, was flat when compared to the third quarter 2016, and quite flat when compared to the last quarter 2015, basically because we could increase price in this division. So we have the same level of revenues with lower volume. However, year-on-year, the net revenue decreased 3.7% year-on-year.

In the chart beside, you have the recurrent EBITDA in Deca Division. The recurrent EBITDA in this final quarter 2016 decreased 18% when compared to the third quarter 2016 and around 12% when compared to the same period of 2015. Given that, the recurrent EBITDA (sic) [EBITDA margin] (15:51) decreased 15% to 12%, basically the main reason is the lower volume that we had in this final quarter. And year-on-year, the EBITDA in Deca Division

decreased 27%, reached 177% (sic) [BRL 177 million] (16:10) basically from the main reason lower volume in this division in 2016. That's it from the Deca Division.

And right now, please turn to page number 15, the last page, and here we have the final management message. So regarding 2016, what we did which was our initiatives last year? First of all, as you know very well, internal agenda, we were very focused in our internal agenda, cost cutting and efficiency programs, optimization of systems and processes, about our culture project. I'd like to reinforce that this program will keep going this year and next year, and we were very focused of investment on sustaining operations only.

Regarding 2017, what is the scenario? What's the environment? First one, outlook of a slow and gradual recovery in the economic activities, reduction in interest rates and fall in unemployment and, finally, improvement in the consumer confidence and business environment.

What will be our focus in 2017? We keep our focus in our internal agenda to become lean and more efficient, efforts to improve the product mix. We are very, very focused on working capital management, focus on inventories and account payables. I'd like to raise here that this is our main target for the financial value of the company, but not only financial value, but all companies to reduce inventories, okay. Investments mainly for the sustaining of the business as I said before and finally, due to the all efforts that we are doing, cutting net debt and financial expenses.

So that's it. Thanks very much for your time and right now, Filipe (18:14) and myself, we are able to answer the questions.

Q&A

Operator

Ladies and gentlemen, we'll now begin the question-and-answer session. Our first question comes from Paulo Valaci, Citi.

Q - Paulo Guimaraes Valaci {BIO 18268142 <GO>}

Good morning, Guilherme and Filipe (18:41). Thank you for the opportunity. Two questions. First one, could you provide an update on the current state of supply? We know there is a significant amount of idle capacity in the wood panels market. I'm wondering what you've seen in terms of maintenance part, just within the sector in the past several months and how sustainable you think this current window of price increases could be as these production lines return to normalized production levels.

And then, second, could you just specify CapEx guidance for 2017? I know you mentioned just maintenance CapEx, will that be around BRL 400 million, is that a decent amount to work with for 2017?

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A - Guilherme Setubal Souza e Silva {BIO 20114864 <GO>}

Okay. So thanks for your question, Paulo. So let's start with the first one. So regarding the price increase, as we discussed before, this is a scenario to recover pricing okay, so this pricing, suffering a lot over the last quarters, okay. And right now, all industry as a whole, not only Duratex, is trying to recover price. So what we are seeing right now is that we are lack of production as a whole, and given that there is opportunity to increase price, okay.

And we believe that since the second quarter 2017, we can see a recovery in economy, right, so and this recovery will be enough to sustain this price increase that we have announced for March, okay. So regarding the CapEx for 2017, I mean we believe that would be in the same amount of 2016 without of course the acquisition of Tablemac, okay. So we believe that our sustaining CapEx in the industrial side would be below BRL 200 million. And regarding the forest division, it will be below BRL 200 million. So we believe that the same amount of BRL 380 million or something close to BRL 400 million, okay.

Q - Paulo Guimaraes Valaci {BIO 18268142 <GO>}

Perfect. Thank you.

Operator

This concludes today's question-and-answer session. I would like to invite Mr. Guilherme to proceed with his closing statements. Please go ahead, sir.

A - Guilherme Setubal Souza e Silva {BIO 20114864 <GO>}

So again, thanks very much for your time guys. And Filipe (21:37) and myself are available to answer the questions, okay, if you have any new questions further after this call, okay. Thank you very much.

Operator

That does conclude the Duratex audio conference for today. Thank you very much for your participation. Have a good day and thank you for using Chorus Call.

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