

Q4 2015 Earnings Call

Company Participants

- Aurélio Pavinato, Chief Executive Officer
- Ivo Marcon Brum, Chief Financial & Investor Relations Officer

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen, and thank you for waiting. At this time, we'd like to welcome everyone to SLC Agricola Fourth Quarter of 2015 Earnings Conference Call. Today, with us we have Mr. Aurélio Pavinato, CEO; and Mr. Ivo Brum, CFO and Investor Relations Officer. We would like to inform you that this event is being recorded and all participants will be in a listen-only mode during the company's presentation.

After the company's remarks are completed, there will be a question-and-answer session. At that time, further instructions will be given. Also, today's live webcast, both audio and slideshow, may be accessed through SLC Agricola website at www.slcaagricola.com.br in the Investor Relations section by clicking on the banner Webcast 4Q15. The following presentation is also available to download on the webcast platform. The following information is available in thousands of Brazilian reals and in IFRS, except when otherwise indicated.

Before proceeding, let me mention that forward-looking statements are based on beliefs and assumptions of SLC Agricola management and on information currently available to the company. They involve risks, uncertainties and assumptions, because they relate to future events, and therefore, depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of the company and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I'll turn the conference over to Mr. Aurélio Pavinato, CEO. Mr. Pavinato, you may proceed.

Aurélio Pavinato

Good morning and thank you for participating in SLC Agricola's earnings conference call for fourth quarter and fiscal year 2015. Let's go to slide two, where we'll start by commenting on the highlights of the year. As detailed in the management's message in our earnings release, last year, SLC Agricola set various new records, which includes net revenue which reached R\$1.8 billion, growing 17.5% on 2014; EBITDA of R\$340 million, advancing 6%; and free cash flow generation of R\$132.5 million, which is in line with our

current strategic focus of slowing our growth pace in order to prioritize our financial stability.

Let's go to slide four, which shows some indicators for operational efficiency. Here, you can see our general and administrative expenses in the year compared to the numbers of hectares planted in the corresponding crop year, which shows a sharp drop of 38% over the last four years to R\$107 per hectare in 2015. The number of hectares per employee based on the number of people involved in production, processing and administrative activities continues to grow, reaching 163 hectares in the 2014/2015 crop year, up 28% from four years ago.

On slide five, you can see two more of our efficiency indicators. Advances in technology, we have been pursuing clear through (4:14) the numbers of hectares on which we use precision agriculture, increasing to 235,000 hectares in 2016 compared to 97,000 in 2012. This technology enable us to better control the yields activity inside each field cultivated and the resulting optimization of inputs used. Lastly is the indicator of horsepower per hectare of our tractor fleet, where we can see the important decline over the past few years, which shows that we have been able to do more with less due to our ongoing efforts to better control our agricultural operations.

Let's go to slide seven, where we will comment on the price of our main products during 2015. The international cotton market was marked by low price volatility in 2015. There are (5:31) opposing forces acting in the cotton market that prevent major prices variations. On one side, we have the continued contraction in planted area and adverse weather factors in various parts of the world. And on the other side, we have the uncertainties related to the high level of China's cotton stockpiles, or more specifically, the uncertainty regarding the policy the country will adopt to place these stocks in the market.

Planted area suffered reductions in almost all cotton-producing countries in 2015/2016 crop year. The harvested area contracted 9% on the prior crop year, which combined with the 6.5% drop in yields led to a drop in production of 116% (6:34). So, for the first time in five years, production should lag consumption, which points to drawdowns in world inventories, especially outside of China. In the Brazilian market, the weaker local currency supports higher exports, which reduced domestic supply and considerably increased the price of cotton lint in Brazilian real.

Note that the current level of U.S. dollar exchange rate makes Brazil even more competitive in cotton production. Soybean prices, however, declined on the Chicago Board of Trade during 2015. This decline is mainly associated with the growth in U.S. stocks and the expansion in planted area in South America in the 2015/2016 crop year, as well as the uncertainties regarding the world economy, especially the dropping oil prices, which left speculators less willing to hold the defensive positions in commodities.

If the USDA's current estimates are confirmed, world production should reach 320 million tons in the 2015/2016 crop year, while the world consumption should reach 314 million tons. Despite the resulting nominal growth in (8:10) stocks, it's important to note that the stocks-to-use ratio should remain stable at 25.6% due to growing world consumption.

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Considering the trend in consumption based on the average growth of 4.5% in the last five years, we estimate demand of around 330 million tons in 2016/2017 crop year, creating the prospect of a reduction in stocks and consequently the need to expand the planted area. For that to occur, a rebound in international prices is needed. USDA data for the United States in the 2016/2017 crop year validated this expectation since it projects a stability in the soybean area, combined with a slight drop in yields, as well as growing consumption, which would lead any stocks to decline and the stocks-to-use ratio to fall from 13% to 11%.

Corn prices also fell in the international market in 2015, although to a lesser degree than soybean prices. However, in Brazil, the weak real led to a significantly higher corn prices in local currency in the domestic market and support the strong sales volume, especially in the export market, where the countries have become more competitive. In the last quarter of 2015 and early 2016, the market was already pricing in a declining stocks called by experts (10:04) and corn price in the Brazilian market surpassed international prices even in dollar, which presents good sales opportunities.

World corn production fell 3.9% in the 2015/2016 crop year, and according to the USDA, should amount to 970 million tons. World consumption, in the other hand, continued to grow to 976 million tons, increasing 1.6% on the previous year and also pointing to the prospect of leaner stocks in the coming years.

I will now hand the call over to my colleague, Ivo Brum, our CFO and IRO, who will comment on our financial results in the period.

Ivo Marcon Brum {BIO 16639894 <GO>}

Good morning, everyone. Let's go to slide nine, which presents some highlights from our income statement for 2015. As Aurélio (11:15) commented, the net revenue of R\$1.8 billion set a new record and was 17% higher than 2014. Revenue growth was driven by the higher volume of cotton and soybean invoiced in the period and by the higher average prices obtained. EBITDA in the year was R\$339.7 million, advancing 6.1% on the prior year, which is explained by higher margins for all products except cotton. Net income in the year was R\$121.2 million, increasing 72%, mainly due to the 30% improvement in gross income.

Let's go to slide 10, which shows a break-down of our net debt. During 2015, net debt increased 13.9% to end the period at R\$1.09 billion. Note that R\$102 million of this increase was due to the non-cash effect from exchange variation on the dollar-denominated debt. The increase in the net debt is also explained by the growth in the working capital needs generated by the effect on the global currency depreciation on inputs purchased over the course of the year.

Note that this increase in cost will be offset by a proportionate increase in the revenue in 2016. The ratio of adjusted net debt to adjusted EBITDA increased from three times in 2014 to 3.2 times in 2015. Going to slide 11, which shows details of our debt, note that the average debt term increased during 2015, so that (13:23) today 50.4% is long-term

compared to 41% in 2014. Debt in dollar-denominated also declined in 2015 to only 17% compared to 22% in 2014.

I will now pass the call back over to Pavinato, who will comment on the outlook for 2016.

Aurélio Pavinato

Turn please to slide 13, which shows our current projection for yields in the 2015/2016 crop year and a comparison with the performance obtained in the previous crop year. With the exception of soybean, we are keeping unchanged our estimate for the other crops, which are presenting good development and consequently good production potential.

For soybean, we are at the moment concluding harvest for the Midwest region, where yields so far obtained were higher than the initial forecast. However, at the Northeast region, we suffered losses due to lack of rainfall in February. The impact of the drought was more intensive on immature fields, that is (14:47) five years of cultivation, which presents lower fertilization profile and are more susceptible to climate variation.

When we break-down yield performance by region and field maturity, difference become more evident. At the Midwest region, our average yield for mature crops is of 67 bags per hectare, and for younger fields, of 50 bags per hectare. On the Northeast region, even with the lack of rain, mature fields should produce 50 bags per hectare, whereas for immature fields we are estimating only 34 bags per hectare. It's important to highlight that, with the natural maturation of our fields over the next few years, we can expect better stability of production even in years with low rainfall levels.

Let's turn please to slide 14. The table shows our cost per hectare and current crop yields compared to the average cost calculated by CONAB at the regions where we have operations, as well as comparison specifically in the State of Mato Grosso in which we also include the data from IMEA. As you can see in the table, the results of our strong cost management, which is one of our main priorities, seeking to obtain the lowest unit cost possible, which would effectively combine low production costs with high productivity.

Slide 15 shows our currency hedge position for 2016. The average price hedged in dollar for soybean and cotton and the average exchange rate rigidity (17:09) allow us to estimate revenue growth for 2016 of 121% compared to the average increase in production cost of 117%, which allow us to project margin expansion for this year.

Lastly, we would like to leave an optimistic outlook in relation to the upcoming (17:37) 2016/2017 crop year, which is currently on the agricultural planning and input acquisition phase. We see a scenario of stable prices in reals with a possibility of increase depending on the climate and economic conditions and the trend of cost decrease, chiefly on fertilizer and chemicals, given the current moment (18:12) of lower prices for agricultural commodities and oil.

We have already acquired 85% of our fertilizers need for the next crop with a 18% reduction in prices in dollar terms, even considering the low comparison basis of the

previous crop, given we have purchased at the best moments in terms of prices at the international market. Our constant efforts in cost reduction and yield increase reinforce our certainty that we are on the right track towards our Big Dream, to positively impact future generations, being global leaders in efficiency in the agri-business and respect to the planet, as you can see on slide 16.

Thank you, and we'll now start the question-and-answer session.

Q&A

Operator

Ladies and gentlemen, we will now initiate the question-and-answer session. Showing no questions, this will conclude the question-and-answer session. Thank you. This concludes today's presentation. You may disconnect your line at this time and have a nice day.

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