Q2 2020 Earnings Call

Company Participants

- Aurelio Pavinato, Chief Executive Officer
- Ivo Marcon Brum, Chief Financial and Investor Relations Officer

Other Participants

- Guilherme Palhares, Analyst

Presentation

Operator

Good morning, ladies and gentlemen, and thank you for waiting. At this time, I would like to welcome everyone to SLC Agricola to the Second Quarter of 2020 Earnings Conference Call. Today, we have with us Mr. Aurelio Pavinato, CEO and Mr. Ivo Marcon Brum, CFO and Investor Relations Officer. We would like to inform you that this event is being recorded and all participants will be in listen-only mode during company's presentation. After the company's remarks are completed, there will be a question-and-answer session, and at that time, further instructions will be given. (Operator Instructions)

Also, today's live webcast, both audio and slide show, may be accessed through the SLC Agricola website at www.slcagricola.com.br, in the Investor Relations section by clicking the banner of webcast 2Q '20. 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 upon the beliefs and assumptions of SLC Agricola management and on the information currently available to the company. They involve risks, uncertainties and assumptions because they relate to the future events and therefore depend on circumstance 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 will turn the conference over to Mr. Aurelio Pavinato, CEO. You may proceed.

Aurelio Pavinato {BIO 16456795 <GO>}

Good morning. Thank you for participating at SLC Agricola's earnings conference call for the second quarter of 2020.

Let's go to Slide 3, please, where we will comment on our operating performance. This is the end of the soybean harvest, the final yield was 3,900 kilograms per hectare or 8.1% higher than our initial estimate and 19.2% higher than the national average. Note that for the third straight year, we set a new soybean yield record, which is in line with our current strategy to focus on maximizing operating efficiency.

For cotton, with 55% of the area harvested, the estimated yield considering the waiting between the cotton's first and second crop, is 1,761 kilograms per hectare, down 2.5% from the initial forecast, which is explained by the low precipitation. Lastly, for the corn second crop, with 84% of the area harvested, the estimate yield is slightly below forecast at 7,220 kilograms per hectare due to below-average precipitation in the State of Mato Grosso and Mato Grosso do Sul during the flowering and seed-filling phases. Even so, the result is 34% (sic) above the national average for corn second crop published by CONAB already using the data released yesterday by the institution.

Let's go now to Slide 5, where I will comment briefly on the international price of our main products. The second quarter of 2020 registered a recovery in international cotton prices, giving that the supply side responded to lower prices by reducing the planted area in a large hemisphere. On the demand side, the beginning of a recovery already can be observed as economies begin to resume retail activities, albeit, slowly. In Brazil, the effect from the lower prices in dollars was significantly mitigated by the weaker Brazilian real against the dollar. In addition, taking advantage of the expansion in planted area in the '18-'19 crop year, which was harvested in the middle of 2019 and the stability in planted area in the '19-'20 crop year currently being harvested, the AMIA estimated that in 2020, Brazil will export 1.9 million tons, in line with the growth trends observed in the last four years.

Soybean spot prices on the Chicago Board of Trade and the prices paid for the grain based on the Paranagua/CEPEA reference, also staged the recoveries over recent months. The maintenance of the premiums paid and the local currency depreciation enabled soybean price to reach levels above those in same period of last year and more recently, resulted in quotes of over BRL115 per bag according to CEPEA data from -- for Paranagua. In a quarter marked by risk aversion due to the economic slowdown, prices for the soy complex in Chicago showed resilience in relation to the Bloomberg Commodities Index, which registered a decline of approximately 15% in 2020.

The resumption of imports by China, driven by expectation of a recovery in domestic demand in that country has been the main factor sustaining prices, especially after the past cycle marked by the US-China trade war and the African swine fever, which contributed to the scenario of depressed prices for the commodity in international markets.

For corn, international prices currently are down from the same period of last year, reflecting to a large extent the scenario of lower consumption in the United States, which is basically due to the closure of corn ethanol production plants in the country and the resulting increase in estimated ending stocks. In Brazil, however, the market was strong in the first half of the year due to the demand from the animal protein industry and from export markets, supporting to date a continuation of high premiums over prices in Chicago.

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

Ivo Marcon Brum {BIO 16639894 <GO>}

Good morning, everyone. Let's go to Slide 7, which presents some highlights from our income statement. Net revenue grew by 36% year-over-year in the second quarter mainly due to the higher volume of soybean invoices. In the first half of this year, net revenue advanced to 15.8% due to 11% increase in the invoiced volume, combined with the higher invoiced unit price for all crops except cotton. Adjusted EBITDA was BRL145 million, advancing 31% on the second quarter last year. Adjusted EBITDA margin ended the period at 25.7%. The variation in the adjusted EBITDA reflected the growth of BRL35 million in gross income, excluding variation in the Biological Assets. Analyzing the contribution by crop, gross income growth in the quarter was driving by soybean crop, which registered growth in the invoiced volume added by margin expansion. This higher gross income was partially offset by increase in SG&A.

In the first half, adjusted EBITDA was BRL327.7 million, 3.3% higher than the prior year period, with adjusted EBITDA margin of 27.4%. Net income in the second quarter was BRL196.1 million, decreasing 7.5% year-over-year, mainly due to the accounting dynamics of Biological Assets, especially soybean. In 2020, most of the net income attributed to crop was recognized in the first quarter when compared to 2019. This is confirmed by an analysis of the net income in the year-to-date, which grew by 9% on the year on the prior year period to BRL352.5 million. As we have been emphasizing in our communication materials, the accounting dynamic of Biological Assets can shift income recognition between quarters, which means that the analysis of the year-to-date results better reflect the expectation of the given crop year.

To conclude, Slide 8 present our debt position. Adjusted net debt ended the second quarter of 2020 at BRL1.4 billion, representing an increase of BRL487 million from the fourth quarter of last year. Net debt was affected mainly by the higher working capital needs, which in turn were influenced by the higher payments of agriculture inputs for the '19-'20 crop year. Note that this increase in debt is expected for this period of the year, given the financial cycle of the business, given that we are now harvesting of cotton and corn, which will be invoiced in the second half of the year, generating higher operational cash flow.

Gross debt also increased in the period, reflecting the conservative strategy to maintain a comfortable cash position to protect the company from any further economic financial stress caused by pandemic. With the new interest rate scenario, the company raised mainly long-term debt indexed to the CDI rate, which led to a reduction in the cost of the debt with the annual average rate falling from 5% in the fourth quarter 2019 to 3.2% in the first half of this year.

Lastly, I wish to highlight that Annual Shareholders Meeting held virtually on July 30, approved a new dividend distribution of BRL73.7 million which was paid yesterday, bringing total dividend paid in the year to BRL147.5 million.

I'll now pass the call back to Pavinato for his outlook for the rest of the crop year and the next crop year.

Aurelio Pavinato {BIO 16456795 <GO>}

Thank you, Ivo. Let's go to Slide 10, which shows the updated hedge position for the '19-'20 and '20-'21 crop years, already converted into Brazilian real. We made great progress in selling production from the crop year, obtaining prices above the current market and above less crop year based on the amount in local currency. We also concluded our purchase of fertilizers and chemicals for the '20-'21 crop year, with the negotiations leading to significantly lower prices in dollars compared to last crop year. Considering the current scenario of dollar, costs and prices, as well as the level of the FX rate, our expectation is for the good level of profitability to be maintained for 2020-2021.

Thank you. We'll go for [ph] questions.

Questions And Answers

Operator

Thank you. The floor now is open for questions and we will initiate the Q&A session. (Operator Instructions) Our first question is from Guilherme Palhares from Bank of America. Mr. Guilherme, you may proceed.

Q - Guilherme Palhares {BIO 20879946 <GO>}

Hi, Pavinato, Ivo, hope you're all safe. I have two questions from my side. The first one is regarding the mix of crops for the next season, given the outlook that you have already designed for us. How are you thinking about the planning for the production for the next crop? And also, given that we saw this huge forecast bean having expectations lowered? What are your thoughts going forward during this crop? I know that the company is already harvesting a large share of it crops, but do you see any downside risks to users as well? And lastly, a third question here is regarding cost of the current season, when comparing to your first budget last year, how costs are behaving during this quarter? Thank you.

A - Aurelio Pavinato {BIO 16456795 <GO>}

Good morning, Guilherme. About the mix of crops, we are going to announce in October, our planted area for next crop year. But the trend Guilherme is to maintain the share of costs because the soybean profitability is in a good level. The corn has been a profitable crop better than the year before. And so we're going to plant as much as possible corn. And the cotton prices recovered. And when we see the contribution margin of the cotton compared to soybean, normally, it has been higher than soybean. So consider this information, we can say the trend is not to change so much in the share of crops.

About the cost production, as we mentioned, the reduction prices of fertilizer and chemicals is going to help us a lot to reduce our production cost in dollar terms, considering that the real depreciation and all of our real basis cost will be much lower in dollar terms. So our forecast that next crop year, we are going to have a strong reduction on cost in dollar terms. And as you can see, with the pricing level in the market, it give us probably an opportunity to keep good margins over the years.

I don't know if I answered all your questions?

Q - Guilherme Palhares {BIO 20879946 <GO>}

That's very clear Pavinato. And if I may ask about the dollar that you marked your cost during this season, what is the average dollar that you had during this season? And when looking at the next one, if taking the current FX could be a good proxy, so we can estimate cost growth for the next season.

A - Aurelio Pavinato {BIO 16456795 <GO>}

I would like Ivo to answer this hedge position. Ivo, please.

A - Ivo Marcon Brum {BIO 16639894 <GO>}

Okay, Pavinato. So thank you, Guilherme. So, as you know, you have a hedge policy. So accordingly, you are paying the suppliers we started to sell the index for future sales. So less the crop, our dollar basis for the cost was around BRL4 per dollar. In the end of the crop, the crop will have around BRL4.20 because of capital devaluation of real in this process. For the next crop, our position nowadays is around BRL5.20 per dollar. So we have a few payments, I can say, of the suppliers. So when you have the position, you'll sell the dollar. So -- but our idea is to have something around BRL5.20 as a base for the next budget. But you have the definition nearly in the next quarter because we have a meeting with our Board to define our budget.

Q - Guilherme Palhares {BIO 20879946 <GO>}

Okay, that's very clear. Thank you.

Operator

(Operator Instructions) Thank you. This does conclude today's presentation. You may disconnect your lines at this time, and have a nice day.