

Q4 2015 Earnings Call

Company Participants

- Guilherme S. Souza e Silva

Other Participants

- Karel Luketic

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

Guilherme S. Souza e Silva {BIO 15325478 <GO>}

Good morning, everybody. Thanks for following Duratex's fourth quarter results 2015. My name is Guilherme Silva. I am the IR Manager of Duratex.

First of all, please turn to the page number one. And the idea here is to discuss the highlights from this fourth quarter subject theme and the year as a whole. The first highlight is regarding exports, so we increased exports more than 50% in the volume, when you compared to the volume of 2014. So, as you know, this part of our strategy to increase the business out of Brazil through exports plus Tablemac.

The highlight number two is regarding dividends. This year, we announced the payment of 50% over the net profit of 2015 of dividends, okay? By law, normally we pay 30%. Highlight number three is regarding Deca Division. So, in 2015, the margin from Deca Division increased from 17% to 17.7% in this tough scenario that we're facing since the mid of 2014. This is due to the CapEx adjustment that we did in the end of 2014 and some improvement in our mix of products.

And finally, the last one is regarding the capacity utilization. So as you know, we announced in the mid of December, a temporary shutdown of our activities in Itapetininga plant. Itapetininga plant has at around 23% of our total capacity on the Wood Division, basically 500,000 cubic meters of MDF and 400,000 cubic meters of MDP. With this

reduction, we'll reduce a fixed cost, the fixed costs estimated for in this plant is at around BRL 35 million per year. In addition to that, we have the no (02:29) depreciation of the plant, so we are talking about net around BRL 25 million per year. And finally, with this temporary shutdown, we'll improve the productivity in the other four plants on the Wood Division. So we will the increase the occupancy rate of the other plants on the Wood Division.

So, right now please, turn to the next page, page number two. And here, we have discussed the consolidated financial highlights and the net revenues of the company in the fourth quarter and the year as a whole. The net revenues in this fourth quarter of 2015 of Duratex was BRL 955 million. This amount was at around 80% (sic) [around 8%] (03:10) lower than the net revenues in the third quarter of 2015. However, year-over-year, the net revenue was quite stable. The net revenues in 2015, the total was BRL 3.963 billion.

On the Wood Division, the net revenues in this fourth quarter of 2015 was BRL 525 million. In Tablemac, the net revenues in this quarter was BRL 100 million. So it was our record in Tablemac. And in Deca Division, the net revenue was BRL 331 million. So in the picture below, you have the breakdown, the percentage per division. So, Wood Division Brazil represented 55% of the revenues, Tablemac 10%, and finally, Deca Division with 35% of the revenues.

In the figure below, we have our relation between domestic market and foreign market. So the good news is that foreign markets reached 18% in this quarter, right, the fourth quarter 2015. So if you remember, this number in the fourth of 2014 was 10%. And we announced that this time that part of our strategy was to increase the revenue that is coming from out of Brazil through Tablemac and exports. So, our target is to reach at around 30% in the near future.

So, right now, please turn to the next page, page number three. And here, the idea is to discuss the consolidated financial highlights, the volume, EBITDA and net profit of the company. So the Deca volume in this fourth quarter of 2015 was 6.2 million items. The volume was at around 11% lower than the volume in the third quarter of 2015. However, the year as a whole, the volume decreased 2.3% when you include Corona. Without Corona, the volume decreased at around 3%.

On the Wood Division, the volume in this fourth quarter of 2015 was 595,000 cubic meters, the volume was at around 5% lower than the volume in the third quarter 2015. However, year-over-year, the volume decreased at around 10%.

Regarding EBITDA, the EBITDA in this fourth quarter of 2015 was a BRL 185 million. The EBITDA decreased 18%, when you compare it to the third quarter 2015. And in the year as a whole, the EBITDA reached BRL 837 million. So, the EBITDA margin in this fourth quarter 2015 was 19.4%, so in the year as a whole, the average EBITDA margin was 21.1%, and when you compare to the margins of 2014, the margin decreased from 23.9% to 21.1%.

So, regarding the net profit, the net profit increased to BRL 17.2 million (sic) [BRL 76.2 million] (06:13) in this fourth quarter of 2015, basically because we are losing the [ph] all

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benefits (06:18) from JCP, the interest of own capital. This was responsible for BRL 37 million of gain in this fourth quarter of 2015. The net profit in the year, when it compares to 2014, decreased at around 38% from BRL 359 million to BRL 222 million, basically for four reasons: the lower volume; the cost increase, basically energy costs; in addition to that, we have increased our financial expenses due to the Central Bank that we started in the end of 2014 to increase interest rates; and in addition to that, we have a positive fluctuation in biological assets that happened in 2014, and didn't happen in 2015. If you remember, in March 2014, we bought Caxuana's forests. And with this acquisition, we had a positive situation in our biological assets and this didn't happen in 2015, because we didn't buy any new forests last year.

So right now, please turn to the next page, page number four. And here we'll talk about the Wood Division. And we will start with the panel market in Brazil as a whole. The MDF markets, in this year of 2015, decreased 9% when compared to the whole market of MDF in 2014. But when you compare quarter-over-quarter, so fourth quarter 2014 against the fourth quarter of 2015, we decreased more than 21% in terms of volumes on MDF. About MDP, the market as a whole decreased 50% (sic) [15%] (08:06) when you compare with the market of 2014. And quarter-over-quarter, fourth quarter 2014 against the fourth quarter of 2015, the volume decreased 19%.

So, turn to the next page, page number five and the idea here is to discuss the operational highlights of Wood Division of Duratex. So the volume in the fourth quarter of 2015 was 595,000 cubic meters. So this volume was at around 5% lower than the volume in third quarter of 2015. However, when you compare year-over-year, the volume decreased at around 10%. The total volume of Wood Division in 2015 was 2.5 million cubic meters. So in the picture beside, you have an occupancy rate in this fourth quarter 2015. So, on MDF, the occupancy rate was 54%; on MDP, the occupancy rate of 56%; on hardboard, the occupancy rate was 82%. So as you can see, a very low level of occupancy rate, that's why we decide to do a temporary shutdown of our activities in Itapetininga, as I said in slide number one.

So turn to the next page, page number six, here you have the financial highlights of the Wood Division in this fourth quarter of 2015 and the year as a whole. So the net revenues on the Wood Division and this fourth quarter of 2015 was BRL 624 million. The net revenue was at around 80% lower than the net revenues in the third quarter 2015. However, year-over-year, the net revenues on the Wood Division was quite stable. The net revenues in the Wood Division in 2015 was BRL 2.6 billion.

In the picture- beside, you have the EBITDA and the EBITDA margin in this fourth quarter 2015. On the Wood Division, the EBITDA in this fourth quarter 2015 was BRL 138 million. In the year as a whole, the net - the EBITDA in the Wood Division was BRL 595 million. So when you compare 2014, on the Wood Division, the EBITDA decreased at around 18%. Regarding the margin EBITDA, the EBITDA margin throughout the year was 23% in the average. So, that's the end of the Wood Division.

Please turn to the next page, page number seven, and the idea here is to start to discuss Deca Division. So, in the first slide, you have the ABRAMAT index, the building material index of the market - internal market as a whole. So, in this index, in 2015, decreased

12.6%. So, it's a huge decrease. However, Deca's volume decreased only 7%, that's why, we believe that we are gaining market share over the last 1.5 years.

So, turn to next page, page number eight. And here, you have the operational highlights of Deca Division. So, the volume in the fourth quarter of 2015, as I said before, was 6.2 million items. The volume was at around 11% lower than the volume in the third quarter 2015. Year-over-year, the volume decreased 2.3%. However, this number is including Corona. Without Corona, the volume in 2014 against 2015 (sic) [2015 against 2014] (11:41) decreased at around 7%. In the picture beside, you have the occupancy rate. So, on the sanitary ware, the occupancy rate in this fourth quarter 2015 was 56%. On the metal fittings, the occupancy rate in this fourth quarter 2016 was 63%.

So, turning to the next page, about Deca Division, so the financial highlights. So, the net revenues of Deca Division in this fourth quarter 2015 was BRL 331 million. This amount is at around 9% lower than the third quarter of 2015. However, year-over-year, it's important to for mention here that net revenues of Deca increased at around 2%. The total net revenues of Deca Division in 2015 was BRL 1.365 billion.

Regarding EBITDA, EBITDA of Deca in this fourth quarter 2015 was at around BRL 48 million. In the picture beside, you have the EBITDA year-over-year. It's very important to mention here again that EBITDA increased more than 6% year-over-year from BRL 227 million to BRL 242 million. This happened in this tough year, basically due to our better mix of product, and our reduction of our capacity that we did in the end of 2014. In addition to that, as I said in slide number one, that margins increased from 17% to 17.7% in 2015, when you compare to 2014. So, that's the end of Deca.

Let's now turn to page number 10 and the next three slides which cover the CapEx, the corporate debts, and finally, our strategy for 2016. On the CapEx side in 2015, we did BRL 525 million (sic) [BRL 556.2 million] (13:42). Basically, BRL 116 million was from Corona acquisition, BRL 178 million was regarding our CapEx on the forest side. Basically, BRL 10 million was from Caetex, our joint venture with group Caetex in the Northeast of Brazil to plant forests, BRL 20 million was came from Tablemac, the investment on the forest. And the rest was coming from the sustaining of the forest in Brazil. And the rest BRL 260 million was our industrial CapEx right, only for the sustaining of the business. Our forecast for 2016 is to have only BRL 420 million in terms of CapEx basically to the maintenance of the business.

So, turn to next page, page number 11. And here you have our corporate debt composition. So the net debt in December of 2015 was BRL 1.9 billion. This amounted at around BRL 28 million lower than the net debt in the third quarter 2015. However, year-over-year, we increased at (15:01) around BRL 180 million basically due to Corona acquisition. However, the net debt to EBITDA increased from 1.8 times to 2.3 times, basically for two reasons. First of all, as I said before, Corona acquisition, and the other point is, we reduced our EBITDA in 2014 when compared to 2015. However, it's important to say here that we are comfortable with this level of leverage.

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In the picture below, we have the amortization schedule of our debts for the next years. So for 2016, we have at around BRL 500 million in debt, that will expire over this year. However, it's important to mention that we have enough cash to pay all debt of 2016, and the majority of the debt of 2017. We have in cash today more than BRL 900 million, but part of our strategy is to roll over our debt this year.

In the picture below, we have the composition of our debt. So, 62% of our debts are in domestic currency; basically BNDES loans, rural loans and working capital. And 37% is in foreign currency, basically for Resolution 4131. But important to say here that 100% of our debt in foreign currency are hedged to BRL. So we don't have any exposure in other currency than our local currencies, BRL in Brazil and pesos Colombianos in Colombia. This is part of our hedge policy.

Finally, please turn to the last slide, slide number 12. The idea here is to discuss our strategic position for the next years. So in the chart below, we have our capacity evolution. So in both divisions, Wood Division and Deca Division, we've doubled our capacity from 2007 to 2014. For example, on the Wood Division, in 2007, our capacity was 2 million cubic meters; and right now, in the end of 2015, our total capacity was more than 4 million cubic meters. So more than double. On the Deca Division, the movement was the same. In 2007, our capacity was at around 18,000 items; and in the end of 2015, our capacity was 37,000 items. So more than double in the both divisions.

So what were our priorities from 2007 to 2014? So as you can see in the picture above (17:33), to increase capacity through expansion and acquisition, right? So organically and through acquisitions. Point number two, integration between the Duratex and Satipel, the merger happened in 2009. During this period, we've bought more than six companies: ceramics business in the north east, two electronic showers, Tablemac and (17:57). At that time, we are very focused on geographical diversification and product diversification. We are consolidating our corporate governance. At that time, we are very focused to increase market share. And finally, we are focused in the customer service.

Right now, what would be our focus in 2016 and we started using 2015? The point number one and more important one would be our internal agenda. So, basically, we had three external projects that we are doing with our external consulting. Project number one is Duratex Management System. So it's a project that started in the second semester of 2014, (18:43) more focusing (18:45) costs and the review of our process. Project number two is regarding the zero based budget. So, as you know, we started this project in July 1, 2015, more focused in reducing the fixed costs.

And, project number three is regarding our logistic project. So, the idea is to reduce our logistic costs at around 10%. So, the expense for the year at around BRL 250 million. And, the idea over the next year is to reduce 10% of these costs.

Point number two, and a very important one is regarding exports. As I said in the slide number one, we increased more than 50% in terms of volumes in 2015 against 2014. And the idea is to increase more 50% in terms of volume in 2016 when compared to the volume in 2015. So, the idea in the near future is to reach 20% of our revenues coming

from exports in Duratex. Point number three, is regarding our CapEx, our CapEx in 2016 will be only to the maintenance of the business, it will be a sustaining CapEx.

Number four, our integration between Hydra and Corona, the two electronic key business that we have. Point number five is regarding our capacity adjustments. So, as I said in the slide number one, the adjustment of our capacity to reach the new demand that we are seeing in near future, that's why we shut down temporarily the plant in Itapetininga. The last one is regarding M&A, so we have the same strategy on the M&A side, so we're more focused in business related to Deca Division.

So, that's it. Thank you very much for the time. I am open to answer the questions. Thank you.

Q&A

Operator

Our first question comes from Karel Luketic, Bank of America Merrill Lynch.

Q - Karel Luketic {BIO 16467278 <GO>}

Good morning, guys. Thank you for the questions. I have a couple of questions. First, if I may, on the Wood Division on prices and cost. If you may just give us a bit of explanation on what led prices to decline at 2.5% sequentially? Was there a consequence of product or geographical sales mix? Or was it effective price discount? That's the first question.

Second on the cost side, we are seeing cost quite pressured. We saw wood panel cost increasing of over 20% year-over-year. Could you also provide some details in terms of what led to that increase, the dollar or domestic inflation or maybe higher exports, just for us to have bit more of clarity on that? And that's the - on what you just mentioned, Guilherme, in terms of your CapEx for 2016, could you just give us a sense of what's the maintenance CapEx for this year should be more or less, just [indiscernible (21:49) that would be great. Thank you very much.

A - Guilherme S. Souza e Silva {BIO 15325478 <GO>}

Just a second, Karel, please. So regarding the price, the pricing in the second semester of 2015 decreased due to a low - a very low level of demand of the market as a whole. So we followed the market to maintain the same level of market share. Okay?

Regarding the costs, so basically with the lower volume that we had in 2015, we had a low fixed cost in the plant as a whole. In addition to that, we have increased on products linked to US\$ (22:34) and energy costs. Energy cost was responsible for basically more than 30% in terms of our cost increase in 2015. However, it's important to mention that in this year, we are facing a decrease of the commodity price. So, for us in 2016, we are seeing a better condition in terms of cost as a whole.

Q - Karel Luketic {BIO 16467278 <GO>}

Okay. That's perfect. Thank you.

Operator

Our next question comes from Paola Mello, CCT (23:43).

Good morning. Thank you for the opportunity. My question is about capacity utilization in Brazil for wood panel production. The presentation shows that there was a clear reduction in the effective capacity for panels in the market as a whole. I was wondering, if management has a view on whether this capacity decrease is temporary or permanent in nature. What I'm referring to is, if you think that a lot of this capacity would come back on stream, if demand increased, the way Itapetininga (24:15) would be or a lot of those capacity is gone basically for good?

A - Guilherme S. Souza e Silva {BIO 15325478 <GO>}

Just a second, Paola (24:25), please. So Paolo (24:44), on to your question. First of all, so the average coupons rate of the market in the fourth quarter 2015, not only for Duratex, but the average of the market as a whole was between 60% to 65%. Okay? Regarding the Itapetininga temporary shutdown, as I said before, is a temporary shutdown. So, we can restart the plant, as soon as we see an increase of demand. So, we are not seeing this in the short run, but if necessary, we can do that in two months or three months. Okay?

Q - Operator

Okay. Thank you.

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

A - Guilherme S. Souza e Silva {BIO 15325478 <GO>}

So, again, thanks very much to follow Duratex fourth quarter results. So, myself and our team is available to answer any new questions over the next months. Okay. Thanks very much for your time.

Operator

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

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