Q3 2012 Earnings Call

Company Participants

- Edison Ticle de Andrade Melo e Souza Filho, Financial Officer
- Fernando Galletti de Queiroz, Chief Executive Officer

Other Participants

- Aaron Holsberg
- Alan Alanis
- Analyst
- Denis Parisien
- Eric Ollom
- Luciano Coster
- Wesley Brooks

Presentation

Operator

Good morning ladies and gentlemen and thank you for waiting. At this time, we would like to welcome everybody to Minerva's Third Quarter 2012 Results Conference Call. Today with us we have Fernando Galletti de Queiroz, the Chief Executive Officer; Edison Ticle, the Chief Financial Officer; and Eduardo Puzziello -- recorded and all participants will be in listen-only mode during the company's presentation. [Operator Instructions]. The audio and slide show of this presentation are available through a live webcast at www.minerva.com/ir. Slide show can also be downloaded from the webcast platform in the Investor Relations section of the website.

Before proceeding, we wish to mention that the forward-looking statements maybe made during the presentation relating to Minerva's business prospects, operating and financial estimates and goals. They are based on the beliefs and assumptions of company management and on information currently available. 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 Minerva and could cause results to differ materially from those expressed in such forward-looking statements.

I would now like to turn the conference over to Mr. Fernando Galletti de Queiroz, CEO of Minerva, who will begin the presentation. Mr. Queiroz you may start the presentation.

Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Thank you. Good morning to some, afternoon to others. It is my expression that I thank each of you for participating today's in Minerva conference call to discuss the results for the third quarter of 2012.

Let's move to slide two, where we present the highlights of our quarterly results. For the second consecutive quarter, Minerva recorded free cash flow which amounted to R$47.2 million and for the fourth straight quarter we reported positive operating cash flow of R$126.9 million for trailing R$350 million in the 12 months.

We ended the third quarter with an EBITDA of 134.5 million and an EBITDA margin of 11.7%, representing an expansion of 3.1% in relation to the same period of 2011. Note, that this will be highest EBITDA margin since our IPO in 2007 and it reflects the combination of the positive cattle cycle in Brazil and a consistent strategic plan that focus the operation in sourcing cattle in South America, operational efficiencies distribution adjusted through the production capacity and focus on the risk management and strict financial austerity policy.

Other point is that we closed the quarter with a growing revenues of 1.2 billion, 7.6% more than in the same period of 2011. In the last 12 months, growth in revenues increased by 13.1% compared to the same quarter of 2011. Also as a positive highlight our leverage measured by the net debt-to-EBITDA fell to 3.7 times in the last 12 months.

Let's move to slide three, where you can see that domestic beef prices increased 6.9% compared to this prior quarter, reflecting the increase in the prices of grain combine it with the substitution effect caused by the higher price of other proteins. That means that the pressure on the prices is making -- moving in the same direction.

In addition beef exports also increased as compared to the prior quarter. It's worth highlighting the greater pressure on grain prices, in particular corn and soybeans due to the weather condition especially in the United States.

We believe that this pressure should directly affect the price of other protein in the coming quarter, where we and the international peers have the benefit of the prices of beef produced in South America, meaning that Brazil and South America is gaining market share not only in relation to the other beef producers but also in relation to other proteins.

We announced the acquisition of another slaughterhouse, Frigomet located in Asunción, Paraguay and which has slaughter capacity of 1,000 heads of cattle per day. The acquisition consolidates among the market leader in Paraguay which is an important global player in this sector.

I also would like to point at that this conference call our constant efforts should build on mutual ties with our suppliers. Today, we have more than 20,000 cattle producers with 3,000 of our farm suppliers. Partnerships are developed by sharing information and know how which is we discuss between agents. We offer our suppliers a wide range of financial instruments including forward contracts, minimum prices and finance. We also provide market reports from our research team, quarterly results reports specifically to cattle producers, social networks and monthly conference. Our aim is at sharing our expertise in the segment and building our supplier loyalty.

Another point is that regarding MDF operations, our value-added operations, we recorded an excellent result in 2012. The development of new products in partnership with our clients has further strengthened their loyalty. Also the depreciation of Brazilian real benefited the company exports. We expect to continue increasing the capacity utilization rate of MDF, which currently stands at around 65%. We expect to reach a rate of 85% by the end of 2012, and continue boosting the profitability of operation -- sorry 2013.

Lastly, we would like to emphasize that in August we presented to the market Minerva's new visual identity, which now brings under a single concept all the group companies, packaging, fleet and other identification features at the points of sale. The company has since adopted the logo Minerva Foods, an umbrella brand for all of the group's products. The brand restructuring marks another step towards the creation of a single identity to sustain the company's growth.

Moving to slide four, which presents the industry overview in Brazil. We observed in the third quarter of 2012, the confirmed inversion of the cycle, which with an increase in cattle supply despite the scarce rainfall and the beginning of the off-season.

Despite this period of reduced cattle supply, the price of cattle fell by 7.5% in relation to the third quarter of 2011. In the third quarter of 2012, we maintained our focus on exports, due to the lower arroba costs, strong demand from consolidated markets such as CIS, Far East and Middle East countries, and the weakening of the main exporting competitors due to the higher dependents on grains and the higher grain prices. Although, our strategy being to maximize the return of our product mix.

Slide five. Moving on, we present an industry overview for Paraguay. As presented in the chart, the slaughter volume in Paraguay continues to grow over successive slaughters resulting from excellent industry margins, while the lower prices stabilized at a low level.

We would like to reemphasize, Paraguay has been consolidating itself as one of the region's main beef beef producers with the high quality in a competitive slaughters, thanks to smaller and efficient production structure. With our latest acquisition in Paraguay, Frigomet we have underlined our leadership in effect.

Let's look at Uruguay on slide six. We would like to note that although in Uruguay third quarter is also marked by the fiscal seasonal effect with the offset of decreasing the supply of finished cattle, we observe that finished cattle supply especially in July which enables the industry to operate at--margins.

Note that we have beef region highly profitable market to our operation in Uruguay by niche products organic products as implied by the USDA.

Have a look at slide seven shows the operating results. The first highlight is our capacity utilization which stood at around 70%. Note that we remain an industry based market in terms of capacity utilization. Currently we have one of the most modern industrial complex in Brazil with the vast operating - in the sector. Export volumes remains solid as you can see in this chart in the lower right side.

The other segment expanded by approximately 32% in relation to the prior quarter and around 35% compared with the same period of last year, this is by the MDF, Brazil and-operation. It's worth emphasizing that the construction of schedule - behavior in relation to the global economic activities and the cattle products price have increased considerably in international market as a result of the lower slaughter volume in the beef producing counters.

We have recorded a considerable growth in exports, thanks of the weakening of the main beef producing slaughters combining to our focus on meeting the strong demand for top qualitative and in the case with emerging markets.

Note that Frigomet plant in Paraguay together with our FRIASA will allow us to obtain synergies in the combination of global operations. We will--a leading position and consolidating among the market leaders in the country.

Let's move through slide nine. We will comment on our operational results in the domestic market. This slide--increases 7% into domestic market compared to the previous quarter. The increasing chicken and pork prices due to the higher grain prices created a highly favorable scenario for increasing beef margins. Thanks for the decreasing of cattle price and increasing of retail price, in tune with the trends in other proteins.

I will now turn to Edison who will comment on the financial highlights. Edison please.

Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

Thank you Fernando. Good morning everyone. On slide 10, we comment about our financial highlights. As you can see in the chart in the lower left side, reported growth revenues of R$1.2 billion for third quarter 2012 or 8% higher than in the same period last year. We also recorded EBITDA of around 135 million in the quarter, a 50% -- around 50% growth if you compare to the third quarter of 2011.

EBITDA margin increased to 11.7%, an increase of 3.1 points over the same period a year ago and it's important to highlight that these EBITDA margins have a highest margin since the company became listed in 2007.

Moving to slide 11, we show our net income before tax, came to almost R$21 million in the quarter. If you adjust to offset the non-cash foreign exchange, the non-cash currency exchange impact, the currency valuation that we have in the quarter, if we adjust for that non-cash expense, the figure would reach R$38 million.

Let's move through slide 12 to present our cash flow metrics. Minerva again recorded free cash flow, positive free cash flow which reached more than R$10 million in the quarter. If you however exclude the effect from an increase on export in transits that were about to be cleared through letters of credit, at the end of the quarter, our adjusted free cash flow would reach R$47 million in the quarter.

Our operating activities generated positive free cash flow of R$89 million, keeping our solid operating performance into the fourth quarter of 2011. Again, if you exclude the same effect that impacted the accounts receivable line in the working capital, the adjusted operating cash flow would have reached R$126 million.

On the next slide, number 13. We present our capital structure. As you can see in the upper chart on the slide, we closed the quarter with a cash balance of R$920 million which is sufficient for debt amortization that the company has until 2017. Our net debt-to-EBITDA ratio decreased to 3.7 times at the end of the quarter, showing the commitment that the company's management have to the deleveraging process that is taking place in our company.

I will now return the floor to Fernando who will conclude the presentation, briefly discussing the outlook for the sector and the company for the following quarters.

Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Thank you, Edison. The inversion of the cattle cycle in Brazil increased the finished cattle supply and reduced the average price of arroba by 7.1% in the nine months of 2012 compared with the same period of last year. However, the dollar appreciation at the current levels further benefits export margins.

The increasing grain prices accelerated the substitution effect of other proteins for beef prices, weakening our main international competitors. These affects benefited the Brazilian beef prices both in the domestic and international markets in the quarter and is expected to benefit the industry margins in the following quarters.

The continuous growth of the emerging markets in 2012 and 2013 should maintain global demand at high levels. Fourth quarter are seasonally stronger for the beef industry in the domestic market. The consumption of cattle byproducts represents an presents an inelastic behavior in relation to global the economic activities and lowering slaughter volume in the main producing countries have increased their prices have considerably in the international market. This trend, this cycle shall continue for the next -- at least for the next three years as we are seeing on our forecast.

Before going to the Q&A, I would like to talk a bit about one of the disclosure, one information has to be disclosed that Minerva has entered into negotiations with the IFC (International Finance Corporation), that's the arm of the World Bank special projects. The main reason for us to be dealing with IFC is that field that we have on the label that we bring to Minerva or sustainability on governance, on strategy and that makes Minerva a different company, that makes Minerva a unique company in the sector. This is why the project selected by the IFC to be the model for the our industry sector. So Minerva is working together with them. We haven't negotiated the terms. Yes, that can be as our market information reported, there can be some debt in the--or combined instrument, or both. It--in financial terms, but brings a label that is unique for our sector.

Now we can start the Q&A session.

Questions And Answers

Operator

Thank you. We will now start the question-and-answer session for investors and analysts. [Operator Instructions]. Our first question is from Wesley Brooks, Morgan Stanley. Please go ahead.

Q - Wesley Brooks {BIO 16407564 <GO>}

Good afternoon, guys. So a couple of questions from me please. The first one is on the live cattle exports. Obviously a very big improvement by the look of it in this quarter. And it sounds like you had some big shipments quite close to the end of the quarter. Could you just talk about your outlook for that segment, did you see pull forward of volumes from Q4 into Q3, or should we expect this big improvement trend to continue in Q4 and into next year? And then, my second question was around beef and around this chicken versus -- chicken and pork versus beef prices. Are you seeing a clear shift in demand form chicken and pork to beef or is it more just that you're able to price your beef better relative to the falling cattle prices? And if so, which markets are you seeing that shift? Thank you.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Thanks Wesley for the question. And I think first live cattle export is a business that was pioneered in Brazil that's the business that's consistent and actually this is for two reasons. One there are companies go to regions they want to pork, others are companies that are trying to--, so they are importing cattle. And there are companies that having a lot of infrastructure, they want to keep the cattle on as a reserve of proteins. This is a market that Australia has been the major player that is moving ground and Brazil is occupying some ground.

We see it as stable business, not growing but also not decreasing. As you mentioned, there was -- there are big vessels that we do big loads and that was explained that had also affect on the working capital. So, it's a business that we see that is stable with margins that are very similar to the beef -- to the meat margins. But we don't see it growing any share in our revenues.

In relation to beef versus chicken and so pork, the fact is that there is a shift in some countries, specially there is a shift for chicken consumers to consumers that imports lower, cheaper cut, these are examples. Pork order cuts, they are very demanded that this is an indication that they are -- the consumers are replacing chicken by ground beef or meat and beef. This is one indication that we see. The result is that there is an increase, there is a shift, there is an increased consumption and it reflects better prices. So, the increase of chicken and pork affect us by increasing consumption and improving the prices.

Q - Wesley Brooks {BIO 16407564 <GO>}

Thank you very much.

Operator

The next question is from Alan Alanis, JP Morgan. Please go ahead.

Q - Alan Alanis {BIO 15998010 <GO>}

Thank you. Congratulations Fernando on the quarter. Just had a couple of questions. The first one has to do with the selling expenses. We're seeing on the quarter selling expenses increasing by 94%. Could you elaborate a little bit more of what's behind this number and what should be the trend going forward?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Do you want to make all the questions and then I go one-by-one on it?

Q - Alan Alanis {BIO 15998010 <GO>}

No, I don't have that many actually that one in the effective tax rate this quarter was 1%, I was wondering what's behind it. And also some comments going forward. And then I mean what just your overall view in terms of what are your expectations for next year whatever color you can provide? It's simple as that, Fernando.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Okay. Selling expenses, they went up because of increase in the live cattle export. So, freight important part of it, freights in live cattle exports. But if you look that our gross margin went up in the same way. So, that goes back to the question that Wesley made that live cattle exports plays important part for the market basically the same that we have on beef, and they have been increasing due to the lack of competition that we are having from other countries.

Overall, what we see is that cattle cycle gets positive. I see Alan that chicken and pork producers will face new and unknown world because traditionally if you look at the past models when grain price goes up there is a decrease of grain consumption, basically because the chicken producers they launch their chicken as same as pork. But now even if chicken and pork producers own large chicken, they will not have a drastic effect on price of grain because what are the drivers of the price of grain today is the consumption of ethanol. So that means that grain prices will be very in inelastic nowadays, different from what we saw in the cycles in the past. This all reinforce the position that South America has with its natural resources, with its natural advantages of being the main area for producing proteins in general but specially beef that is basically--part of it.

So this is only increasing the stress that located in South America and different countries in South America, in different states in Brazil allows us to arbitrage and to take more strong lead position in the international markets or in the international protein markets.

Q - Alan Alanis {BIO 15998010 <GO>}

That's clear. If I may just go back to the quarter and the live cattle comment that you're making, what would be your view in terms of your market share of exports during the quarter? Because it seems that your volumes for exports which if I'm reading this correctly are up 5% and that includes the live cattle, correct? And the subject data that we get for the full third quarter indicates an increase in exports of volumes that are several times higher than that 5%. So I wonder what happened in terms of -- are seeing some losses of market share in terms of Brazilian exports during the quarter Fernando?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

What we are doing is that Minerva is also focused on segments and Minerva is exporting not only to Brazil, but also to Paraguay and Uruguay.

Q - Alan Alanis {BIO 15998010 <GO>}

Okay.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

On our market share, we do not include the live cattle, that's another market.

Q - Alan Alanis {BIO 15998010 <GO>}

Okay.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Minerva, all its sales, as its market share on export market between 20% and 25%. This is the range that we are always in. And that depends a lot Alan on the sales of the vessels, because different from the competitors, we have our own chart of our own vessels that make a big volumes moving at once. So at the end of the day this can affect the analysis of a single quarter. My suggestion for you is to analyze the LTMs in the last 12 months that we see our consistent growth on our share both on the local market and export markets.

Q - Alan Alanis {BIO 15998010 <GO>}

Got it. I'll take a look at the LTM. Thank you. And just a last question, could you comment on the -- your effective tax rate going forward?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Sorry.

Q - Alan Alanis {BIO 15998010 <GO>}

Your effective tax rate I mean the tax outlook. Basically -- where the question is coming from. Basically you are saying 1% effective tax rate during the quarter. So I am trying to look for a number that we can use to forecast, that's all?

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

For your model Alan, you can use in the next five years, very close to zero, the cash tax payment.

Q - Alan Alanis {BIO 15998010 <GO>}

Okay. Fair enough.

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

Basically because we have a lot of tax credits. After the five years, you can use something between 15% to 20%.

Q - Alan Alanis {BIO 15998010 <GO>}

Got it. That's very, very clear. And again, congrats on the quarter. Thank you so much.

Operator

Our next question is from Denis Parisien, Deutsche Bank. Please go ahead.

Q - Denis Parisien {BIO 20333702 <GO>}

Good morning and good afternoon. Thanks for the call and congratulations for your results. I'm wondering your slaughter volume went down and your capacity utilization went down, your sales volume went up. Were you buying more bone and beef? If so why, or were you running down some work in progress inventory. Could you just give us a little bit more color on that please? And then on the topic of the higher margin or byproducts. Can you give us a little bit more definition on that as how much of that line is leather, how much tallow fat, where is it going. And if you can talk, or give us any more definition on the various line items which ones are generating the most volumes and margin and why and how sustainable that might be in those various segments that would be great? Thanks.

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

Denis the volume of the slaughter is rapidly changing, it has to do with Minerva measures we have in the quarter. But you make an analysis of the volume of sales, it went up significantly. Also it has to do on the Minerva's strategy of not only buying cattle, we can buy cattle or we can buy--to grow that.

So the main thing about Minerva is there is a processing flexibility of using our own cattle or buying--whatever is more economic whatever makes more sense in terms of costs. So you see that there is -- and if you look at the growth of the LTM of 2012 versus LTM of 2011, there is a growth of 36.4%, that indicates that stabilize the curve in few days analyzing a quarter. So it's a clear trend increasing -- utilizing more capacity not only in slaughtering but production capacity. So this is the what -- this is the way that Minerva operates on managing the risk and taking the most economic decision.

Q - Denis Parisien {BIO 20333702 <GO>}

So was there more--available on the market sheet. Is that what we should derive from that?

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

It has to do with people in different regions or the the availability that our competitors had--arbitrage that buying focusing on the region A, not in region B. This is all part of our risk management strategy that we now have.

Q - Denis Parisien {BIO 20333702 <GO>}

Is there any seasonality to that, or it's just purely coincidental and opportunistic?

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

There are some seasonality in some regions, but of course there are all opportunistic opportunities as well.

Q - Denis Parisien {BIO 20333702 <GO>}

And just the chart on page eight of your press release the capacity utilization numbers quite histrically lower than 2Q, '12 and 3Q '11. I'm just wondering going forward into the fourth quarter what should we expect on capacity utilization?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

What happened is that we for 2012 relative to three quarter of -- see the first quarter of '12 we've been adding capacity. That's the new -- the greenfield projects that went into operation. So that's why capacity utilization went down. It's moving up again. And it will be consistently moving up from now onwards.

You are looking at percentage wise, but you'll have to look at the phases that the phases of capacity has increased on quarter versus quarter.

Q - Denis Parisien {BIO 20333702 <GO>}

Can you tell us how many heads did you add of capacity?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Two plants that is--approximately 2,000 heads--figure later on.

Q - Denis Parisien {BIO 20333702 <GO>}

Okay. And will you add anymore capacity in the fourth quarter?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

No, we are already ramping up the initial projects now.

Q - Denis Parisien {BIO 20333702 <GO>}

Okay. So we can expect higher capacity utilization in the fourth quarter I guess?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Definitely.

Q - Denis Parisien {BIO 20333702 <GO>}

Okay. And then can you provide any color on the question that I asked on the byproducts?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Well, the byproducts, this is as we said, in the last, what is happening is that due to the decrease of slaughtering in other parts of the world byproducts in general--, in among others, they are -- the prices are going up. So it's a trend that shall continue and I think it adds more profitability to the operation. Meat and bone meat that has to be situation for grain is also moving up. So, all that makes that we produce more profit.

Q - Denis Parisien {BIO 20333702 <GO>}

Great. Thanks a lot. And just a last one. I know there is only so much you can say about the IFC transaction. But did I hear you say correctly that it would not be very meaningfully large number but you're more interested in the being associated with the IFC reputation wise and obviously the stamp of approval that it gives. But if you were to do debt is there anything that you can say about use of proceeds, would you pay down little debt or would it be more specific for you to use in developing plans, or are they interested in any particular use of proceeds for the financing?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

It was meaningful financially speaking. We are in the IFC project much more for the labels, as I said clearly to IFC because we believe that IFC not only audits but it enhance the level of governance, the sustainability, the strategy of the company. We went through--IFC and increased very positively. It will grow through a public consultation where the IFC will publish from 60 days -- for 60 days opening for the disclosing that doing an investment in Minerva. But the investment will not be a repeat, the investment will not be meaningful or significant in terms of finance of amount of money.

Q - Denis Parisien {BIO 20333702 <GO>}

Great. Thank you so much.

Operator

[Operator Instructions] Our next question is from Alexander Allant, Bank of America. Please go ahead.

Q - Analyst

Thank you. Good afternoon everybody. My question is about financial strategy. I mean Minerva has been posting very good results, leverages falling and will fall until the end of the year, and there is also the possibility of a ratings upgrade on the credit side. However, you do have a some debt in particular a dollar bond which has a very high coupon of 12.25% which is now trading actually at around 8%. So, on the financial strategy side, do you plan to do any liability management exercise, do you plan to may be exchange this bond or do another capital markets transaction? And what else can you do with the debt that you are have in order to reduce the cost?

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

Alexander, Edison speaking. As you know, we are always taking advantage of opportunity to reduce the cost of debt. I'll give example, this quarter, if you take a look, the short-term debt increased a bit, it's roughly because of decrease -- in our debt that we had across around 3% in dollar for one year which is significantly lower than the cost of debt we were seeing this kind line in one year, one year and half when we were at 5% and 8%, 9% of that. So, we are always taking steps to reduce the cost of our debt keeping a comfort liquid position and also keeping a very long-term profile for our debt.

Q - Analyst

Would it make sense for you to perhaps make an exchange of this bond which now appears to be very expensive, and it's a sizeable amount? I mean we are talking about $450 million right of your total debt?

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

But we should take in order to decrease the cost of our debt, would always make sense.

Q - Analyst

Okay. Thank you.

Operator

The next question comes from Eric Ollom, Citi. Please go ahead.

Q - Eric Ollom {BIO 4374335 <GO>}

Yes, hi. Good afternoon I guess everyone and congratulations on the result. My question has to do on the export markets. I think most people are expecting continued strong export pricing, can you just define your expectations a little bit for us for the balance of this year and next year? And also, could you just address the situation in Iran which is a fairly large part of your overall exports? My understanding is shippers are not shipping to

Iran just as a result of these sanctions. Can you just talk about how your product is getting into Iran and what's your outlook there? Thank you.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Great. Export markets have been good and South America is in a situation that there are no competitors for Brazil. U.S. is increasing, the only place that U.S. is increasing is export in for Canada. So the rest of the world will be back for South America just would like. We are seeing a consistent demand for our Middle East, in Africa, North of Africa, Eastern Europe and especially--on the dynamics of the world Australia has been supplying part of the Chinese demand is switching to United States with no chance for Australia to increase its production.

So U.S. though used to be an importer or an exported will be--in quarter next year, according to new FDA. So South America will benefit from--so we'll see a trend of trend that is probably well for these and these are not totally in the equation. There is situation in fact that the higher chicken and pork prices in the international markets in giving Brazil the opportunity just to give an idea today the price competitiveness of Brazil compared to through U.S. is 40%, Brazil is 40% more prices than U.S. on cost production.

So this gives you an--and I'll tell you that two years ago, 1.5 year ago the prices were-so this give you a good indication of how the dynamics will move not only for this year but for -- at least for the next tow years.

The situation gets more complicated because the farmers are in U.S. are decreasing overall female not only cow but also --. So that means that even if there is a change on the quality, it will take three to four years at least to recover. We'll see this effect even more pronounced in 2013 and 2014 because there are few female being slaughtered in U.S. and in Europe, female cows and so this will bring a very, very interesting scenario for South America in 2013 and 2014.

About Iran less than 5% of--next quarter, as we easily replace it by other countries in different regions we are always cautious on how to deal with Iran not only in terms of financial but also in terms of export.

Q - Eric Ollom {BIO 4374335 <GO>}

Okay. I understand what you are saying on the export side and how the U.S. cycle plays into that. But do you just -- I mean do you have any estimates or budget planning numbers that you can share with us in terms of appreciation of the export price. What's your sort of expectations with the percentage increase in beef prices over the next year, or perhaps a range what you think its feasible?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Let's make some very conservative projections, simply projected the pricing will remain stable in dollar terms. With the real appreciation, with the real depreciation makes us much more competitive and increasing our volume. So this doesn't even count on price increase on projections. Account of price stability that makes us to gain market share and to gain profitability.

Q - Eric Ollom {BIO 4374335 <GO>}

Okay, great. Okay. Well, thank you very much. Perhaps I'll follow up with you directly later. Thank you.

Operator

The next question is from Luciano Coster, Credit Suisse. Please go ahead.

Q - Luciano Coster {BIO 20318475 <GO>}

Hi. Thanks for the call. Congratulations on the results. Just had a few questions. Do you guys have any more color on the acquisition in Paraguay? And what is your acquisition strategy going forward? Also, do you have any detail on CapEx plan and how you may possibly fund those plans? And my question on the IFC was answered already. Thank you.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Our CapEx is basically the--CapEx projected for this year and for next year that is around R$25 million for the quarter. And our strategy of growth is always to look at opportunities in South America. Our acquisition in Paraguay presented a good opportunity that produced a deleverage effect in--, because the multiple that we paid was an accretive multiple. And second because one-third of the acquisition was paid that in shares. So this allowed us to add capacity to occupy a more important hold into Paraguay and the industry that's the country that has a big investments on the country side and for the farmers, on genetics, on their techniques of production. That's increased the competitiveness. So this is an indication of how we--this acquisition, but acquisitions are opportunistic, but the--according to our business plan but we are very disciplined on our CapEx, will be $25 million per quarter.

Q - Luciano Coster {BIO 20318475 <GO>}

Alright. Thank you guys. Congrats on the results guys.

Operator

The next question is from Aaron Holsberg, Santander. Please go ahead.

Q - Aaron Holsberg {BIO 16876068 <GO>}

Yeah. Good morning and congratulations on your results. I just wanted to ask it looks like your net debt went up slightly during net quarter again. And since you had positive free cash flow, I was wondering what was happening there?

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

That's currency devaluation that brought non-cash expense that increases the debt. We used part of the proceeds to buy back shares during the quarter. This was the main reason why the net debt went up a little bit, although we generated free cash.

If you want the day of calculation we can give the figures, we can supply to you, you just make a call.

Q - Aaron Holsberg {BIO 16876068 <GO>}

I appreciate. Thank you.

A - Edison Ticle de Andrade Melo e Souza Filho {BIO 15435343 <GO>}

Ratio and also the buyback of shares, operating NII.

Q - Aaron Holsberg {BIO 16876068 <GO>}

Thank you.

Operator

[Operator Instructions]. Our next question is Christopher Vandergrift, Hartford Investment Management. Please go ahead.

Q - Analyst

Wanted to say congratulations on the quarter. This was addressed a little bit, but you guys mentioned in the press release that Brazilian beef producers continue to export more to China. I was wondering can you talk about your expectations for growth in that market? And then two, give a little more color on if you are displacing Australia and any other Asian markets? Thanks.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Yeah. There is a growth -- one of the regions is growing more into the Asian markets that specially because they are going to a more Western style food, fast food chain, food service chain are gaining market share. So they are having more burgers and more sausages. So importance that the market is having is becoming becoming bigger and Minerva is well positioned in that region.

Q - Analyst

Thanks. Is there any more explanation aside about China and expectations for your volume growth there?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

We have more expectations of increasing volume in China. Hong Kong is a channel and Mainland China is another. So there are series of actions in terms of--protocol that is moving, that is making China a more important destination for South American exports.

Q - Analyst

And do you have a time line on that?

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Well it's already happening, it will only be intensified in terms of how to be more important specially because as you mentioned South America is replacing part of what Australia is doing.

Q - Analyst

Thanks.

Operator

Our next question is a follow-up. Denis Parisien, Deutsche Bank. Please go ahead.

Q - Denis Parisien {BIO 20333702 <GO>}

It's okay. My follow-up question was already asked and answered. Thank you very much.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

Thank you.

Operator

Having no further questions, this concludes the question-and-answer section. At this time, I would like to turn the floor back to Mr. Fernando Galletti de Queiroz for any closing remarks.

A - Fernando Galletti de Queiroz {BIO 15387377 <GO>}

In conclusion, we ended the third quarter in an extremely optimistic scenario for the closing of the year and also for 2013. Considering our operating margins expansion, positive cash flow generation due to the confirmed inversion of the cattle cycle and the dollar stabilizing at a level that benefits exports.

The outlook for the domestic market is very positive. Since--a seasonally stronger demand combined with the continued efforts, social mobility and consequently new beef consumers in the market. In this quarter,--the importance of having a distribution system adjacent to our production capacity and our strategy of sales of third-party products focused on small and mid-sized retailers, which complemented sales of our own products.

In the export market, we believe South America is other growing unique momentum in terms of competitive advantage. While the main competitive exporter of cattle are weakening by the weather conditions for--interventions reducing government incentives among other factors, South America has been leading market share consistently with the focus on emerging markets which presents rate above the global average.

Currently we have one of the most modern industrial complex in Brazil with the best operating cattle in the sector. We closed the quarter with 11 important lands strategic located in six Brazil, Uruguay and Paraguay. In Paraguay the development of our industrial complex in recent years. We have adjusted our local and international distribution effort in order to expand in an organized manner adjusting to our operations allowing great flexibility to our sales strategy which enables us to benefit from market opportunities.

Also we are very glad to share our optimism regarding our latest acquisition in Paraguay our new plant is located next to our-plant which will maximize synergies especially cost savings, production planning, capital integration and commercial management. The combination of both operations will guarantee our leading position as we consolidate as market leaders in Paraguay and in South America. --dollar expansion strategy made in South America competitive advantages for cattle rising, Paraguay faced an important--on it.

Lastly, I would like to thank the Minerva team that consistently contribute to the good performance of the company results. Thank you very much for your attention and we remain at our--and with our compromise to generate revenue for our shareholders.

Operator

Thank you. This concludes today's presentation. You may disconnect your line at this time. Have a nice day.