

Q1 2013 Earnings Call

Company Participants

- Antonio Sergio Alfano, CFO, IRO
- Fabio Schvartsman, CEO

Other Participants

- Juan Tavarez, Analyst
- Lucas Ferreira, Analyst

Presentation

Operator

Good morning. Welcome to Klabin's audio conference. At this time all participants are in a listen-only mode. Later we will conduct a question-and-answer session and instructions will be given at that time. (Operator Instructions) As a reminder, this conference is being recorded and also being broadcast live via webcast and may be accessed through website at webcall.riweb.com.br/klabin/english where the presentation is also available.

Before we proceed I should like to clarify that any statements eventually made during this audio conference in connection with Klabin's business outlook, projections, operating and financial targets and potential growth should be understood as merely forecasts based on the expectations of Company's management in relation to the future of Klabin. Such expectations are highly dependent on market conditions, on Brazil's overall economic performance and on industry and international market's behavior. They are therefore subject to change.

With us today in Sao Paulo are Mr. Fabio Schvartsman, Chief Executive Officer, and Mr. Antonio Sergio Alfano, Chief Financial Officer and Investor Relations Director. Mr. Fabio and Mr. Sergio will comment on the Company's performance during the First Quarter. After that they will answer any questions that you may wish to formulate.

Now, I will pass the call over to Mr. Fabio. Please go ahead sir.

Fabio Schvartsman {BIO 2067677 <GO>}

Thank you. Good morning to all. It's a pleasure to have you listening to this conference call regarding results of Klabin in the First Quarter of 2013. And it is -- it is very good for us to be -- actually we are proud to be able to deliver to the market results that are based in very good fundamentals. We had an increase in EBITDA of 23% in comparison to the same quarter of last year. That was no minor thing because actually we have already a

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sequence of seven quarters where the results have been growing continually, and therefore, it's obviously over a much higher basis that we are delivering this 23% growth in EBITDA of the quarter.

More important than that, it was -- it was made with an increase of sales in volume in the Brazilian market by 11%, again a very special performance because the markets in general grew only by 4% in the -- the specific markets of packaging paper grew by 4% only, and Klabin grew by 11% during this period. Besides that we had costs totally under control because costs were not only maintained materially, it slightly reduced during this quarter again.

I know and we -- and we have been questioned about the pulp project that we called internally Puma Project. This project is in its final stages, but it's not ready to be announced yet. There are a number of things that are being treated at the same time. We are -- we can tell you that the financial arrangements are going very well, but besides the financial arrangements we have several other aspects that have to be treated at the same time. For instance, we've been negotiating with the state of Parana a protocol through which the state of Parana will basically be supporting the project. Actually the state will be in charge or will be -- or will reimburse Klabin by the infrastructure investments that will be needed for the project. And we are on the verge of signing this protocol.

I can tell you that for sure that we are going to sign it in May, this May. Therefore, this is another precondition for the project that will be fulfilled. Therefore, we cannot expand too much on comments on the project because we are so close to the final decision. I appreciate and thank you for your comprehension in this aspect.

Regarding what we are expecting for the next quarter, we can anticipate in this quarter that the behavior of Klabin will be quite similar of the First Quarter of this year, in comparison to the same quarter of last year with two meaningful differences. The first difference is the fact that we are going to have the stoppage, general stoppage of Monte Alegre mill in Otacilo da Costa mill during this quarter, this -- the annual stoppage. And therefore, we will have more -- slightly more cost during this period and less capacity available during this period as happened in the same quarter of last year.

On top of that we are stopping our boiler number six. It is a big boiler that we have in the Monte Alegre mill that is in charge of more or less 20% of all the energy that is produced in the mill. And this stoppage will be made for a complete revamp of the boiler. This boiler, to give you an idea is a 30 years old one, and it had stopped the last time 15 years ago. Therefore, once each 15 years we have to stop it and make it -- make a comprehensive service in the boiler. And it will be made in this Second Quarter. It will be stopped for 40 days for this purpose. As a consequence, Klabin will be using more oil during this period in exchange of biomass, and therefore we will have slightly higher costs during this period.

So if you think this apart, operationally wise we see the same kind of evolution in Klabin in the Second Quarter that we are noticing in the First Quarter, especially because now the conditions in the international markets for the products with Klabin are very good as well.

That means that there is almost no difference in this moment to sell in the Brazilian market or to export, meaning that Klabin is -- has a challenge of how to supply all these markets with limited capacity as we have today.

So that was the brief comments that I like -- I wanted to make to you. And now I'm going to pass to Sergio that will comment in more detail what happened during the second -- the First Quarter of the year. Thank you.

Antonio Sergio Alfano {BIO 4337533 <GO>}

Thank you, Fabio. Good morning, everyone, and thank you to participating in our conference call. During the quarter, despite the favorable scenario and the result -- solid signs of economic recovery. During the First Quarter of 2013 packaging paper markets grew in Brazil mainly due to shorter imports of non-durable goods package in corrugated boxes and boards, which were pressured by high exchange rates compared with the First Quarter of last year.

In this quarter, despite the seasonal effects typical of the beginning of the year, Klabin has maintained high domestic sales, an increase of 11% over the same period of last year. This factor together with the (competitive) structured measures of efficiency, it raised the Klabin's results with consistent EBITDA, a growth of 23% compared with the First Quarter of 2012.

Sales volume in the First Quarter, excluding woods, totaled 430,000 tonnes, 3% up from First Quarter 2012. During the First Quarter domestic market sales reached 302,000 tonnes, growing 11% in comparison with the same quarter of last year. Export volumes was 129,000 tonnes, down 12% from First Quarter 2012.

Net revenues including woods total BRL1.1 billion, 10% higher than the First Quarter 2012 due to a better mix and diversified markets. In the -- in Brazil net revenue was BRL812 million, 10% higher, and accounted for 76% of the total net revenues. Even with short volumes net revenues from export was BRL254 million, 9% higher than the same period of last year.

The unit cash cost in the quarter was BRL1,613 per tonne, 1% below Fourth Quarter 2012. Compared to same quarter last year cash cost was down 2% despite -- higher, sorry, 2% (sic; see slide four "3%") higher despite inflation and the labor cost increases during the year.

Adjusted EBITDA was BRL384 million, 20% (sic; see press release "23%") higher compared with the same period last year. EBITDA margin reaches 36%.

At the end of March, net debt was BRL3.1 billion and the net debt EBITDA ratio was 2.2 times versus 2.4 times at the end of December last year.

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Cash and financial investments totaled BRL2.8 billion in the end of March. This amount exceeds the amortizations of loans coming due in the next 33 months. During the First Quarter Klabin invested BRL152 million in the new and forest operations and the capacity expansions of sack kraft paper in Santa Catarina State and the recycled paper plant -- recycled paper plant in the northeast of Brazil. The new corrugator in Jundiai is still undergoing in its learning curve, and we'll continue its operation in the coming months to meet the increasing volume expected for the plant.

The installation of the sack kraft paper machine in Correia Pinto is in line with the budget and the schedule -- and the scheduled. And the equipment began to be installed.

Goiana in the northeast of Brazil unit is going through the preparation of the land and the pipes to receive the recycled paper machine. The capacity of this paper machine is 110,000 tonnes per year. The start-up is scheduled for the middle of 2014.

With these investments which aim to increase paper productivity and efficiency through new and modern equipment, Klabin will remain prepared to meet the demands of its customers with products and services of very high quality.

Now, Fabio and I, we are available to take any questions you may have. Thank you very much.

Questions And Answers

Operator

Excuse me, ladies and gentlemen. we will now begin the question-and-answer session.
(Operator Instructions)

Lucas Ferreira, JPMorgan.

Q - Lucas Ferreira {BIO 16552031 <GO>}

My first question relates to the investment grades. I mean, what is (inaudible) investment grade, what is -- are your plans to reduce your average cost of debt? What is in the pipeline? What can be done? And what do you think would be potential reduction of your average cost of debt after gaining investment grades. And how could that impact on your future projects and the financing of your future projects? This is my first question.

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

Thank you, Lucas, for your question. We had in Klabin an important target to become the company to reach in the company the -- as an investment grade company. And in the last month and the few months ago we received two -- from two agency ratings the investment grade. It's obvious that we will take advantage of that, and we will reach the financial market to explore the advantage to be a investment grade company to swap some investor -- some loans which we consider today too expensive to and swap for a

very lower financial cost. We hope in the future to reach the markets and take the advantage to have this investment grade.

A - Fabio Schvartsman {BIO 2067677 <GO>}

And if I may add, it is very nice on the verge of a big investment project, as we are, to receive this kind of rating because it -- obviously, it helps for the financing of the project of Klabin.

Q - Lucas Ferreira {BIO 16552031 <GO>}

Okay. Thank you. And my second question is related to all the cost cut initiatives that you were doing this year. If I am not wrong, your estimates, your initial estimates were to save something around BRL100 million. That would be the impact in your EBITDA of combining all the cost cut initiatives. So do you keep this estimate? And if yes, if this is to the target, how much of that was captured already in the First Quarter and how much is still pending to be captured in the coming quarters?

A - Fabio Schvartsman {BIO 2067677 <GO>}

Lucas, just to clarify, we don't give that specific guidance on cost reductions. We are actually reducing costs and continuing to do so. Nevertheless, we don't recognize the figure that you mentioned as the one that we are looking for. Nevertheless, it is important to emphasize that all the projects for cost reductions are moving forward, are in good shape. Cost is under reduction right now, especially in the forestry area but in the packaging division as well. And we can see that costs even in Monte Alegre mill are still going up. That means that we have a number of efforts in place. And which we are pretty sure that by the end of the year we are going to deliver a very interesting cost reduction in comparison to last year's.

Q - Lucas Ferreira {BIO 16552031 <GO>}

Yes, great, Fabio. If I may rephrase my question, my point would be if the First Quarter numbers already reflect on an annualized basis the efforts that were implemented, especially in the end of the year with such a bottleneck of the Monte Alegre mill. If Monte Alegre is already running at the rates that you would expect on an annualized basis or -- I think your answer as part of the question is still -- there is still things to happen and still cost cuts to capture throughout the year, right?

A - Fabio Schvartsman {BIO 2067677 <GO>}

Yes. There are. Usually, we target our efforts for the last quarter of the year --

Q - Lucas Ferreira {BIO 16552031 <GO>}

Okay.

A - Fabio Schvartsman {BIO 2067677 <GO>}

-- because we use the beginning of the year for planning what's going to be -- to make a diagnosis, to plan what's going to be execute, to start execution in order to see costs

going down in the last quarter of the year. This is more or less the mechanics. Therefore, what is happening in the First Quarter was the consequence of the cost cutting process of last years.

Q - Lucas Ferreira {BIO 16552031 <GO>}

Excellent. Thank you very much, and congrats for the results.

A - Fabio Schvartsman {BIO 2067677 <GO>}

Thank you.

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

Thank you.

Operator

Juan Tavaréz, Citigroup.

Q - Juan Tavaréz {BIO 15083199 <GO>}

My first question is just to get a better sense of what's expected in the Second Quarter here with these stoppages. Could you give us some guidance in terms of how much of your production will be impacted just by the maintenance stoppage? Then with the revamping of the boiler if you have any sense of how much that can impact your overall cost for Second Quarter?

A - Fabio Schvartsman {BIO 2067677 <GO>}

Juan, this is Fabio. This stoppage is no different from what we had last year. Therefore, you can take more or less the same kind of effect that we had in Second Quarter of last year. It will be similar this year regarding both production availability and regarding the total cost of the stoppage.

The second point that is -- that we have this time, we have this total revamp of the boiler number six, biomass boiler number six of Monte Alegre. That will pass through a big investment. This is -- it happens only once each 10 to 15 years. Therefore, it is a non-recurrent event but we will have it in this quarter. And I already mentioned that the net effect of this will be approximately 3% to 4% of the EBITDA of the quarter. Why is that? Because we are going to have to buy oil instead of using biomass, that is certainly much more expensive for the Company during this period. And it is a 40 days stoppage. And this boiler represented 20% of the capacity of energy of Monte Alegre mill.

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

(inaudible).

Q - Juan Tavaréz {BIO 15083199 <GO>}

And could you give a sense since you mentioned that it will be high CapEx, this revamping. Could you mention how much is this revamping CapEx and remind us what your full year CapEx figure is?

A - Fabio Schvartsman {BIO 2067677 <GO>}

It's approximately BRL50 million, the cost of revamping this, this boiler. It's a big investment --

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

So that is a CapEx --

A - Fabio Schvartsman {BIO 2067677 <GO>}

This will be CapEx, okay.

Q - Juan Tavaréz {BIO 15083199 <GO>}

And what is your full year, could you remind us what your guidance is for full year CapEx?

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

Between BRL700 million to BRL750 million.

Q - Juan Tavaréz {BIO 15083199 <GO>}

Okay. Thank you. And just my -- my last question is just on overall fundamentals, specifically given that you have announced previously some price increases in the market. I'm just trying to get a sense if you're feeling any resistance since there is a lot of discussion around inflation pressures and just curious if you're seeing any resistance from your customers on the implementation --

A - Fabio Schvartsman {BIO 2067677 <GO>}

Juan, nobody likes price increases, that's for sure. Resistance, you can count, that is always there.

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

Yes.

A - Fabio Schvartsman {BIO 2067677 <GO>}

But usually it's an issue of offer and demand, I mean that's not something that Klabin has the monopoly of deciding things but this is just a simple equation. Take for instance what's happening in kraftliner. European kraftliner prices are going up very sharply, and so there is no way of not impacting the domestic market because when you stop exporting and sell in the domestic market you have to -- you have to pass through the price changes that are happening internationally, for instance --

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Q - Juan Tavaréz {BIO 15083199 <GO>}

Okay. Okay. So you're moving fairly okay with the whole implementation phase at this stage?

A - Fabio Schvartsman {BIO 2067677 <GO>}

I suppose so, yes. And as we have capacity limitation, it's -- it obviously helps a lot because --

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

Yes.

A - Fabio Schvartsman {BIO 2067677 <GO>}

-- it's -- end up having a natural selection through prices.

Q - Juan Tavaréz {BIO 15083199 <GO>}

Okay. Perfect. Thank you very much.

A - Antonio Sergio Alfano {BIO 4337533 <GO>}

Thank you, Juan.

A - Fabio Schvartsman {BIO 2067677 <GO>}

Most welcome. Welcome, Juan.

Operator

(Operator Instructions) Ladies and gentlemen there being no further questions I would like to pass the floor to Mr. Fabio for the final considerations.

A - Fabio Schvartsman {BIO 2067677 <GO>}

Well thank you all for joining us in this conference call. As we already told you, we are very happy with the recent results. And again, another aspect that is very positive in Klabin, and that is we have a very clear view of what's going to happen with the Company in the next few months. That helps a lot for planning. It helps a lot for managing. And this allows us to communicate with the market, with -- a more precise way. We are going to try to continue this way. And thank you very much for being with us, and I hope you will join us again next quarter. Thank you, bye-bye.

Operator

This is the end of the teleconference promoted by Klabin. Thank you very much for your participation and have a good day.

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