

Q2 2013 Earnings Call

Company Participants

- Marcelo Martins, CFO and IRO
- Marcos Lutz, CEO

Other Participants

- Alexandre Falcao, Analyst
- Isabella Simonato, Analyst
- Juan Tavares, Analyst
- Paula Kovarsky, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. At this time we would like to welcome everyone to Cosan's Second Quarter of 2013 results conference call. Today with us we have Mr. Marcos Lutz, Cosan's CEO; Mr. Marcelo Martins, CFO and Investor Relations Officer; and Mr. Guilherme Machado, Investor Relations Manager.

We would like to inform you that this event is recorded and all participants will be in a listen-only mode during the Company's presentation. After Cosan's remarks there will be a question-and-answer session for industry analysts. At that time further instructions will be given. (Operator Instructions)

The audio and slideshow of this presentation are available through live webcast at www.cosan.com.br/ir. These slides can also be downloaded from the webcast platform. Before proceeding, let me mention that forward-looking statements will be made under the Safe Harbor of the Securities Litigation Reform Act of 1996.

Forward-looking statements are based on the beliefs and assumptions of Cosan's management and on information currently available to the Company. They involve risks, uncertainties, and assumptions because they relate to future events and therefore depend on circumstances that may or may not occur in the future.

Investors should understand that general economic conditions, industry conditions, and other operating factors could also affect the future results of Cosan and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Martins. You may now begin your conference.

Marcelo Martins {BIO 16440115 <GO>}

Good morning, everyone. I wanted to start the presentation today highlighting the recent changes in our earnings release. We have just formalized our decision to change the fiscal year to match the calendar year; therefore, we're reporting now the Second Quarter of the fiscal year of 2013. This used to be the First Quarter of the fiscal year of the -- of 2014, and we're comparing the Second Quarter with the Second Quarter of what would be the fiscal year of 2012.

We have also adopted IFRS 11, which basically means that from now on we'll no longer consolidate Raizen's results in our balance sheet, which basically means that we will start to report Raizen's investments and results through an equity pick-up line. And to compare the current and the future results of Cosan and Raizen with the past performance of both companies, we decided to do a pro forma where we will continue to basically compare the results as we used to do before the change in the IFRS, in our reporting.

We have also now started to disclose the results of the Lubricants and Specialties business. We have also started to disclose the corporate structure results of the Company and the cost of the corporate structure and the contingencies ex-Raizen and other investments as well.

I would like to now start with the presentation of the consolidated figures for Cosan. We had an increase in net revenues of 18% in this quarter compared to the Second Quarter of 2012, which basically means a jump from BRL7.4 billion to BRL8.8 billion of revenues. We had an increase of 35% in our EBITDA in this quarter coming from BRL616 million in the previous year to the -- to BRL833 million in this quarter. That represents an EBITDA margin of 9.5% compared to 8.3% in the Second Quarter of 2012.

Despite an improvement in all business lines, not only in revenues but in EBITDA as well, the big variance in the exchange rate in Brazil caused a negative impact in the net profit of Cosan on a consolidated basis. Therefore, we actually in this quarter presented a net loss of BRL198 million.

Now, talking about the business lines, different business lines of the Company, we started with -- we'll start with Raizen Combustiveis where we saw a 6% increase in the volumes sold coming from 5.3 billion liters to 6 -- to 5.6 billion liters, net revenues increase of 15% from BRL10.2 billion to BRL11.8 billion, and an EBITDA jump of 14%, representing BRL420 million -- BRL417 million in this quarter compared to BRL367 million in the First Quarter -- in the Second Quarter of 2012.

The EBITDA margin per cubic meter was BRL74 in this quarter compared to BRL67 in the Second Quarter of last year. And we have an EBITDA of BRL77 per cubic meter in the year 2013 so far.

For Raizen Energia we saw a 60% (sic -see slide seven "68%") increase in the volume of sugarcane crushed represented by 18.5 million tonnes coming from 11 million tonnes in the year of -- in this quarter of 2012, of '12. We had an 85% increase in sugar production from

643,000 tonnes to 1.2 million tonnes in this quarter, and a 70% increase in ethanol production from 350 million liters to 595 million liters in this Second Quarter of 2013.

The TSR also went up by 1% coming from BRL120 to BRL121.3 in this quarter. And the volume of energy sold jumped 35% at a price, an average price of BRL170 per megawatt hour compared to BRL167 in the First Quarter -- in the Second Quarter of 2012.

We had net revenues of BRL1.478 billion compared to BRL1.264 billion last year, which basically represented an increase of 17%. We also saw a jump of 30% in EBITDA of the Company of Raizen Energia coming from BRL318 million to BRL414 million, represented by an EBITDA margin of 28%.

In terms of the hedge of the sugar that we export from Raizen we had an average price of \$0.191 per pound, at the end of this quarter for the remainder of the year of -- the crop year of 2013 and '14, at an average exchange rate of BRL2.14. And for the next crop year we had average price of \$0.1821 per pound, at an average exchange rate of BRL2.32.

Now, moving to Comgas, which had its earnings release yesterday, we saw an increase of 6% in the volumes sold from 1.348 billion cubic meters to 1.431 billion of cubic meters. We had an increase of 24% in the gross revenues that reached BRL1.96 billion in this quarter. And an increase in EBITDA of 86%, resulting in BRL314 million compared to BRL169 million in the respective quarter of last year at an EBITDA margin of 19.6% in this quarter.

For Rumo, we also saw a big jump in the volume loaded at the port of 31% coming from 1.5 million tonnes to 1.98 million tonnes, a net revenue increase of 104% coming from BRL105 million to BRL214 million, and an EBITDA jump of 98% coming from BRL43 million to BRL85 million in this quarter represented by a margin of 39.6% compared to 40.8% in the same quarter of last year.

For the business we're starting now to disclose the results, which is lubricants, we had a total volume sold increase of 2%, represented by 78 million liters, a net revenue increase of 6% resulting in BRL386 million, an EBITDA jump of 48% resulting BRL45 million.

We will not consider the whole BRL45 million to be recurring as in this specific quarter we had a reduction in the marketing expenses of the business which will basically be resumed in the next quarter, but in any case, we are providing guidance for the EBITDA of the business so that you have a better idea of what we forecast for this business in this fiscal year.

We had at Radar, a reduction in the net revenues of 43% from BRL35 million to BRL20 million. That basically resulted from a smaller numbers of, the smaller number of farms being sold, but on the other hand the EBITDA increased 44%, jumping from BRL13 million to BRL18 million, and that basically resulted from the increase in the market value of the land portfolio of the Company.

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Now, talk a little bit about the net debt position of Cosan. We saw an increase of 6.9% coming from BRL8.5 billion to BRL9.1 billion. That -- the biggest impact by far was the FX variance in this period of time in this quarter. I would like to emphasize that all the debt at Cosan, except for the Perp has been hedged, and at Raizen we have exports which more than offset the US dollar exposure in the net debt position of the Company. Therefore the results we're seeing here are accounting results and they do not have any financial impact in the Company, but they were sufficient to reduce the profit of the Company, which ended up presenting a net loss of BRL198 million as I have shown before.

We had an exposure in the long-term of 82% of our debt, only 18% in the short term that is there to be refinanced at the subsidiaries level. And next year we don't expect any debt refinancing at Cosan level except if there is an opportunity to reduce our cost of debt which we always monitor. We have recently refinanced, as you know, part of the Comgas facility in the international bond markets with instruments in US dollar and reais, and we don't foresee any other refinancing at the Cosan level, as I mentioned before, except for any opportunity that may eventually come up.

In terms of the net debt to EBITDA ratio, we're at 2.3 times even after the impact of the US dollar variance in the quarter.

There is one comment I would like to make that I skipped basically when I presented the fuels business, the Raizen Distribuidora performance, which has to do with the impact of the aviation business in the business. What we saw was a reduction in the volume of jet fuel sold in the quarter, and that had a negative impact on the growth of the volume of the business overall. But if we basically exclude this impact from the other businesses, we see a growth of 8% in the volume of fuel sold, which comes down to 6% when we include the aviation business.

We see the impact in the aviation business based on what we have noticed in the month of July as a temporary effect. The month of June overall was a very, I would say, bad month in terms of financial performance of -- for the fuel distribution business, but we have seen a market rebound in the month of July.

We have also updated our guidance to the market. We have adjusted the projected CapEx for the overall portfolio in BRL150 million, reducing the range, BRL2.95 billion to BRL3.2 billion of CapEx during this fiscal year. The bulk of the CapEx that was reduced in our projections here comes from Cosan's -- I'm sorry, from Raizen Energia. We have also included an EBITDA projection for the Lubricants and Specialties business, as I mentioned before, in the range of BRL140 million to BRL170 million. And we have also reduced the EBITDA range for Comgas to BRL1.35 billion to BRL1.55 billion as a function of the potential impact that the US dollar variance had and -- or could potentially have in the regulatory account for the gas distribution business.

That's -- well, I just wanted to make an extra comment. We have already set up the dates for our Investors Day in New York and Sao Paulo. In New York, it will be on the 19th of September at the St. Regis Hotel, the same venue we had our Investors Day last year. And for Sao Paulo it will be on the 24th of September at the Grand Hyatt; just (map with a

pencil) these dates in your calendar, and we're hoping to see you guys either in New York or in Sao Paulo.

I would like to turn it back to you now so that you can ask your questions. I am here with Marcos, and we'll be prepared to answer your questions. Thank you.

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Questions And Answers

Operator

Excuse me. We will now begin the question-and-answer session for investors and analysts.
(Operator Instructions)

Juan Tavares, Citi.

Q - Juan Tavares {BIO 21336472 <GO>}

My first question is on sugarcane. First, given specifically that bigger crop has been key here to your operating leverage, I am wondering if the recent frost in the region is impacting your view on the potential output for sugarcane. And second, connected to that, if you can comment a little bit about how you are seeing profitability between sugar and ethanol and whether that is starting to also impact your view on the potential change in mix for the second half of this year.

A - Marcos Lutz {BIO 6779636 <GO>}

Hi, Juan. This is Marcos. First about the frost, we have --- I mean, our view is that we might have a reduction of 100,000 tons in the Carapo mill. That's the only mill that was somehow affected. Just to give a perspective, we crushed about 330,000 tonnes a day. So this is not relevant at all. As I mentioned in the other call in Portuguese, this is a lot less impact for us than a couple of days of rain. So this is really non-relevant.

In terms of, let's say, mix, I mean, we never actually switch the mix towards ethanol. You have always, the start of the crop with more ethanol versus sugar being produced compared to your yearly average because in the beginning of the crop you stabilize the production of ethanol early -- earlier than you would stabilize your production of sugar. So this is the only thing. But we are crushing towards sugar because it is more profitable, because we are very efficient in the exports of sugar as well. So we actually have a price -- let's say method from cost and everything in sugar that is better than ethanol even before the increase in the tax rate. So we are towards sugar.

Q - Juan Tavares {BIO 21336472 <GO>}

And just to clarify a little bit there. So the difference between the sugar and ethanol profitability, are you considering also the, a tax benefit in the ethanol side?

A - Marcos Lutz {BIO 6779636 <GO>}

Yes, I consider everything.

Q - Juan Tavares {BIO 21336472 <GO>}

Okay. And just my second question is on fuel distribution. If you could give us a little visibility on how you are seeing the trend here in the sales mix, if you can give us a sense first in gasoline, are you seeing further penetration of the V-Power gasoline or have we reached the level here that it's somewhat stabilized for the coming months?

And second, just on the other products, specifically on ethanol and jet fuel. Do you see any changes here going forward in terms of maybe higher ethanol, and would this new jet fuel percentage be the new level to look for for the coming months?

A - Marcos Lutz {BIO 6779636 <GO>}

Well first on the V-Power mix, we see further increase in the V-Power mix mainly because we are bringing in to the Shell brand about 400 to sometimes 500 a year in our plan, (white flax). And when you do that obviously you actually have a conversion rate that is not on the same day. So we still are maturing, let's say, gas stations that were converted more recently. So there is a further penetration expected on the V-Power mix.

On ethanol, I don't see a big change in the beginning of the crop because we anticipated when we compared to last year you have more ethanol because you started crushing earlier. But on the overall picture, I don't see that changing much.

And on the aviation thing, this is for us one point that we observe very closely. We don't see that mix last quarter as a trend. This was for us a bad quarter in terms of how the sales behaved. We already saw a strong recovery in July. So I think we will have to watch closely, because if the economy is slower in terms of activity this will be the segment that can have an impact. But again, nothing to be too concerned now, we are seeing actually a recovery at this point.

Q - Juan Tavares {BIO 21336472 <GO>}

Okay. Great. That was helpful. Thank you very much.

Operator

Alexandre Falcao, HSBC.

Q - Alexandre Falcao {BIO 5515455 <GO>}

I have two questions. Actually the first one is how do you see the consolidation scenario on the sugar and ethanol business? There is a couple of three or four rough years for the industry, leverage is high at this point, and you guys have been, have been surfing the wave of consolidation very well in the past cycles. In the next intercrop, do you think there is going to -- there is going to be opportunities out there and you guys are looking for some of these opportunities?

A - Marcos Lutz {BIO 6779636 <GO>}

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Well we always look. We have to say that, I think we believe we are far from a point where consolidation will resume at least with us as consolidated. We don't see the returns on investment that we used to see five, seven years ago. So given that the companies are very leveraged, the negotiation is kind of complicated because the equity portion of those entities is really close to zero. So the negotiation at some point will become a negotiation with banks. And this might be something that can be more promising I would say.

But we are at this point very focused in improving our model and improving the quality of our operations. And this is being a successful move. We have been reducing cost and we are actually switching slowly to smarter models of less capital deployment on the business.

I think at some point further on, but may be more down the road we might be again a player for consolidating this market. We are doing a strong and large homework in becoming more and more efficient and opening the gap towards the average of the industry in terms of cost of operation. So that's our strategy at this point, and not consolidation strategy.

Q - Alexandre Falcao {BIO 5515455 <GO>}

Okay. Thank you. And just a quick follow up. On the logistics side, you implemented an internal change and Julio is now leading the whole logistics and infrastructure efforts for the Company. Is there any news on -- for you guys migrating to new sorts of products, especially on soybeans and grains and fertilizers. Is there any -- is there any development on that front? Thank you.

A - Marcos Lutz {BIO 6779636 <GO>}

Besides the intention there is no concrete disclosable development on those. But what we have done is we are actually developing leadership in the Company, so Daniel actually is now running the Rumo operation, Julio actually is looking on opportunities in the infrastructure business. We will have some interesting bidding rounds for port operations in the next 12 months. We want to be very prepared to be an efficient bidder if something good in terms of assets come to the market. We don't know yet. We are -- we just want to be very well prepared to look on those things.

Q - Alexandre Falcao {BIO 5515455 <GO>}

Okay. Thank you, so much.

Operator

Isabella Simonato, Merrill Lynch.

Q - Isabella Simonato {BIO 16693071 <GO>}

My question is more on the STP deal that you guys just announced. If you could give us more color on the potential you see on the business apart from the new consumers that

might become more users of the shale gas stations, but what in terms of growth going forward and the potential, you being a shareholder of the business, what is the potential that you're seeing there?

A - Marcos Lutz {BIO 6779636 <GO>}

Hi, Isabella. Well at this point we have many initiatives around this move. I think what we have, I mean we have to disclose at this point, is that we have a clear orientation in the Company. We have a good platform to have -- good platform relationship with my final clients. And STP has a fantastic platform. They're really well operated, they are first movers in what they do. And what they do at this point is to have a means of payment for an automobile and a truck. And this is really well-developed by them to basically access not only toll roads but parking in Sao Paulo and other regions all over Brazil.

Those guys have more than 4 million tags already installed in cars and trucks, and those tags are responsible for roughly 60% of those toll road revenues. So again, they have a very deep, I mean, very good penetration on those heavy users. So they are great platform to develop.

On our side, what we want to bring is those automobiles, they basically are users of fuels, lubricants, and toll roads, and gas stations. So at the end -- and then sorry, and parking lots. So at the end, we are kind of complementing that offer and we can actually join -- joining them on the strategy for the Company, but also having raising very a line in terms of bringing offers and products to these people. I mean, we can establish a very good relationship there. It's tough to give a guidance, but basically this is the alignment that we are pursuing now.

Q - Isabella Simonato {BIO 16693071 <GO>}

Perfect. Thank you.

Operator

Paula Kovarsky, Itau BBA.

Q - Paula Kovarsky {BIO 15363001 <GO>}

I wanted to make a follow-up question from the previous caller regarding, I mean, we talked about the views on EBITDA per cubic meter margin for the second half, but can you guys talk a little bit about the volume expectations. I mean, if we look at the first half of the year only it seems to point more to the low end of the guidance and -- but I just wanted to know whether you see additional things that can be done in the second half to perhaps drive the volume growth higher to the midpoint or to the upper part of the guidance. And what are the strategies to do so, perhaps grow beyond the industry, market share gains, what exactly are you guys thinking about?

A - Marcelo Martins {BIO 16440115 <GO>}

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Paula, as you noticed, I mean if we exclude aviation we had an 8% growth in volume in this quarter, which we believe is a very strong growth. And you know well, the first half is given to seasonality, it's not necessarily the reflection of what's going to happen in the second half, which tends to be stronger in volume.

So we think that it's probably not in the lower end of the range, we think it's higher than that. We think that the 8% growth is -- probably in other products except for aviation is a good proxy for growth. And in terms of market share, we don't expect any major moves from what we're seeing now. We expect it to be where it was in the first half of the year.

Q - Paula Kovarsky {BIO 15363001 <GO>}

Okay. And the guidance for 500 and -- 500 to 550 stations this year is maintained or is there room for more?

A - Marcelo Martins {BIO 16440115 <GO>}

No. This is -- that's still the guidance. I mean, what we have to take into consideration that may cause some distortion here is the fact that we're now using the First Quarter of the year as part of this fiscal year, which basically means that we are not going to be able to profit from the full volume of the stations, we're going to converting over time. So on a pro rata basis, the volume will be lower because of the remaining two quarters only. But in terms of number of stations and average volume per station we keep the same guidance we have provided to the market.

Q - Paula Kovarsky {BIO 15363001 <GO>}

Okay. Thank you.

Operator

(Operator Instructions) That concludes the question-and-answer session for investor and analysts. I would like to invite Mr. MarcosÂ Lutz to proceed to his closing statement. Please go ahead, Sir.

A - Marcelo Martins {BIO 16440115 <GO>}

It's Marcelo. Well I just wanted to thank you for participating in our call. I mean, we are -- we think that there was a big improvement in all businesses in terms of net revenues and EBITDA. We basically believe that the volatility in the economic and political environment in Brazil has not impacted our business and we don't forecast any substantial impact in the second half except for the aviation business as we will continue to monitor in the next couple of quarters. But again, we just wanted to thank you again. And I hope to see you at our Investors Day in New York or in Sao Paulo. Thank you.

Operator

That does conclude the Cosan's audio conference for today. Thank you very much for your participation and have a good day.

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