

## Q1 2019 Earnings Call

### Company Participants

- Cristiano Teixeira, Chief Executive Officer, Chief Financial and Investor Relations Officer
- Douglas Dalmasi, Packaging Director
- Flavio Deganutti, Paper Commercial Director
- Jose Artemio Totti, Forestry Director
- Jose Soares, Pulp Commercial Director
- Unidentified Speaker

### Other Participants

- Carlos De Alba, Analyst
- Ricardo Monegaglia, Analyst
- Thiago Lofiego, Analyst
- Unidentified Participant

### Presentation

#### Operator

Good morning and welcome to Klabin's Conference call. At this time, all participants are connected in listen-only mode and later, we will have a question-and-answer session when further instructions will be given for you to participate. (Operator Instructions) As a reminder, this conference is being recorded and also broadcast live via webcast, and it may be accessed at [cast.comunique-se.com.br/klabin/1Q19](http://cast.comunique-se.com.br/klabin/1Q19), where the presentation is also available.

Before we proceed, we would like to clarify that forward-looking statements that might be made during the call related to Klabin's business outlook, projections, operating and financial targets, and potential growth should be understood as mere forecast based on the expectations of the Company's management in relation to the future of Klabin. Such assumptions are highly dependent on market conditions on Brazil's overall economic performance, on industry and international market behavior. Therefore, they are subject to change.

With us in Sao Paulo, we have Mr. Cristiano Teixeira; (inaudible) and other officers of the Company. Mr. Teixeira will be making remarks about the operating performance of the Company during the first quarter of 2019 and afterwards the officers will be the available to answer any questions that you might ask.

Now I would like to give the floor to Mr. Teixeira.

## Cristiano Teixeira {BIO 17567319 <GO>}

Thank you very much and welcome to our call regarding the first quarter of '19. The first quarter is where the flexibility of Klabin is more evident and in the first quarter of '19 things were not different. We delivered more paper in our conversions. We made a priority of profitability (inaudible) repeating the EBITDA of 40% and 5 percentage points higher than the first quarter of '18.

Puma once again showed strength, maintaining a vigorous capacity to generate cash for Klabin. We reduced our leverage. We significantly improved our debt profile, placing Klabin on a safe and sustainable road [ph ]for the financial part establishing the necessary basis for another important cycle of growth. Now I would like to give the floor to Marcus and he will be talking about our figures and then we'll be back to the Q&A session.

## Unidentified Speaker

Thank you, Cristiano. Good morning, everybody, and we start the presentation of the results of this quarter and on slide number 2, you have the highlights. Adjusted EBITDA reached BRL1.5 billion, a growth of 32% vis-a-vis the same period last year and net liability management already executed, but not reflected totally in our position in March 2019, which led the average tenure to 52 month making the Company's balance sheet aggregated for PUMA II.

On the next slide, net revenue in the quarter was BRL2.5 billion, a growth of 14% vis-a-vis the same period last year and the distribution between domestic market and export was kept at the same level of the previous year, exports representing 42% of the net revenue, the total net revenue. As it was mentioned before, adjusted EBITDA for the period was BRL1.5 billion. EBITDA margin reached 40% in the first quarter of 2019, which represents an improvement of 5 percentage points year on year.

On slide number 4, in the pulp business, the volume of sales in the quarter was 353,000 tons, an increase of 13% vis-a-vis the first quarter of 2018. Highlighted the participation of sales to the domestic market, that in the period represented 28% of the overall volume of pulp sales. Net revenue from pulp was BRL921 million, growing by 35% vis-a-vis the previous year.

In the paper business and packaging business, the volume of sales in the first quarter reached 432,000 tons, a reduction of 4% when compared to the same period in 2018. Net revenue in spite of the reduction in the sales volume went up by 6% on the same comparison basis, reaching BRL1.5 billion in the first quarter of 2019.

On the next slide, details about pulp performance during the first quarter of 2019, once again higher than the nominal capacity, reaching a volume of production of 396,000 tons. And for comparison purposes, I would like to remind you that in 2018 the scheduled stoppage occurred in the first quarter and in 2019 the scheduled stoppage will be in July. Production cash cost for pulp, that includes all the fibers produced by Klabin, net of the effect of the stoppage was BRL720 per ton in the first quarter of 2019, an increase in line

with inflation when compared to the same period last year. In US dollars, the cost per ton was \$185, a reduction of 13% comparing on the same basis.

On slide number 6, we can see that in spite of the final exchange rate of the quarter was higher than the final one in the previous quarter, the Company was able to maintain a consistent trajectory of deleveraging, closing March with a net debt to EBITDA of the last 12 months of 3 times, a reduction of 0.1 time vis-a-vis the quarter immediately before, a 0.8 reduction when compared to March 2018.

On slide number 7, Klabin closed March 2019 with a cash of BRL7.5 billion. And besides the Company (inaudible) of \$500 million with a liquidity by the end of March 2019 of BRL9.4 billion. As a result of the liability management process that has already concluded all the transactions such as you can see in the subsequent events of the quarter, but have not reflected on the profile of debt in March 2019. The average tenure of debt went from 48 months at the end of 2018 to 52 months at the end of March 2019, maintaining the same cost levels.

On the next slide, you can see the free cash flow, adjusted free cash flow, dividends and discretionary package was BRL100 million in the first of '19. And this result was pressured by one-off non-recurrent event working capital and financial expenses. The working capital increased in the period by BRL297 million due to the increase in the inventories for the scheduled stoppage for the maintenance of the (inaudible) plants and those are due to seasonality of suppliers and accounts payable that historically are lower at the beginning of the year. The expectation of the Company is that over the year most of the increase in the working capital that occurred this quarter will be reversed.

Financial expenses were impacted by non-recurring costs related to liability management with payment of a (inaudible) in the quarter and also due to the seasonality in interest payment which are not linear between and among the different quarters. Adjusted free cash flow in the last 12 months was 9.6%.

Now going to slide number 9. In April 30, 2019, the Board approved the payment of interim dividend amounting to BRL201 million. In the last 12 months, shareholders remuneration via dividends and interest on equity reached BRL988 million, which represents a dividend yield of 5%.

And concluding the presentation now, Cristiano and the other officers and myself will be available to answer any questions that you might have.

## Questions And Answers

### Operator

Ladies and gentlemen, now we will start the Q&A session. (Operator Instructions) Our first question comes from Mr. Thiago Lofiego from Bradesco BBI.

## Q - Thiago Lofiego {BIO 16359318 <GO>}

Thank you very much. Good morning. I have two questions, the first one has to do with the kraftliner capacity. We know that there are some companies placing new capacity by 2021 in the market and maybe others also claiming additional capacity for the future. How do you see that? Do you have any concerns regarding supply and demand and what about the global scenario that was different from what was expected until a few months ago. And the second question has to do with the project and I would like to understand the announcement of growth that you made. Does it eliminate the possibility of consolidation in other fronts [ph] here in Brazil are not necessarily so?

## A - Cristiano Teixeira {BIO 17567319 <GO>}

Thank you, Thiago. I will answer the part of the kraftliner additional capacity vis-a-vis the market together with Flavio Deganutti. (inaudible) will be talking about some characteristics of the market. But I would like to first mention that kraftliner has been behaving more and more as a friendly solution. Regarding this new world of transformation and packaging and we count not only on the vigorous growth of kraftliner in product that I always mention here during our presentations, like fruit for instance because most of fruits in Brazil are transported bulk, but also all over the world, there is regulation coming on because of sustainable characteristics of the product and (inaudible) etcetera. And because of all that kraftliner will be the big winner in this new wave of more sustainable packaging.

So our belief is very strong in the product. In order to give you figures regarding market characteristics and organic growth, I'd like to ask Flavio to answer.

## A - Flavio Deganutti

Hello, Thiago. Good morning, everybody. We have a major structural growth in these markets and I would like to remind you that Klabin will be making two products in the new machine, the brown kraftliner with 1.2% increase in growth -- in weight and the Klabin project and others in the near future. We will be very well received by the market. And besides, we had even bigger growth in the top line or the white one that goes on top of the brown one and it is not produced in this region, and this is one of the things that is the characteristics that Klabin will be producing and connected to e-commerce and lighter packaging. We will have lighter products than the average, as we said regarding the weight of (inaudible) we see a very important demand for the next two years. And for this reason, we will have a very strong future market. And so on the supply side, we have many announcements of capacity as you well know, however, just a handful of these from the viewpoint of virgin kraft which is our case very high competitiveness and 100% eucalyptus.

Now I will give the floor back to Cristiano and he will talk about consolidation.

## A - Cristiano Teixeira {BIO 17567319 <GO>}

Thiago, thank you for the question regarding consolidation. This is an opportunity for us to reinforce the role of consolidators and the packaging market of Klabin. Klabin now and more than ever with this capacity, Klabin will be looking for a major part of this paper and

integration. Integration proves as you can see in the results of the first quarter and I tried to mention this at the beginning of my presentation, integration in fact is the major flexibility driver for the Company and Klabin, more than ever seeks consolidation in this sector.

**Q - Thiago Lofiego** {BIO 16359318 <GO>}

Could you say a few more words about that, when you say you look at for consolidation in the market, are you going to go after that, after the kraft machine is fully operational, are we talking about something very big or maybe some smaller capacities?

**A - Cristiano Teixeira** {BIO 17567319 <GO>}

Thiago, for some reason I cannot understand your question 100% because the sound is not good. So, I'm going to try to answer but when we talk about looking for consolidation in this sector, this is totally aligned with the demand from the new global brands that work in Brazil, that operate in Brazil and that require more investment in printing and in new types of packaging and packaging systems. And Brazil is a country of continental dimensions and the consolidation characteristics follows the profile of each one of the regions. And Klabin has a vision, it's important to say that it has vision, we seek consolidation in order to better serve the key accounts, the large clients that operate in Brazil, but details, well, they have to do with strategy of the Company and we will not be able to go into that. But what is important is to say that there is nothing already underway and that might oblige us to make any formal remarks and what we have is this vision, Klabin's vision in terms of seeking consolidation in this sector, which is one of the most fragmented sectors in the world still. Thank you.

**Operator**

Ricardo Monegaglia from Santander.

**Q - Ricardo Monegaglia** {BIO 20701786 <GO>}

Good morning. I have two questions, the first one has to do with inventories. Could you talk about this increase in -- how much of this increase is because of the gap between the Puma productions and the sales of pulp in the quarter. And what about potential negotiations for exports of pulp. And my second question has to do with cash generation. It was a little bit worse than estimated because of the higher inventories. Could you give us some more color about the normal cash generation in the quarter. How much improvement should we see in this next quarter. And what about the leverage level when you start to disburse for PUMA II?

**A - Cristiano Teixeira** {BIO 17567319 <GO>}

Thank you, Ricardo. Regarding inventories, well, we have to prepare for stoppages and we have another characteristic that is the end of our contract with the old Fibria and we prepared these inventories in order to comply with our commitment to these inventory spend to get into a normal pace. So, there is nothing special for us to tell you besides what I have already said, that is to say the preparation for the stoppage that start in April. And the second question before the free cash flow, you asked something about pulp and

the sale of pulp. And Jose Soares is going to answer this. He's our Commercial Director for Pulp.

#### **A - Jose Soares** {BIO 17576738 <GO>}

(Technical Difficulty) by Klabin as we announced as of April we started the process of having a gradual volume of direct sales and in April 15,000 tons, in May 13,000, June 45,000 and July, 60,000 tons. In April, we have already realized this and we have already exceeded the volume a little bit because of the inventory that we have built up in order to make direct sales and it requires more inventory in the chain. Sales are going well. We are contracting clients that will be sustaining this volume over 2019.

And we are preparing ourselves for at the end of the year signing the contract for 2020. Things are going quite well and the process as clients already knew, Klabin's fiber showed through Fibria. The qualification process is very fast. Some clients are not familiar with the product yet, but the main players, most of the clients have already tested our product and this facilitates the process of direct sales. And I think this is all I could say.

Regarding the free cash flow, (inaudible) will answer you.

#### **A - Unidentified Speaker**

Ricardo, in relation to the free cash flow of the quarter, the two factors, the line items that had not normal results yet, one was working capital, we have already talked about that and the expectation of the Company is that part of this or a major part of this increase in the working capital that we saw in the quarter will be reverted over the year. And the second line item that had this non-recurring effect was financial expenses. So, BRL53 million in one-off expenses having to do with liability management and the other part, which is a non-linearity of disbursements between the quarters in our financial expenses line. You also asked a question about disbursement for Puma II. Okay. We will start the disbursements for this project by the end of May and the Company's expectation is that still within this year we will have this disbursement of about BRL2 billion.

#### **Q - Ricardo Monegaglia** {BIO 20701786 <GO>}

Very clear. Thank you very much.

#### **Operator**

Our next question is in English. Carlos De Alba from Morgan Stanley.

#### **Q - Carlos De Alba** {BIO 15072819 <GO>}

Good morning, everyone. My question is, you could talk a little bit Cristiano as to the average (inaudible) that the Company had in the first quarter and given the (inaudible) reasons or it probably the main reason for the increase that we saw in the Puma cash production cost, how do you see the evolution in the coming months on that metric. The second question is if you could comment on any further development regarding the negotiations with minority shareholders on potentially buying the royalty of the Company

-- buying the royalty contract or the brand name, the Klabin brand name from the Company shareholders. Thank you.

**A - Cristiano Teixeira** {BIO 17567319 <GO>}

Thank you, Carlos. Our forestry officer is here and if you allow me I would like to have him answer your question. And then I will come back and answer your second question. The first question will be answered by him.

**A - Jose Artemio Totti** {BIO 3014707 <GO>}

There has been an increase in the average wages because we have been buying more wood than we did before and we are preparing ourselves for this new project and most probably in the next few months or the next few quarters, the average wages will continue to be the same as we had in the first quarter. So it was a strategic move in terms of buying wood from third parties and it will be maintained.

**A - Cristiano Teixeira** {BIO 17567319 <GO>}

Now talking about the royalties and I will once again describe the scenario that we have today. The management, myself and the other officers of the Company, we continue with this negotiation in this new period for the acquisition of this contact from the controlling shareholders that own the brand and this negotiation came to good terms at a certain point in time and then it was questioned by minority shareholder. The controlling shareholder, the owner of the brand removed himself from the negotiation and placing us in a situation that we had to cancel the shareholders' meeting. That would make a decision about this. The Board meeting that would be deciding on this matter. And we had worked very hard on this matter and we thought we had reached a good solution, but now we are expecting this is being re-discussed and the discussions will continue in the next two to three months, and with the help of the new Board members, we expect to once again find a solution for that and this will be submitted to our Board of Directors for a decision. So on the Executive Board side we trust that this theme will be solved still within 2019.

But I repeat, it had already a solution and this was interrupted by my counterpart that negotiated this and therefore we are expecting to resume this negotiation as soon as we can.

**Q - Carlos De Alba** {BIO 15072819 <GO>}

Thank you.

**Operator**

(inaudible) is now speaking in English.

**Q - Unidentified Participant**

Hi, thank you. Good morning, everyone. I guess my first question just on pulp, if you can give us an update there on just current demand environment and maybe also if you can

confirm what pulp price are you currently selling in China. And then my second question is regarding your pulp inventories. Could you give us some clarity on what are your pulp inventories today and what will you consider normal. And how do you see the progression of your inventories into the coming months and I know you're taking some downtime. So I'm curious on how you expect that to essentially stay flat during this environment or trending towards what you consider normal, just to get your sense there on pulp inventories as well. Thank you.

**A - Cristiano Teixeira** {BIO 17567319 <GO>}

Thank you, Juan. Soares will answer your question.

**A - Jose Soares** {BIO 17576738 <GO>}

Hello. Juan, the question regarding prices, right now we see stable prices in the market and we have been selling something already, making direct sales and we have 670 to 690 in these with China and it seems to me that this is the price in the market. There is still some pressure on the market. We believe it will continue for some time because the inventories are still high. But in the last report of EVBC [ph], these are already coming down and there is more equilibrium there, but the market still has a degree of instability. Right now our forecast is being around 670, 690 with the market stabilizing at this level. And in the other fibers, the process is quite similar. Of course of fiber ends up having an impact on the other, one goes up and the other one follows and follows the same movement for long fiber or softwood, 690 to 700 and plus around 740s, 730 for the Chinese market. This is the (inaudible) that we see in May -- for May. And the deals are being closed at these levels. And regarding inventories, we saw this move in terms of reduction and it seems to me that demand has a slow reaction that we already see, but already with the favorable trend that we had not seen in the last six months. So slowly we expect inventories to go to normal levels again over time.

**Q - Unidentified Participant**

Okay, great. Thank you.

**A - Cristiano Teixeira** {BIO 17567319 <GO>}

So talking about inventories, I believe that you are asking about global inventories and the information that we will follow. You can see that there has been a call [ph] that was reflected in March, and as far as I know these figures have not been published yet, but regarding Klabin specifically, we have already said that the increase was due to the contract that we referred to and also preparing the Company.

**Operator**

(inaudible) from Bank of America.

**Q - Unidentified Participant**

Good morning, everyone. A follow-up about China to Soares. Because of the contract or determination the Fibria contract, there was an upside in terms of Klabin being able to



capture the smaller clients and when do you expect to mature the pricing strategy? In the first quarter for the domestic market, well, the figures were weak, flat 16% year-on-year. So, could you say towards about this beginning of the year and what do you expect for the next quarters in this regard.

**A - Cristiano Teixeira** {BIO 17567319 <GO>}

Antonio, thank you. Starting with Soares.

**A - Jose Soares** {BIO 17576738 <GO>}

Hi, Antonio, thank you for the question. The strategy that we described is looking for smaller clients and medium-size clients, we continue in this direction. This does not mean that we are not selling to our key accounts. We have a mix, we have the key accounts, the large clients, but limited to a certain volume, but our focus continues to be in terms of looking for smaller clients and medium-size clients, which will give us a better price condition than the average of the market and this strategy is underway. We are doing this in Southeast Asia and China and Europe and even in Latin America and the results are good. We already have in our portfolio clients in this mix that we have designed, that is to say small and medium clients. Of course, we continue to have the key accounts. They are Klabin's clients and other fibers as well and we are getting into them with some volume of hardwood fiber to make out this mix.

**A - Douglas Dalmasi**

Antonio, this is Douglas. The economy was performed below our expectation with 0.8% drop that was published and we dropped something a little bit higher than that on the sack side. We had a strong drop in the domestic market and it was very weak in the first quarter, and we were able to export sacks in order to partially offset this, but the drop was very big in the domestic market, 3% on average between sacks and corrugated boxes, but our strategy was to increase our margin and our revenue went up 4% and we had this really in the last quarter of last year and it is important for us to ensure a stronger profitability mix and in spite of a weaker market we were able to strengthen our margins with price increases and the better mix.

**Q - Unidentified Participant**

Just a follow-up. Thank you. How do you see the situation from now on the market overall?

**A - Douglas Dalmasi**

For the second quarter, our expectation is still similar to the first quarter, no news regarding the domestic market that might strengthen the market in the second half of the year, then we expect the market to be stronger for the domestic market and for Klabin but -- thank you.

**Operator**

(Operator Instructions) The Q&A session is closed. Mr. Cristiano Teixeira will make the closing remarks now.

## A - Cristiano Teixeira {BIO 17567319 <GO>}

Our expectation for the second quarter is that uncertainty about the Brazilian economy might diminish, maybe creating some room for the improvement of the domestic market. We all expect in minimum political stability for us to have some predictability for the public accounts so for investment for employment and for income. This is the expectation of our Brazilian citizens.

Now talking specifically about Klabin, by end of May we will have the general downtime of (inaudible) scheduled downtime. So ex this effect, the pace of result will be quite similar to the one that we have delivered now and I would like to take the opportunity to thank our Board of Directors. The Board of Directors was extremely important in this whole process giving us the guidelines and placing their trust on this executive committee so that we could have the approval of Puma II. So the alignment was evidenced, the alignment between the Executive Board and the Board of Directors and Klabin more than ever is a highly competitive player with global reach, focused on consistent growth and creation of value for all shareholders. Thank you very much and see you on the next call.

## Operator

Klabin's conference call is closed. Thank you very much for participating and we wish you a good day.

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