

Q2 2011 Earnings Call

Company Participants

- Antonio Sergio Alfano, CFO
- Fabio Schvartsman, CEO

Other Participants

- Thiago Lofiego, Analyst

Presentation

Operator

Good morning. Welcome to Klabin's audio conference.

(Operator Instructions) As a reminder, this conference is being recorded.

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 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 behavior. They are, therefore, subject to changes.

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 Alfano will comment on the Company's performance during the first half and the perspective for 2011. After that, Mr. Fabio and Mr. Sergio Alfano will answer any questions that you may wish to formulate.

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

Fabio Schvartsman {BIO 2067677 <GO>}

Thank you. Good morning. Welcome to everybody to our teleconference of results of Klabin for the Second Quarter of 2011.

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I will start making brief remarks regarding three topics -- the evolution of markets in the Second Quarter of this year, the evolution of the results of Klabin in the Second Quarter of this year, plus a brief comment on our expectation for the second half of this year.

Starting with the market, I guess everybody knows -- everybody is aware that the market was weak during the first half of the year, especially during the Second Quarter. It's specifically in the paper industry. We had a reduction in the level of inventories during this Second Quarter in comparison to the growth of increasing inventories in the Second Quarter of last year, the reason being that last year the expectation was of an improvement in the overall economic scenario, therefore, a growth in demand and the opposite was happening during the beginning of this year, therefore explaining why there was this reduction in inventories.

Second, everybody is following the fact that the Brazilian currency has improved or got even stronger with a 4% improvement against the dollar during the Second Quarter of this year, in comparison to the First Quarter of this year -- of last year, sorry. No, no, second against the first. I was making a confusion.

So in the -- because of this combination, the market was truly weak. Looking at the results of Klabin in the Second Quarter, they were affected by two factors -- the exchange rate itself cost us some points in margins and the longer maintenance stoppage in Monte Alegre. That was planned, nevertheless it cost a lot in terms of EBITDA margin during the period.

I want to emphasize that this stoppage had a benefit, because it was successful and in July the industry had already operated with a better level of industrial costs that they used to operate before the stoppage.

And another positive aspect that I would like to emphasize is that Klabin was able to overcome the weakness in the board market in Brazil, that, according to Bracelpa, went down by 12%. Nevertheless, Klabin was able to deliver the same volume this year that we had delivered in the Second Quarter of last year, that is given the versatility of Klabin that allows Klabin to face difficult market conditions.

So a quick remark now about the expectation for the second semester. In the second semester, we will have the benefit of all the stoppages of all of our main plants. Therefore, we are authorized to expect better industrial costs throughout the second half of the year, plus our efforts for cost reductions will start to pay back, closer to the end of the year.

And this can overcome the fact that real will, very likely, remain strong and the market will, very likely, remain weak. Nevertheless, the second half of the year as a seasonal factor that is a better period of the year than the first half. So in the combination all of that, we can expect a better second half of the year, in comparison to the same period of last year.

So with that, I will pass the conference to Sergio Alfano that we will make further remarks regarding the results of Second Quarter.

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Antonio Sergio Alfano {BIO 4337533 <GO>}

Thank you, Fabio. Good morning, everyone.

The first half of this year was marked by continued inflationary pressures on the domestic economy and the weakening of major markets. Brazilian currency continued to strengthen against the dollar and in response to the inflationary pressures, the government announced hikes in interest rates, which directly impacted the domestic economy and revenue from the country's exports.

Klabin increased its sales volume to exports markets during -- in relation to 2010 and in spite the weaker exchange rate, revenue registered growth due to the higher international prices.

In the first half of the year, sales volume, excluding wood, reached 873,000 tonnes, 1% higher than the same period of 2010. Domestic sales volume came to 557,000 tonnes in the period, lower 2% from the first half of last year and representing 64% of the Company's sales mix, while the exports reached 316,000 tonnes, higher of-- 8% higher from the same period of last year.

In the first semester, wood sales volume reached 1.4 million tonnes, 9% lower than the same period last year. Due to the heavy rains in the south of Brazil and the transport problems.

Net sales was BRL1.9 billion in the first semester, representing a growth of 9% from the same period of 2010. Despite the stronger local currency in the period, Klabin's exports revenue was BRL451 million, about \$266 million, and that grew by 11% from the same period of 2010, reflecting the high international price and the better product mix. Net revenue for the domestic market accounted for 76% of total net revenue in the quarter.

Unit cash cost in the quarter was BRL1,742 per tonne, 12% more than the Second Quarter of last year, due to the higher costs with the maintenance stoppage of the Monte Alegre mill. Excluding costs associated with the stoppage, unit cash cost was BRL1,645 per tonne or 2% higher than the same quarter of last year.

Cost of goods sold was BRL773 million in the Second Quarter. In addition to the fixed costs with the maintenance stoppage at the Monte Alegre mill, cost of good sold was impacted by higher consumption of fuel oil in the quarter and higher costs with purchases of wood from third parties.

EBITDA in the Second Quarter was BRL190 million, a margin of 20%. EBITDA in the quarter was impacted by a stronger Brazilian real and the costs with the scheduled annual maintenance in Monte Alegre mill. Excluding fixed costs with the annual maintenance, EBITDA margin fell 3percentage points from Second Quarter 2010. On the other hand, the appreciation of 11% of the real against the dollar in the same comparison period led a contraction of 2percentage points in EBITDA margin.

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In the semester, EBITDA was BRL440 million, with a margin of 23%.

Net income in this period was BRL303 million versus BRL190 million in the same period of 2010.

Gross debt stood at BRL4.6 billion on June 30th, of which 59% was denominated in foreign currency. In relation to December 2010, gross debt declined by BRL273 million and short-term debt accounted for 19% of the total debt.

At the end of June, cash and cash equivalents was BRL2.7 billion, surpassing the amount of short-term US debt by 3.1 times.

Net debt stood at BRL1.9 billion at the end of the period, decreasing by BRL235 million comparing to December 2010.

Net debt to EBITDA ratio declined from 4.4 times in June 2009 to 2.8 times in the end of June 2010 and then in June 2010 at 2.0 times.

Klabin invested a total of BRL209 million in the first six months of the year. The investment made to sharply reduce costs at the paper mills and expanding capacity in the converting plant.

CapEx for 2011 is estimated at BRL500 million.

In Monte Alegre, the new energy transmission line will start up in the Fourth Quarter of this year.

In the Otacilo Costa plant in Santa Catarina state, in addition to the new biomass boiler, which began operating in January, a new operations system will begin operating Third Quarter of 2011.

And in Correia Pinto mill in Santa Catarina, also, a new biomass boiler will be installed in early 2012 and will result in self sufficiency in terms of electricity.

These investments will also generate important cost savings to Klabin.

Investments of approximately BRL100 million to expand production capacity at our corrugated box plants in the northeast in August, now, and in the First Quarter of 2012 in Jundiai in Sao Paulo.

At the plant of Lages in Santa Catarina, an additional line to produce multi-layered bags will expand our capacity by 10%.

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With these capacity increases in our converting plants, Klabin remains ready to meet the demand of its clients with high-quality products and services.

During the second half of the year, Klabin will continue to focus on reducing its leverage to support its future growth.

Fabio and I now are available to take any questions you may have. Thank you.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from Mr. Thiago Lofiego from Merrill Lynch.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Hi, thanks. Just a follow-up question from the Portuguese call. It's about your strategy for your forestry base and your wood business. So over the last year you increased harvesting in your forestry base, basically aiming to replace pine with eucalyptus and, therefore, increase wood volume. So what should we expect, going forward, in terms of wood volumes? And also, if you could give us some color on your forestry base strategy, that would be great? Thank you.

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

Thiago, this is Sergio Alfano speaking. Well we are quite stable in our volume to third parties of logs to sawmills. We are selling, roughly speaking, every year 3 million tonnes per year to the market.

And probably in the future, we are now studying a project in Klabin and we will see in the near term some information about our availability to continue to sell probably this volume, or a little bit lower volumes, of our wood logs to sawmills.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Okay, so that's -- basically, what I'm trying to understand is your volumes were lower versus the First Quarter, your wood volumes. I'm just trying to understand, which would be the normalized levels for wood volumes?

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

Yes. Well our yield in our forest -- in our -- where Klabin is located is so high that I prefer to have available the studies to answer you better in the future. But we hope to continue to supply our customers in the sawmills business.

A - Fabio Schvartsman {BIO 2067677 <GO>}

In other words, Thiago, what we are trying to get a new sense. For the short run, we are able to continue to supply the market with 3 million tonnes per year.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Okay, so 3 million tonnes for 2011 is a good number. 2012, that would be a good number as well?

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

Yes.

A - Fabio Schvartsman {BIO 2067677 <GO>}

Oh, yes. Yes and Yes.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Okay. Great. Thank you.

Operator

Excuse me. (Operator Instructions) Ladies and gentlemen. there being no further questions, I would like to pass the floor to Mr. Fabio for his final consideration. Please, sir, go ahead.

A - Fabio Schvartsman {BIO 2067677 <GO>}

Very good. Thank you, all for being with us during this teleconference and we are happy that we have this Second Quarter without further problems, because we had so many things happening during the Second Quarter that it's good to pass through it and be able to come back to you and say, look, we can now be reasonably optimistic about the second half of the year, because we now have plants more productive. We have less industrial cost. All of our initiatives of cost reduction are starting to pay back -- will start to pay back by the end of the year.

And all in all, we think that we did the right thing, that was to focus the Company on cost reduction in the beginning of this year. That is the reason why we can expect to have a better second half than we had last year.

Having said that, I will hope to have you again on the teleconference of next quarter and thank you, all, for joining us. 'Bye-bye.

Operator

Thank you. This concludes Klabin's audio conference call for today. Thank you very much for your participation and have a nice day.

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