

## Q3 2011 Earnings Call

### Company Participants

- Antonio Sergio Alfano, Chief Financial Officer and Investor Relations Officer
- Fabio Schvartsman, Chief Executive Officer

### Other Participants

- Analyst
- Bruno Montanari
- Tiago Lociago

### Presentation

#### Operator

Good morning and welcome to Klabin's Audio Conference. At this time, all participants are in a listen-only mode. Later, we will conduct the question-and-answer session and instructions will be given at that time. [Operator Instructions]. As a reminder, this conference is being recorded.

Before we proceed, I should like to clarify that any statement eventually made during this audio conference in connection with Klabin's business outlook projections operating and financial target and potential growth should be understood as nearly forecast based on the expectations of the company management in relation to the future of Klabin. Such expectations are highly dependent on market conditions and Brazil's overall economic performance and an industry and international market behavior. They are therefore subject to change. With us today in São Paulo some are Mr. Fabio Schvartsman, Chief Executive Officer; and 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 third quarter and the prospective for the end of the year. After that, Mr. Fabio and Mr. Sergio Alfano will answer any questions that you may wish to formulate.

Now I'll pass the call over to him. Mr. Fabio, please you may now begin.

#### **Fabio Schvartsman** {BIO 2067677 <GO>}

Okay. Thank you. Good morning to everybody and thank you for joining the conference. It is a pleasure to have you all listening to us and especially because the third quarter was a good quarter as expected, confirming for my benefit the capability of Klabin's results.

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As we've been discussing in this several months, I will try to take advantage of this call today to give you a few more details on our cost cutting program. I would like to mention briefly about our pricing strategy. And finally, strategy itself. I will try to make some comments on these.

Starting with costs, Klabin is making a very true effort of cost cutting regarding both variable and fixed costs. Starting with variable costs, they are mainly connected to investments and I would like to explain to you which are these investments for cost cutting.

This year, in February, we started the boiler, new boiler Otacílio Costa. This is a biomass boiler to substitute an oil boiler that we had before. This will now, this is already producing an important benefit since last February.

On June this year, we made unusual big intervention in our boiler 8 in Monte Alegre, the famous boiler that went into the lot of problems during the last years. And this intervention proved very well seeded. So in such a way that we are now in November and since June, when this intervention was done, the boiler. And therefore, the overall Monte Alegre view is working without problems with improved profitability and productivity.

This November, we started, we'll have the first month of full operational evaporation system, a new evaporation system in Otacílio that we'll reduce variable cost as well.

Next month in December, we are expecting the beginning of the operation of the new transmission line of our electricity energy in Monte Alegre. Again, very important benefits for the company.

In next January, we have a couple of investments in our forestry area, basically for harvesting in Santa Catarina, where we are buying machinery in order to do the harvesting ourselves instead of doing through third parties, we've meaningful benefit as well. And we are starting an brand new soil preparation process through heavy machinery in Monte Alegre. Again, there are lot of investments associated with this, a very important reduction in cost.

In June next year, we will start a big boiler, a big biomass boiler in Correia Pinto. It is investment of R\$86 million, a very important cost reduction given the substitution of oil.

And finally, in next September, we will start investment that we produce at debottlenecking in Monte Alegre, through which we will be able to produce more white coat instead of buying it in the market, saving a lot of cost for the company as well.

All these investments together, they add to approximately R\$300 million and they have consolidated return of above 30% in all of them. Therefore, they will be very good for our further results. And the beauty of this is that we will have, they will be entering month-after-month and the results will be improving accordingly.

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Well, the second part of our effort was regarding fixed costs as we anticipated to you in our former calls. We retained INDG, that is a Brazilian institution, very famous here and very useful for cost cutting. But what they really do, they give us a good tool for cost cutting. As you know, tools are only growth if they are well used. And the good news is that our mill Monte Alegre where this work started.

Basically by completely actually this program of cost cutting is proprietary of Monte Alegre mill right now. Therefore, it's being implemented with a lot of energy, with a lot of dedication and very much less stress than is normal in this kind of situation.

They started with this analysis last April, the analytic period went from April to August and we had in September the first month with the system fully operational producing important cost reductions for the company. That we can already see in the results.

The use of was very successful in the company. And because of that, we are bringing in as we speak to start the same kind of work in the corporation center. It will start immediately and therefore in some months, we will see the benefits. It's important nevertheless to emphasize that the kind of cost cutting is that we are able to see in Monte Alegre are of another magnitude than the one is possible in the corporation center.

Nevertheless, it's not less important because I think that is truly important for example that we do the same in the corporation center that we've been doing in the news as well.

Next step for starting next February, we'll be doing the same work in our forestry area. It didn't before because it was necessary to make a full organization, a full restructuring of our forestry area before that. The good news is that this is already done and our forest area is complete and working properly. So this effort will be possible from February on.

Besides that, the other factors of Klabin especially the ones in Santa Catarina. Look at the example of Monte Alegre and actually on their important this system that has been used in Monte Alegre to Otacílio Costa and Correia Pinto. And therefore, we can claim now that we are addressing a 100% of the costs of Klabin in this effort of cost cutting and this is, and the good news is lot of program that belongs to me or just for the main executives of the company but actually is a process that is conducted by the business unit itself with a very good results.

And we would like to say that we have to at moment the effort for our Monte Alegre people specially the Sateri director, Arthur that he doing recent job of motivating his people in this job. And therefore, the work there is going very well as many of the investors could notice when visiting the factory in the late months.

So all of that, I know that you are always very focused in numbers and so let's give you some. I can tell you that the results of cost continuing in the last September was reduced a 5% reduction in the overall cash cost of Klabin. That is a very important the reduction in cost. And I have all reasons to think that this is sustainable in the next months.

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And on top of that, we have all the other efforts towards variable cost cutting that will add to that. And the work of INDG will continue and will produce more improvement in costs. Therefore, Klabin is delivering as we promised a very important cost reduction for the company. Therefore, putting the company in a better situation to face the very challenging international environment that we're seeing right now.

One minute on pricing, Klabin through my initiative is focused in sustaining margins. Therefore, sometimes we've been letting volume down in order to keep margins where we think they should be. This is more real in the packaging sector and in the industrial bags, where we certified some volume in order to sustain margins. And as you can notice in our results this produced the desired effect and we continue to be like this.

The good news on the other hand is the fact that we were able to grow 5% in volume in our board business in Brazil, selling 5% more boards in Brazil in a very difficult scenario where there is a lot of competition from international competitors plus local competitors. Nevertheless, we through this growth sustaining margins, we can say without a doubt that we are very competitive regarding boards in Brazil.

So, one minute about strategy now. As we promised in the beginning of the year, sequentially, we would focus first in cost cutting. This call today is basically to explain the efforts of cost cutting that we have been doing so far and in the sequence, we are going to focusing the strategy. Of course, we are doing this right now. We are very close of putting together a growth strategy for Klabin. I think that in the next months, we will be in a position to share this with you investors and shareholders of Klabin.

We came to do it today right now because we are still in the process of finalizing the analysis and structuring everything in a very cautious way and we'll be prepared to explain and defend it completely for you very shortly.

Thank you and I'm sorry for being so long this time. And now I am going to pass to Sergio Alfano that we will deliver a brief explanation on our results of the third quarter. Thank you.

**Antonio Sergio Alfano** {BIO 4337533 <GO>}

Good morning, everyone.

The third quarter was marked by the dollar hike in September, to the hike level since July 2009. The effect of the dollar appreciation on company's debt was reflected in the quarter, in the quarters negative result.

Nevertheless, it is a pure an accounting effect and does not imply cash reimbursement. Despite the stability of the world economy, consumption in Brazil grew in comparison with the second quarter, reflecting the seasonality of the Brazilian market. In scenario, Klabin once again channeled higher sales volume to the domestic market in the third quarter.

In the first nine months of the year, sales volume excluding wood totaled 1.3 million tonnes, 1% more than in the same nine months period of 2010. Domestic sales are accounted for 66% of the company sales mix and 71% in the third quarter.

Net revenue came into 2.9 billion, 6% higher than the same period of 2010. Domestic revenue grew 6% during the same period accounting for 78% of the total net revenue.

Exports totaled R\$639 million, approximately \$391 million, 4% higher than the same period of 2010, mainly on accounting of the higher international prices and the better product mix.

Unit cash costs of Klabin in the quarter stood at R\$1,644 per tonne against the R\$1,742 per tonne in the previous quarter, when there were additional costs related to the maintenance shortage at Monte Alegre in June.

The cash cost in the third quarter was impacted by non-recurring expenses related cost cutting measures and by the gain from the sale of land in Monte Alegre State. Excluding non-recurring revenues and the expenses in the periods being compared, the unit cash cost in the quarter was R\$1,612 per tonne which is 2% lower than the third quarter of 2010 and 1% lower than the previous quarter.

EBITDA in the quarter was R\$277 million. The best result since the third quarter of 2004 when the exchange rate at that time was R\$2.98 per dollar. EBITDA margin stood at 28%, up 2 percentage points from the third quarter of 2010 and 8 percentage points from the previous quarter. Apart from the reduction of cost, EBITDA growth in the quarter was the result of the higher share of domestic market sales.

EBITDA in the first nine months of the year came to R\$717 million with a margin of 25%. The net result of the quarter was loss of R\$243 million, mainly caused by the foreign exchange variation of R\$501 million, reflecting the impact of the weakening of the real on the company's debt at the end of September. Net debt close to September at R\$2.3 million, an increase of R\$185 million over the balance at the end of December 2010.

The net debt-to-EBITDA ratio which was 3.7 times in September 2009, declined to 2.2 times in September 2010, and close September 2011 to 2.4 times.

Investments, Klabin invested a total of R\$305 million in the first nine months of the year. The investment focused on reduction costs at the paper plants and increasing production capacity in the converting plans. A new power transmission line in Monte Alegre will be operational in the fourth quarter, and cost of plant in Santa Catarina State, in addition to the new biomass boiler for January, February 2011. The new operation system went operational at the beginning of the fourth quarter.

The new biomass boiler at Correia Pinto, Santa Catarina plant has concluded installation of the equipment. We are concluding the civil construction and the installation particularly will be operational at the second quarter of 2012.

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Three investments in this expanding production capacity of the corrugated box unit in São Paulo in Northeast of Brazil and the production capacity of industrial bag unit in Santa Catarina, Klabin will remain prepared to meet the demand of its customers.

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

## Questions And Answers

### Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. [Operator Instructions]. Our first question comes from Mr. Tiago Lociago from Merrill Lynch.

### Q - Tiago Lociago

Good afternoon, thank you for the call. First question, could you give us some color on input cost trends for the coming quarters such as wood and chemical, so could we expect chemical cost in the fourth quarter, and also if you could touch on wood cost trends that would be great, that's my first question?

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

Our raw materials Tiago, especially speaking are quite stable in terms of prices. We are not suffering any impact or pressure in cost, price increases in our raw materials. As prices of food are also quite stable, so was quite stable in the last quarter and we don't have any pressure in terms of suppliers right now.

### Q - Tiago Lociago

Okay. If I may add could you touch also on labor costs for the fourth quarter and may be for 2012, what are the trends you are seeing?

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

Our main plans in our corporate center and also we have our annual agreements in October. Normally, we make provisions during the year to support this salary increases.

### Q - Tiago Lociago

Could you give us the extend of the agreement in October I mean...?

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

No, it's being negotiated right now, Tiago. We don't have till now a final decision between the unions and all the syndicates.

### Q - Tiago Lociago

Okay. And then that should, that will have an impact in the fourth quarter, right?

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

No because we made how the provisions for labor you see in our numbers.

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

Tiago, obviously there is an impact in the sellers themselves. But just on the sellers, just a portion of it.

**Q - Tiago Lociago**

Yeah. Okay, clear. Thank you. My second question is could you provide a breakdown of your EBITDA margin or EBITDA evolution in July, August and September, so basically to understand how margin and how your EBITDA generation evolved during the third quarter?

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

You are talking about by month?

**Q - Tiago Lociago**

Yeah July, August and September for the breakdown performance per month.

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

We have let's say in September already that was R\$110 million, in August 87. Then the remaining I have August and then September 277 minus 110 minus 87, you have 80 million in July, 87 in August and 110 in September.

**Q - Tiago Lociago**

Okay. Thank you very much. Do you have the EBITDA margin as well?

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

No we don't have right now.

**Q - Tiago Lociago**

Okay.

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

Okay.

**Q - Tiago Lociago**

Great. Thank you very much for your.....

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

Okay.

## Operator

Excuse me. Our next question comes from Mr. Bruno Montanari from Morgan Stanley.

### Q - Bruno Montanari {BIO 15389931 <GO>}

Good morning. Thanks for taking my question. Going back to cost cutting initiatives, I was wondering the cycle of the cost cutting muchso we just try to capture all the benefits within 2012 or is this a more medium long-term affect in the company's results? Thank you.

### A - Fabio Schvartsman {BIO 2067677 <GO>}

If I try to explain, we are going to do it step wise because, we're taking the fixed cost. We are starting with reductions in our Monte Alegre mill. They started in September and they will continue for several months till they stabilize in their final level, then we will start with the corporate center, then we will start with the forestry. At the same time, we are starting in the Santa Catarina mills.

Therefore, it will--the main benefit is coming from Monte Alegre as we have said to you. There are other benefits that we will be adding to this throughout the year. In the variable cost, since it's based on the each investment, when each investment starts, we immediately will start to have the benefit of the cost reduction. So till the end of 2012, we will have all of these things that we've been discussing, certainly in our results. But they will do month-after-month to get there.

### Q - Bruno Montanari {BIO 15389931 <GO>}

Alright. Thank you. And if I may have a second question. Could you comment a little bit on the outlook for coated board demand in Brazil in the fourth quarter of 2011, please?

### A - Fabio Schvartsman {BIO 2067677 <GO>}

What about?

### Q - Bruno Montanari {BIO 15389931 <GO>}

Coated boards.

### A - Fabio Schvartsman {BIO 2067677 <GO>}

Coated board. As I said in the Brazilian call, we expect October, November as regular months without any specific change in comparison to September. And in December is always a question mark because it depends on--and there's holidays and several other companies stop buying in the middle of the month, because they go into vacation. So it depends on how the market we will react precisely there, that I cannot anticipate at this point. But usually December is weaker than October, November.



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**Q - Bruno Montanari** {BIO 15389931 <GO>}

Alright. But is it fair to expect an year-on-year improvement similar to what we saw in the third quarter, for the fourth quarter?

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

Specifically I cannot, I didn't look at the numbers in this way. Therefore, I wouldn't be able to deliver a quick answer for you.

**Q - Bruno Montanari** {BIO 15389931 <GO>}

Alright. Thank you.

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

You're welcome.

**Operator**

Excuse me. Our next question comes from Mr. Andrea Damaro from Itau BBA.

**Q - Analyst**

Good morning, Fabio and good morning, everyone. Congratulations again on the strong results. I have two quick questions, here is my first question. I would like to ask what is your expectations in terms of wood sales for 2012?

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

Well, wood sales will continue in the same level of 2011. I don't see neither improvement nor reductions with comparison to this year. Nevertheless, the overall economy is weak. You remember that we saw, we are selling logs to, some logs that are aiming the international market I mean international markets weak. I don't know exactly what to expect. At this point, we are forecasting a maintenance of the level that we have in 2011.

**Q - Analyst**

Okay, great. And as my second question I would like to ask what do you see in terms of the kraftliner price trends in the short-term?

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

The international kraftliner prices are very weak because of the weakness of the both American and European market, specially the European. Therefore, people, several of the companies that produce kraft in the world and they that are short in cash for some reason or another. They have to sell and they are pressuring prices down. But we think that is just for the short-term, we don't expect this to continue because it's just an issue of the-- We expect the situation to stabilize and recover in the beginning of next year.

**Q - Analyst**

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Okay great. Thank you for answering my questions.

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

You are welcome.

## Operator

[Operator Instructions]. Excuse me. There being no further questions, I would like to pass the floor to Mr. Fabio for his final consideration.

**A - Fabio Schvartsman** {BIO 2067677 <GO>}

Well. Ladies and gentlemen, thank you for joining our results call. And I am very pleased with the results that we have been delivering so far. It's important that we initiated cost reduction that we have investing heavily on during this year. I know that everybody was expecting something like it. And thank you for your patience and thank you for the positive analysis that several of the analysts of the self side have already made on our results. This increases our responsibility and that's okay, that's how we see it.

And regarding strategy, thank you for giving me the opportunity of developing it further and to be able to deliver with all the details in the near future, in a way that it will be sustainable.

So, I'm very pleased with the evolution of being so long and thanks for having you once part. Thank you, have a good day.

## Operator

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

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