

Q4 2012 Earnings Call

Company Participants

- Antonio Sergio Alfano, CFO, IR Director
- Fabio Schvartsman, CEO
- Unidentified Speaker, Unknown

Other Participants

- Juan Tavaréz, Analyst
- Lucas Ferreira, Analyst
- Marcos Assumpcao, Analyst
- Thiago Lofiego, Analyst
- Unidentified Participant, 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 the time. (Operator Instructions) As a reminder, this conference is being recorded.

Before we proceed, I should like to clarify that any statements eventually made it during this audio conference in connection with Klabin's business outlook, projections, operating and financial targets. And potential growth should be understood as merely forecast 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 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 Alfano will comment on the Company's performance during the Fourth Quarter and the perspectives for the year. After that, Mr. Fabio and Mr. Sergio Alfano who will answer any questions that you may wish to formulate. Now, I will pass the call over to him. Mr. Fabio, please begin.

Fabio Schvartsman {BIO 2067677 <GO>}

Thank you. Good afternoon to all. Welcome to our Fourth Quarter results conference and well I would like to start. I cannot avoid to say that we had a very good year in 2012 with EBITDA growing 31% during the year and take in to consideration that the year was a weak one for the Brazilian economy and the world economy.

That means that Klabin was able to deliver that kind of performance even without any help from the economic environment. After that, I would like to make a quick consideration on the overall process that Klabin is following.

Starting in 2011, Klabin began with its main factory or main mill in Monte Alegre with a process of cost cutting that start to deliver results in the Fourth Quarter of that year and all of the year of 2012 was benefited by it -- from it. And on top of that, in 2012, we initiated a process to reduce costs in the forestry department that again, started to deliver good results in the end of last year by the time we were already at a level of 10% below in cost terms that we were a year before.

So it means that the process is paid back in the forest department and I would like to emphasize that was given the effort of the forestry officer, Mr. Totie and all his team, that they were basically in charge or responsible for these improvements in the operations of the Company.

The good news is that this will benefit all the year of 2013 and they are now initiating a new round towards cost cutting in the forestry department that we will probably deliver another amount of cost cutting that will be similar to the amount that we were able to get last year.

On top of that, we are initiating as well, an effort of cost cutting in our packaging area where we have an overall cost basis of roughly BRL400 million in which we are going to deliver cost cutting by the end of this year.

So, then we -- as a consequence of that, we had an important evolution of the results of the Company in 2011, another important evolution in 2012, in a combination with cost cutting and improvement in sales mix that resulted in better performance and better EBITDA for the Company. And in 2013, we again hope to have a combination of another round of cost cutting plus further improvement in our sales mix because we are now witnessing an improvement in the demand in the Brazilian domestic market.

In 2014, we'll have a number of new investments coming on stream. The sack kraft machine with 80,000 tons a year that will start in the end of 2013 and in the middle 2014, we will have the recycled paper machine that we will start operation and we are planning to have a debottlenecking of one of our board machine by the mid of 2014, again improving our capacity and therefore improving our capacity to deliver better results.

In 2015, we are expecting to have our pulp project in full operation, therefore, another jump in the results of the Company in 2015. And in 2016, our expectation that we should have a new board machine coming on stream. So all in all, it means that Klabin is now shifting from a total focus in cost-cutting and mix improvement into growth that where we

think that Klabin will continue to deliver improvement and results year after year in the next few years.

As I mentioned the pulp project, right now, I would like to make a quick comment on that. We are in the process of raising capital for this project. This project is following normally the plans that were made. We are committed to have the startup of this plant in 2015 and we are not only in this capital raising process but we are in the process of the optimization of the project itself in order to have the best possible project.

It's very important to emphasize that in all of our studies we could see that the return on investment is very nice. Therefore, the main issue here is to have the best possible balanced approach to financing it where we are now spending a lot of effort and time and things are moving forward normally. We didn't finish yet. That's the reason why we are not announcing the project yet.

So, one last comment about the First Quarter of 2013, I told you in the beginning of this comment that results in 2013 will be better from 2012 and immediately in the First Quarter, this will become clear because we are facing now a very strong First Quarter. So strong that in spite of the weak seasonality of this First Quarter, we plan and we expect to deliver our results in line or even better than the Fourth Quarter of last year.

Therefore, much better of First Quarter of 2012, showing that Klabin will be operating in a new standard of results as I mentioned.

So, with that, I'm going to pass to Sergio that will make further comments on our performance of last year. Thank you.

Antonio Sergio Alfano {BIO 4337533 <GO>}

Good morning, everyone. Thank you for participating in our conference call. In 2012, expectation of our recovery in global economy was frustrated and in Brazil, GDP growth was lower than in 2011. And industrial production fell by 2.7%. Even with the unfavorable economic environment and weak markets in Brazil and abroad, Klabin had its best performance due to a combination of reduced costs, the increased deficiency of the mills. And it proved product and sales mix.

Sales volume in 2012 excluding would total 1.7 million tons down 1% from 2011. In 2012, the Company exported 544,000 tons down 7% from 2011. In the domestic market, the sales volumes was 1.2 million tons, 3% higher. Net revenue including wood total BRL4.2 billion, 7% higher than in the previous year even though sales volume remained flat in the same period due to a better mix of diversified markets.

In the domestic markets, the net revenue totaled BRL3.2 billion, 5% higher than 2011 and accounted for 76% of the total revenues of the Company. The export was BRL995 million, 14% higher than 2011. The unit cash cost was only 1% higher from the previous quarter. The intensification for the cost reduction initiatives in the forestry area which started to appear

in September was partially offset by the impact of the collective pay on labor costs as of October 2012.

Adjusted EBITDA was BRL384 million in the quarter, 20% higher than the same period of last year. The EBITDA margin was 35% reflecting the sustainability of the Company's improvement programs. In 2012, adjusted EBITDA reached a record of BRL1.4 billion, 31% higher than the previous year. Consolidated net debt was BRL3.3 billion and the net debt to EBITDA ratio was 2.4 times in the end of 2012 from 2.5 times in the end of 2011.

Cash and financial investments stood at BRL2.8 billion in the end of the year. This amount exceeds the amortization of loans coming due in the next 33 months. The Company continues its focus on process optimization in order to generate efficiency gains and the reduced operating costs as well as social environmental impacts, maintaining a proper capital structure and debt profile.

We conclude with some industrial improvements projects such as the new biomass boiler in the Correia Pinto mill which began operation in May and the debottlenecking of the bleaching line in Monte Alegre mill with a focus of increasing bleached pulp capacity which we started operations December last year. These two projects will reduce operating costs of the Company in 2013.

We acquired a new corrugator in the Jundiá-DI plant for our box plants with the annual capacity for 100,000 tons per year. A sack kraft paper machine with an annual capacity of 80,000 tons we will start up in the final quarter of 2013. And the new recycled paper machine with the annual capacity of 110,000 tons is scheduled for a start up in July 2014. In the Fourth Quarter of 2012, the Company invested a total of BRL200 million and the investments in the year was BRL664 million.

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

Questions And Answers

Operator

Ladies and gentlemen. we will now begin the question-and-answer session. (Operator Instructions). Our first question comes from (inaudible) with Brasil Plural.

Q - Unidentified Participant

Good morning, everyone. Thank you for the questions. My first question is about the competition among the local players in the packaging segments. If you can provide us some color on how the competitive environment in the local market is evolving, that would be great.

And the second question kind of related with the first one but more in mainly due to long-term perspective. If you believe that the medium to long-term we may see some

consolidation or new players entering in this market is the packaging segments? That would be my two questions. Thank you.

A - Fabio Schvartsman {BIO 2067677 <GO>}

Okay, the starting is about the competition, the competition, there is nothing new on this department. It's the strongest ever in the packaging with several players -- the market is a really spread among several different players. Klabin has -- is the largest one in the market but with a small stake, 15% to 16% of the market and Klabin is very well-positioned operating at full volume. That means that things are progressing globally and we are all here benefited by the fact that the Brazilian market started the year of 2013 in a very strong way.

In the other forms of packaging, Klabin's strength is such that its competitiveness is very high, therefore Klabin is evolving very meaningfully in all of the other product lines that Klabin has.

Regarding consolidation in the Brazilian market, I think that the Brazilian market is a market that is desired by any paper company in the world. That means that if there is an opportunity the Brazilian market for sure, a lot of different companies will try to enter and participate in the Brazilian market.

But (technical difficulty) it doesn't change a lot because our competitiveness comes from the forest because the forest of Klabin is unique and therefore, the cost competitiveness and to the quality competitiveness that we have because of that is very hard to beat and on top of that, the quality of Klabin's product is very high. That means that in normal conditions, people will probably prefer to buy Klabin products than the competition if at the same price level.

Q - Unidentified Participant

Okay, thank you very much.

A - Fabio Schvartsman {BIO 2067677 <GO>}

You're welcome.

Operator

Excuse me. Our next question comes from Thiago Lofiego with Bank of America.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Thank you. One question. Could you please confirm your CapEx budget for 2013/14 and then if you could exclude the pulp plants. And out of that, what is maintenance and what is growth CapEx, please.

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

Sorry, Thiago, we couldn't hear you so well here.

A - Fabio Schvartsman {BIO 2067677 <GO>}

The line was breaking. We couldn't understand your question.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Okay, just want to -- would like you to confirm your CapEx budget for 2013/14 and then if you could break that down to maintenance and what is also -- into maintenance and growth please.

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

Thiago, regarding CapEx for -- you mean for 2013?

Q - Thiago Lofiego {BIO 16359318 <GO>}

Yes.

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

You're talking about 2013, Thiago?

Q - Thiago Lofiego {BIO 16359318 <GO>}

Yes?

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

Well, regarding 2013, our maintenance CapEx in average is about BRL300 million and for 2013, the total CapEx will be about BRL700 million to BRL750 million because as mentioned, we are in the process to build two new paper machines and then because of these two big projects, we have the increase of our CapEx for 2013. That will be BRL300 million for maintenance CapEx and the remaining four special projects like the recycled paper machines, the sack kraft paper machine and other special projects.

Q - Thiago Lofiego {BIO 16359318 <GO>}

And 2014 is similar or that is -- will be the number.

A - Unidentified Speaker

Can you repeat that? It's bad, your line.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Yes, for 2014, if you could confirm the number for 2014.

Oh, for 2014, we had the continuation for the recycled paper machine investments because if you go through the end of the first half of the year and we have the

FINAL

Bloomberg Transcript

debottlenecking of the board machine, may be we have this restart the second half of this year during the 2014 and then in a separate way, we have the CapEx for the pulp mill. You need more details? Hello?

Operator

Excuse me. Our next question comes from Lucas Ferreira with JPMorgan.

Q - Lucas Ferreira {BIO 16552031 <GO>}

Hi. Good morning, Fabio, Sergio. And everyone. My two questions relate to the sales mix for the international and domestic markets which I think was together with the cost cuts one of the sources of improving margins last year. So I was wondering if you could comment on how do you see the levels of sales to the domestic markets which was 70% if I'm not mistaken in 2012, if you think this could continue or even improve somehow.

And also given that we are probably in 2013, the average FX will be a little more depreciated than what we saw in 2012 and we know that the outlook in the international markets have improved also so if you consider selling a little more. So how would you balance the domestic and international mix?

And relating to this topic, the additional board volumes that you plan to start in 2014, just to get a sense if this additional volume will be mostly sold domestically or internationally if you already know that? Thank you, very much.

A - Fabio Schvartsman {BIO 2067677 <GO>}

Well, regarding sales mix, we are getting to a point where we all or at least almost all customers of Klabin are customers with good margins, are customers that are buying good volumes, both domestically and internationally. So what we have in front of us unfortunately or fortunately is Sophia's choice. Actually you we have both.

We have to understand which is the cost customer that we are going to supply, which is the customer that we are not going to be able to supply because at this moment, the demand over Klabin -- on Klabin products is a really very high. That means that Klabin could increase a lot sales in the domestic market or sales in the foreign market if Klabin had capacity to do that.

So coming to the -- straight to the board machine question, it will add roughly 50,000 tons to our capacity and it's not going to change dramatically the environment because Klabin today has a total capacity of the boards of 700,000 tons. Therefore to add 50,000 is to add at like 7% of capacity. That will help. But it's far from to address all of the opportunities that Klabin has. Therefore, we are going to be very careful in order to select which demand we are going to supply in order to make it what is better for our customers and for Klabin.

Q - Unidentified Participant

Thank you, Fabio.

Operator

Excuse me. Our next question comes from Juan Tavaréz with Citi.

Q - Juan Tavaréz {BIO 15083199 <GO>}

Hello. Good morning, everyone. Just a follow-up on that sales mix question. Just to gain a little bit more visibility on what is driving the domestic demand is it more that you are seeing potential market share gains away from imports or is it that the overall market in Brazil is growing stronger and would probably need the same level of imports in Brazil?

A - Fabio Schvartsman {BIO 2067677 <GO>}

Both are happening but at this point, we have to say that probably the market is warming up a little bit of Brazil because the demand is very strong and we don't see imports coming down, imports of packaged goods at this moment. So it means that we are facing stronger economies in all sectors. It is good for Klabin but it is good for all of the other companies that are in the sector as well.

Klabin is actually gaining more from that because as we've been stating, that given the quality of our products, people will rather prefer to buy ours and the competition if at the same price level. So the demand for us is really strong now. That's the reason why we are poised to deliver a very strong First Quarter of this year. Even with the weak seasonality.

Q - Juan Tavaréz {BIO 15083199 <GO>}

And do you envision probably another price increase sometime this year?

A - Fabio Schvartsman {BIO 2067677 <GO>}

Look, you know how this thing works. It is a market issue. If your offer is limited and demand is very high, then in time, prices will increase. There is no other way of dealing with it.

Q - Juan Tavaréz {BIO 15083199 <GO>}

And just on cost-cutting, as you mentioned, you're going to be focusing this year on the packaging area, on that cost base, what exactly will you be focusing on? And is there any CapEx linked to those cost improvements?

A - Fabio Schvartsman {BIO 2067677 <GO>}

Actually, it's more like the following. Our packaging to apartment went to a round of big investments during the last few years. We made a lot of revamping in our sights. We put new machinery and when you do that, you usually get a higher cost when you restart operations so I think that is the biggest opportunity for us in this department will be to bring down costs that were naturally increased during the process of expanding and renewing our packaging.

The pattern that -- in this particular, we are now finishing everything that means in this year, the year of 2013 we will be mainly focused in delivering better costs and operate at full volume in our packaging department is that we will almost for sure translates into better results in this area.

Q - Juan Tavaréz {BIO 15083199 <GO>}

Okay, perfect. And just lastly, if you could just give us a sense of you mentioned five potential projects. Are all of these board approved? I assume is the pulp project and the new board machine aren't. But could you give us a sense of which ones are (multiple speakers)

A - Fabio Schvartsman {BIO 2067677 <GO>}

Good question. But to clarify that, the only two projects that are fully approved are the sack kraft and recycled machine. Those are under construction, both of them. Actually, the sack kraft will be ready very shortly.

Even the debottlenecking of the board machine is not approved yet because we don't have final figures, not even final numbers that are needed for this approval. But we are pretty sure it will be approved because it is 100% necessary for the Company. But it's not approved, to be quite transparent, it is not approved.

The same happens with the pulp project. The pulp project, our board approach to that is the financial structure of this project is what the terms, the possibility of being well facilitated or not. So the project will only be subject to approval once we have the financial structure in place so it's not approved yet and therefore, the new board machine, the details in this process is not even approved as well.

Q - Juan Tavaréz {BIO 15083199 <GO>}

Great. Great. Thank you, very much.

A - Fabio Schvartsman {BIO 2067677 <GO>}

You're quite welcome.

Operator

Excuse me. Our next question comes from Marcos Assumpcao with Itau BBA.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Hello. Good morning. Congratulations for the strong results. The first question is regarding the pulp project. If you consider developing the pulp project without a partner in the structure that you are developing or designing, if there is this possibility, Fabio?

A - Fabio Schvartsman {BIO 2067677 <GO>}

Look, we are mainly focused in raising capital for investors. This is our goal. This is our objective. Everything else is secondary alternative that is not on the table right now.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

And regarding the cardboard, the bottlenecking, do you think this project could also have a positive impact on cost for Klabin, like diluting the fixed costs even improving the cardboard margin?

A - Fabio Svartsman {BIO 2067677 <GO>}

It must be so because we are going to add 50,000 tons of capacity in the existing machine without new costs and therefore there will be further cost dilution because of that.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Do you have any indication of return on investment capital in this project or internal rate of return? It seems to be a very --

A - Fabio Svartsman {BIO 2067677 <GO>}

Excuse me?

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Do you have any estimate of internal rate of return for project such that it seems to be a very profitable project.

A - Fabio Svartsman {BIO 2067677 <GO>}

It should be a profitable project but to be quite frank with you, we don't have the numbers ready and I don't want to speculate on numbers that I don't know. My opinion is the same as yours. It should be very profitable. But let's wait to see the numbers because we have to have it ready when we have the numbers we are going to submit to board approval and then we are going to announce it in the market.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

And Fabio, do you think there is any potential improvement from better negotiations with clients regarding prioritizing some contracts, cutting some other clients and having a larger volumes from better clients? Are you still see this potential upside from Klabin's results going forward?

A - Fabio Svartsman {BIO 2067677 <GO>}

That's for sure. But I don't see that as a positive thing. It will probably improve our results but it will leave a number of our customers unhappy because we are not going to have volume for all of them. So it's good and bad if you can understand.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Yes. Okay. Last question regarding BNDES, if you have any view regarding what is BNDES strategy on Klabin's preferred shares stake that they own?

A - Fabio Svartsman {BIO 2067677 <GO>}

Unfortunately, no idea whatsoever. I don't have any idea. I'm afraid you have to try to ask them because we don't know.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

No problem, Fabio. Just to clarify. Thank you, very much.

A - Fabio Svartsman {BIO 2067677 <GO>}

You're quite welcome.

Operator

Excuse me. (Operator Instructions) Thank you.

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

A - Fabio Svartsman {BIO 2067677 <GO>}

Well, it was a pleasure having you in this conference call. It was a great year for Klabin, a 31% increase in EBITDA. 2013 is poised to be a very good year as well. We are very positive on the evolution of Klabin and as we anticipated for you in the beginning of this call, we see a First Quarter that will be a very strong one. So strong that will compensate the weak season that usually is the First Quarter and actually will allow us to deliver results in line or even better than the Fourth Quarter of last year.

That's a nice improvement and Klabin focus is slowly shifting from cost-cutting and mix investments into growth and we are -- we, the management of the Company, we are 100% focused in trying to deliver the same quality that we are able to deliver in cost-cutting in putting together the projects we are now starting to focus in. Therefore, I hope that our quarter after quarter we will have very interesting news on the development of Klabin for the next few years.

Again, thank you. And I hope that you join us in the next conference call. Thank you, bye-bye.

Operator

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

FINAL

Bloomberg Transcript

FINAL

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.

Bloomberg Transcript