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Q1 2019 Earnings Call

Company Participants

- Aires Galhardo, Executive Officer, Pulp Operation
- Carlos Anibal de Almeida, Executive Officer, Pulp Commercial Business
- Leonardo Grimaldi, Executive Officer, Paper Business
- Marcelo Feriozzi Bacci, Chief Financial Officer and Investor Relations Director
- Unidentified Speaker
- Walter Schalka, Chief Executive Officer

Other Participants

- Andreas Bokkenheuser, Analyst
- Caio Ribeiro, Analyst
- Carlos De Alba, Analyst
- Daniel Sassoon, Analyst
- Juan Tavarez, Analyst
- Leonardo Correa, Analyst
- Marcio Farid, Analyst
- Renato Maruichi, Analyst
- Thiago Lofiego, Analyst
- Unidentified Participant

Presentation

Operator

Good afternoon, ladies and gentlemen. Thank you for waiting. Welcome to the Conference Call of Suzano to discuss the results for the First Quarter of 2019. Participants will be in a listen-only mode during the presentation of Mr. Walter Schalka, Chief Executive Officer; Marcelo Bacci, Financial and Investor Relations Executive Officer; Carlos Anibal, Pulp Executive Officer; and Leonardo Grimaldi, Paper Executive Officer. Afterwards, we will begin the question-and-answer session when further instructions will be provided. (Operator Instructions)

Before proceeding, please be aware that any forward-looking statements are based on the beliefs and assumptions of Suzano 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. You should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of Suzano and

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could cause results to differ materially from those expressed in such forward-looking statements.

I will hand over the call now to Mr. Schalka, who will begin. Thank you.

Walter Schalka {BIO 2099929 <GO>}

Good afternoon, everybody. Welcome to the First Quarter Results Conference Call of Suzano. It's a pleasure to have all of you. On our side, we have the participants here, all of the management team, except the top management team, except for Carlos Anibal that is on the call as well.

It's very clear to us that the first quarter of this year was a major opportunity for us to look for alternatives to create value for our shareholders. On the internal side, we have been working on different dimensions. We have been working on the synergies. We have been working on the opportunities that we have to align culture of the two companies to create a new company and on unifying process and systems. All of them are critical to our future, and our team is devoted to that.

On the other side, it's very clear that we have very turbulent market conditions at this point of time. And we have been working how to accommodate and how to create value for our shareholders on this market environment. On the results that we had this quarter, it's very clear that one of the top highlights that we have is that net average export price on pulp we had US$711 this quarter. This is aligned from what we discussed with the market on the three months. And this allow us to have even with lower production volumes and lower sales when adjusted EBITDA per ton on pulp of BRL1,480 on this quarter. On the paper side, it performed extremely well on this quarter, BRL1,145. This could allow us and support to have one operating cash flow of BRL1.8 billion.

Just to reinforce what has been discussed in several calls, operating cash flow is showing how healthy is the situation of the company for the future. We -- even on this very turbulent market scenario, we were able to generate BRL1.8 billion. There is EBITDA less CapEx sustaining. Our financial leverage increased -- on dollar terms increased on this quarter to 3.3 times, but it's below what we have been discussing on our financial policies. Then we did not have any problems on that.

And as a very good news that I'd like to share with you, we are not going to give disclosure on numbers on the quarters, but we are going to give the disclosure end of this year. But the synergies are on track and synergies are as expected on creating value to the alternatives that we had on several initiatives that we are doing in the company.

Now I'm going to pass to Leonardo Grimaldi that is going to talk a little bit about the papers.

Leonardo Grimaldi

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Thanks, Walter, and good morning, everyone. So let's move to slide number 4. I would like to present the results of Suzano's Paper business unit for the first quarter of 2019. The figures presented on this slide are specific to our Paper business unit, therefore, excluding Suzano's Consumer business unit's results and enabling us to have a better comparison with the best quarter.

Beginning with the top left graph, we have produced 271,000 tons during the first quarter. This includes previous period. Planned maintenance downtimes at all our paper mills were concentrated during this quarter. As a result, we have produced 18,000 tons less than the same quarter last year. Moving on to the top right graph, we can note that our sales in the first quarter were 22% lower than the fourth quarter '18 and 9% lower than the first Q '18. In face of the lower production of volumes during this quarter, we have reduced allocation for exports during the same period.

In Brazil, despite the fact that the first quarter is seasonally lower, we have noticed a weaker-than-expected market in the beginning of the year. According to the figures posted by IBA, our Pulp and Paper Association, the Brazilian domestic industry sales of printing, writing and paperboard grades have decreased 4.5% when compared to the first quarter '18, and inputs have decreased almost 13%. In this challenging environment, our sales in Brazil were 3.4% lower than the same period last year.

Looking at the lower right side, we can observe that our average paper prices have again moved up during the quarter, being 2.4% higher than what they were in the last quarter 2018 and 18% higher than the first quarter 2018. As an additional information, our prices in Brazil also increased 4% when compared to the last quarter '18.

In international markets, where we have already noticed price reduction movements in some regions of the world, we were able to sustain our prices at US$994 per ton, slightly higher than the fourth Q '18, due to the successful revenue management implementation. Even with up and downtimes at all our paper mills and as you can observe on the lower left side of the slide, our adjusted EBITDA margins for the first Q '18 has reached BRL1,145 per ton. This is a 24% increase in EBITDA margin when compared to the first Q '18, and it has reached BRL1,206 per ton in the last 12 months.

I would now like to invite Carlos to join us and present the results of our Pulp business unit.

Carlos Anibal de Almeida {BIO 19090865 <GO>}

Hello, can you hear me?

Unidentified Speaker

Yes, Carlos, go ahead.

Carlos Anibal de Almeida {BIO 19090865 <GO>}

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Okay. Thanks, Leo, and good afternoon, everyone. So let's go to page 5 of our presentation to cover the Pulp business results. Pulp business results revenue in Q1 '19 amounted to BRL4.6 billion and that is approximately US$1.2 billion. Production amounted to 2.2 million tons for Q1 and sales were over 1.7 million tons. Sales volume during the period was impacted by challenging market conditions, especially in China in the first two months of the year.

During Q1, we concluded the following plant and maintenance shutdowns: Mucuri line 2, Limeira, Suzano, Aracruz line B, Veracel and Aracruz line C, where we started at the end of Q1 and we concluded that on beginning of Q2. The next plants ones who are scheduled for Q2 '19 are Aracruz line A, Tres Lagoas line 1, and we will start at the end of this quarter Tres Lagoas line number 2. So this is what we have in terms of plant shutdown to maintenance.

Talking about prices, our average export price for Q1 was US$711 per ton, a small decline of US$17 over the US$728 realized in Q1 '18 and a low drop of only US$32 when compared to Q4 '18. So prices are pretty well aligned with our commercial policy. Our total adjusted EBITDA for Q1 was almost BRL2.5 billion and EBITDA per ton reached BRL1,480 and that was affected by the lower volumes and prices.

Short-term market dynamics have been affected by macro conditions. By macro, I mean, trade restrictions and trade war and some industry-related events there in China. In Europe, the economic uncertainties have also impacted the paper consumption, especially in the printing and writing segment. In our view, medium and long-term market fundamentals have not changed. Demand growth should outpace supply growth in the next 2.5 or 3 years.

As we disclosed in our last conference call, and also in our Investor Day, our pulp stocks are higher than the historical levels. Inventories increased in Q1. We foresee our inventories at a much lower level when we close 2019 as we continue to manage our business mining the mid and long-term market fundamentals. We continue to optimize our supply chain to better serve all the markets. We will produce the volume needed to well serve our customers always, always taking into account our inventory level.

As far as integration efforts, we have fully integrated our sales and operations teams with no impact to our customers. Our team is wholly committed and motivated to create and share value with our customers moving forward.

Now we can move to slide number 6, in the following page to talk about cash cost. So cash cost, excluding the maintenance shutdown for Q1, was BRL667 per ton, BRL16 per ton higher than Q4 due to mainly higher wood and fixed costs, which were partially offset by savings on the energy side. We expect the cash cost to show a downward trend in the coming quarters as a result of the synergies that we have already started to capture. Very important also to mention that in order to create more value for our shareholders, our priority will always be to consider the wood NPV, I mean, the wood net present value, rather than minimize the short-term cost.

Now I'll turn it over to Marcelo Bacci to cover slide number 7.

Marcelo Feriozzi Bacci {BIO 17648865 <GO>}

Hello. Good afternoon, everyone. Before we get into slide 7, I'd like to remind you that several lines of our Q1 results are impacted by the purchase price allocation effect related to the Fibria deal. On our earnings release, we analyzed those effects in detail seeking to provide a better view of operational results. So I invite everyone to take a look at that analysis to have the full picture.

On slide 7, our net debt-to-EBITDA ratio closed the quarter at 3.3 times as a result of our volumes and also on the changes on working capital related to the increase in inventories that we had in the period. Our net debt totaled US$13.8 billion, and its amortization schedule has been improved in the quarter. We closed Q1 with almost BRL7 billion in cash plus close to BRL3 billion in standby facilities, providing us with the flexibility we need to implement our commercial strategy. We now have 75 months of average term on our debt and an average cost of 4.7% a year, which is very competitive.

Moving to slide 8. Our investments totaled BRL1.4 billion in the quarter, BRL1 billion of sustaining CapEx, which is in line with the figure that we have for the year. Moving on to slide 9. As announced yesterday, we have set our market pulp production estimate for 2019 in the range of 9 million tons to 9.4 million tons. We will implement that seeking to maximize the net present value in the long-term, we will be preserving our high-growth forests, and we will be managing the wood supply mix in a way that we will create the most value to the company and our shareholders, and not necessarily providing the best short-term results in terms of cash cost. The production announced will be implemented gradually throughout the year and will lead to also gradual reduction of our inventory levels till the end of 2019.

Thank you very much.

Questions And Answers

Operator

Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions) Our first question comes from Thiago Lofiego, Bradesco.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Hi. Thank you. Two questions for Carlos. Carlos, could you comment on the pickup rates you have been seeing on the Chinese ports. Has it been evolving at the speed you have been anticipating? Or we've been seeing -- or you're seeing a slower-than-expected inventory reduction in China? And the second question, how are you seeing the evolution of paper prices in Asia, and how do you see the restart of the Chenming pulp line, which we know it's an integrated line into graphic paper, if I'm not mistaken? But how do you see that changing or impacting pulp supply and the dynamics in the short term?

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A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Thiago, do you mind repeating your first question? My connection is not that great.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Sure. Sure. Yes, it's just about the pickup rates in the -- at the Chinese ports. So what's the speed of inventory reduction in China at the Chinese ports?

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Okay. Thank you for the question, Thiago. So I'm going to share with you a broader view of what's going on in the market, but giving some information very sensitive at this moment, we will not comment on any subsequent event. It's very sensitive information that you are requesting us to share. So let's give it a broader picture, a broader build about the markets. So I think we can start with our -- from China, where certainly the mood -- the transmit [ph] there is a bit better today than it was three or four months ago, but the macro uncertainties are still there, and it has improved over the last few days. Although, we know that the finance [ph] team's progress are in place, the command in the U.S. remain mixed.

Why did I say that, on one hand, the last China trade negotiations were expected to yield some positive results soon and now there is a question mark. I mean it remains to be seen what's going to happen. Just one week ago, the assumption was that negotiators would be closing the deal, and now they are trying to keep that from collapsing. Adding to the pressure, the U.S. just announced to raise tariffs on US$200 billion of Chinese goods to 25%.

On the other hand, the China is still expected to have somehow whispered some confidence. Nevertheless, I would say that the last set of manufacturing indices and the trade statistic remain weak while the renminbi appreciated a bit over the last few days or weeks. So in China, there is a big uncertainty regarding the macro scenarios and definitely somehow that may affect our -- the pulp market.

In Europe, the macro scenario seems to be even more challenging. Growth has been fragile, and we had several uncertainties still persist in the U.S. That has been the only economy, the only market performed well. So when taking into account this macro backdrop, certainly that impacted the pulp demand in Q1 in Europe and China. I would say that in the first two months of the year, market conditions were similar to what we had seen in the end of Q4 of last year, kind of continued destocking throughout the supply chain of paper producers.

Market conditions improved a bit in China in March, and our sales volumes came in close to normal levels. In Europe, the pulp market remained challenging, reflecting the poor macroeconomic scenario that I described before.

I think your second question is about prices, if I understood that correctly. On Q1, we heard that producers announced and implemented price increase in China, varying from RMB100 to RMB200, and there was more effective on the encoded paper size. In Europe,

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despite the lackluster demand, graph paper prices were stable. Did I miss any other information, Thiago, that I can share with you?

Q - Thiago Lofiego {BIO 16359318 <GO>}

Yes. No, thank you, Carlos. Just a quick follow-up. You mentioned in Europe is even more challenging. Do you see a chance of prices -- global pulp prices being led by Europe in the near term? Over the last couple of years, we've been seeing China being the leader in terms of price moves? Now that net prices are very similar and you mentioned that Europe is even more challenging, do you think that eventually this could revert and the focus will turn to Europe?

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Thiago, as I said, we prefer not to give any guidance on price at this point in time. This is a very sensitive information.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Okay. Thank you Carlos.

Operator

Next question comes from Leonardo Correa, BTG Pactual. You may proceed.

Q - Leonardo Correa {BIO 16441222 <GO>}

Yes. Good afternoon. Hopefully, everyone can hear me. If not, please interrupt me, guys. The line quality is very bad, so hopefully you can hear me. But thank you very much for the opportunity.

The first question, again, for Anibal. Sorry, Anibal, to insist and maybe you cannot tackle this one, but still on the pulp market, right, we've been seeing a lot of volatility on pricing, and you're talking about a bit of an improvement in China over -- compared to the first quarter, compared to the early start of the year. However, when we look at pricing, prices continue correcting in China, now to about US$680. We've been seeing some transactions come even below US$650. So the impression reading the news flow and following some sources is that the direction of prices is down. Can you just qualify if that assessment is right? I mean are you seeing a relatively balanced market with flattish prices? Or are you seeing the direction still in the short-term down? So the view on the direction of the market, I think, would be helpful, given that the range we've been seeing now is US$620 to US$700 for pricing in China.

In terms of -- second point in terms of shipments. So you're saying that Suzano is back to relatively normalized levels of shipments into China. So I just wanted to confirm if that is -- if we're back to normal or if we're maybe 10% below or any percentage level below the normal level, I think, would help us understand what type of shipments we're going to see going forward.

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And finally, maybe for Bacci. Marcelo, the -- I mean leverage has been rising slightly, right, net debt now reaching BRL54 billion. Depending on the EBITDA scenario, we could see leverage creep up to maybe above 3.5%, maybe 4 times in a more stressed scenario. How do you view capital allocation in this environment? And how do you view working capital management going forward? I just wanted to get a sense of how you're seeing balance sheet management in this scenario, which is clearly more challenging with leverage maybe above what you were anticipating before? So those are the questions. Thank you very much.

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Leonardo, thanks for your question. As I said before, any commercial information, price information is very sensitive at this point in time, so we would not make any comment about it. So apologize me. I can share with you some information related to the Brazilian producers' shipments to China in Q1. So Q1 '19 on Q4 '18, shipments were reduced 21% and Q1 '19 on Q1 '18, a reduction of 6%. So important, Q1 '19 again on Q4 '18, minus 21%.

Q - Leonardo Correa {BIO 16441222 <GO>}

Okay, Anibal. If I may, can you just provide us an indication of what the inventory level at the paper mills in China is in terms of pulp? I mean you have been saying that they were running on the lowest level of inventories of pulp maybe in years. Is that still the information that you're gathering in China?

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Could you please repeat your question, Leonardo?

Q - Leonardo Correa {BIO 16441222 <GO>}

In terms of the paper mill inventories of pulp, you were saying in the past quarter that they were running on the lowest level of pulp inventories maybe in years. Do you still confirm that information? I mean is there any indication that the Chinese paper mills are going to start restocking pulp again in the short term?

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Now it is clear. The information that we have from our sources, from our team there in China is that customers, in general, are running with their pulp stocks below the normal level, between the lowest and the normal level, closer to the lowest level. As far as finished products, the information that we have from our customers is that they are running with a normal volume taking into account a better demand we are facing right now. Am I clear?

Q - Leonardo Correa {BIO 16441222 <GO>}

Yes. Thank you.

A - Marcelo Feriozzi Bacci {BIO 17648865 <GO>}

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So, now in regards to your other question on leverage, we are at 3.3 times. We have -- it's important to emphasize that we have no financial covenants that could be impacted by the leverage going forward. But of course, we want to be within the limits of our financial policy, which is 3.5 times. We will be managing our balance sheet taking that into consideration.

The working capital, looking forward, I think, we are going to have a reduction in working capital usages with the production estimate that we have and the sales that we expect to have. As I said before, our inventories should be going down continuously throughout the year. And that will enable us to generate more cash in the second half of this year.

In terms of capital allocation, our CapEx plan for this year has been set, and it's not our intention to change. Of course, with the lower production, we may have a slightly lower sustaining CapEx because of harvesting less, we're going to be replanting less, but that's not going to be a very significant number in our CapEx. We have a very, very comfortable liquidity position, and our amortization schedule is also very comfortable. So we are not worried about the consequences on our balance sheet of what's going to happen throughout 2019.

Q - Leonardo Correa {BIO 16441222 <GO>}

Okay. Thank you.

Operator

Next question comes from Daniel Sassoon, Itau BBA.

Q - Daniel Sassoon {BIO 16381770 <GO>}

Hi everyone. Good afternoon. Thanks for taking my questions. My first question is related to your cash cost. If you could comment a bit on the expected impact from two factors. First, the reduction in production that you are forecasting, so the impact of lower fixed cost dilution, if you could give us some idea of what we could expect. And second, how we should think about the evolution of cash cost over the next maybe couple of years considering your remarks in terms of not necessarily prioritizing lower cash cost in the short-term, but to prioritize higher net present value for shareholders?

And my second question is, in terms of prices, we are -- you are likely tackling the oversupply in the market with your production cuts. This should try and help to minimize this problem, but if you could list the packing order in terms of ranking, in terms of what are the factors preventing recovery or improvement in pulp prices, maybe is it only lack of -- or weak demand in China and Europe? Is it low spread between softwood and hardwood? If you could comment what is playing against the recovery in pulp prices, that would be great. Thank you.

A - Walter Schalka {BIO 2099929 <GO>}

It's now Walter speaking. In terms of cash cost, as cost has been running with lower results, our fixed cost average increased in a -- by a small portion. But our -- we don't give

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any guidance in term of cash cost for future, but we are improving our synergies in the end-user process immensely, then only we can see the results, of course, in the next quarters.

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Daniel, this is Carlos speaking. I would like to share with you our view more on the medium and long term, and we believe that the medium and long-term market fundamentals have not changed. As I said before, we believe that the demand growth should outpace the supply growth in the next 2.5 or 3 years. So we have a very concerting and very positive view in the medium and long run.

Q - Daniel Sassoon {BIO 16381770 <GO>}

Okay. Thank you.

Operator

The next question comes from Carlos De Alba of Morgan Stanley.

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

Thank you very much. And good afternoon everyone. So, my question has to do with -- as the company runs at a lower capacity utilization that everyone believe and maybe what the company was planning on doing a few months earlier, what are the mills -- if you can talk about, what are the operations that would be running at the lowest capacity utilization or that would be shut down? And which ones, which I assume, obviously, is Tres Lagoas, would be running at 100% capacity? But if you could also highlight other mills as you see the ranking of those operations as you deploy this new guidance for pulp production, that would be very useful.

And second, given that you have this sort of system -- production system and an internal cost curve, how does this new capacity utilization affect the overall cash cost, and particularly, in light of what you say that you're trying to maximize the net present value of your forestry operations in the long term rather than using the cash cost in the short term?

And if I may squeeze another one in there, what about the level of stocks which Suzano ended the quarter? We don't talk about the future, but we can talk about the past. Perhaps you can give us a guidance as to how much the amount of tonnage that you hold in inventories or you held in inventories as of March 31st was, that would be really appreciated. Thank you very much.

A - Walter Schalka {BIO 2099929 <GO>}

Carlos, thank you very much. This is Walter talking here and answering your question. Thank you for the question. Going for the first two questions regarding the utilization -- lower utilization capacity. We are not giving the guidance where we are going to reduce, in which plants we are going to reduce the volumes to be between 9 million tons and 9.4 million tons, but it is very clear to mention to you that our criteria is not to minimize the

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cash cost in the short term, but is to look for -- to minimize the net present value of the cost long term or to bring net present value of that.

How we are doing this? We are increasing our biological assets in several plants since we are not harvesting and transporting wood to the plant, and we are increasing our biological assets in certain of our plants. Maybe we're going to enhance our competitiveness for the future. We understand that this will accelerate the benefit of the synergies, means we are going to reduce our cash cost on a factor basis long term.

Of course, this is going to impact our cash cost in short-term and impact during the first quarter. We've decided to operate some of our plants at lower utilization rates. And this creates a situation where we have higher fixed cost as explained by Aires and Carlos during the presentation. And it's probably -- we will have the same situation as we communicated on the next project.

Talking a little bit about your second question that is related with the stock. Our inventories at this point of time is around 3 million tons of pulp. 1.5 years ago -- sorry, one year ago, this number was around of 1.5 million tons on the combined entity. We understand that 3 million tons is more than necessary to serve our customers at this point of time.

Operator

Next question comes from Renato Maruichi, Santander.

Q - Renato Maruichi {BIO 17847481 <GO>}

Hi everyone. I had two questions. The first is regarding the global pulp demand. So considering the recovery in demand you estimated throughout the year, could you elaborate how much of this potential increasing demand comes from inventory buildup from the paper makers and how much is actually end demand? I'm asking that because considering that you made the production guidance and you will not increase your own inventories, sales volume would have to stably increase going forward.

And my second question is regarding the impacts on lower production. I imagine that you are reducing the production pace of your less-efficient mills. So does this lower production affect the capture of synergies on an overall basis? I mean I know you are looking or you're prioritizing the net present value of the -- of all the mills' management, but is there any correlation between -- or any relation between your production guidance and your guidance of synergies? Those would be my questions. Thank you.

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Renato, this is Carlos. So if I understand correctly, your question that has to do with the demand for the coming years, and we believe that the demand should grow over the next five years about 1.4 million tons to 1.5 million tons. We have not changed that forecast. Was that your question?

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Q - Renato Maruichi {BIO 17847481 <GO>}

Yes, kind of because -- actually, I would like you to break down this demand estimate. How much of this demand would come from inventory buildup from the paper makers, especially in China, and how much really means end demand for the new market pulp?

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

So the demand, as I said, will not change. It will be 1.4 million tons, and that will be supplied by the consistent stocks and by the production for the coming months. So is that your point?

Q - Renato Maruichi {BIO 17847481 <GO>}

It is. Thank you.

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Thank you.

A - Walter Schalka {BIO 2099929 <GO>}

Renato, it's Walter talking a little bit about how we split the difference between synergies and the impact of the cash cost of lower volumes. We understand that the short-term impact on the lower volumes will impact the cash cost mainly on the fixed cost, but we are analyzing all of them. And -- but we are doing a lot of other structural changes on different dimensions to reduce operational costs on the industrial side and forest side that we understand very sustainable along the years, and these we considered these as synergies. We will see these probably at the end of this year when we are going to split and show to you how much could be the synergies on our cash cost. The good news that I'd like to share with you is the fact that the real extent, the claim of the cash costs for the coming quarters are going to be lower than the first quarter.

Q - Renato Maruichi {BIO 17847481 <GO>}

Great. Thank you very much.

Operator

Next question comes from Juan Tavarez, Citi. Mr. Juan, you may proceed. Next question comes from Marcio Farid, JP Morgan.

Q - Marcio Farid {BIO 21017394 <GO>}

Thank you. Good morning everyone. I think most of my questions have been taken already, but I have just a follow-up one. A couple of quarters ago, you mentioned you wouldn't mind having higher inventories going into 2020, because the likelihood of the market being tighter is strong, right? But your production guidance implies lower utilization rate, and you said that you planned slowly, slowly destocking across -- throughout the year, right? I'm just trying to understand if there is any change to your view to 2020? And how much lower in terms of inventories you plan to finish the year? Thank you.

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Marcio, thank you for the question. We will not give any guidance on our inventory at the end of the year. I just can say that definitely it's going to be lower than where we stand today. And as I said before, we have a very positive view in the medium and longer run. We have not changed our view for 2020 onwards.

A - Walter Schalka {BIO 2099929 <GO>}

Marcio, just to add to what Carlos said, our view is that we didn't see any structural change in the demand. We are seeing some short-term effects of destocking of some of our customers and some minor changes in consumption in certain geographical areas in certain specific rates. But we understand no major change on the future growth of this market that we understand there is going to be in the ballpark number of 1.4 million tons a year, as Carlos mentioned. And as we didn't see any structural change, it's very clear to us that we would be able to reduce inventories throughout this year. We are not giving any guidance to the end of the year how much we are aiming in terms of inventory, because it would be a very sensitive question that we bring to our customers, to our competitors as well. How much would be our total sales in the next quarters, we cannot give this kind of guidance. But it's very clear that on the structural side, we are extremely comfortable with the position that we have been on the last quarters and the last conversations with our investors.

Q - Marcio Farid {BIO 21017394 <GO>}

Great. Thank you.

Operator

Next question from Juan Tavarez, Citi.

Q - Juan Tavarez {BIO 15083199 <GO>}

Hi. Thank you. Good afternoon everyone. I guess, my first question is to touch on cash costs. I noticed they were -- on the pulp side, they have been under pressure, and you mentioned in the press release about the radius to the mill increasing. Can you confirm that the synergies that you're executing now, will they be reducing some of these radiuses? And how do you see that in the coming quarters in terms of the paces decline? And maybe just some actualization of what is the current radius on average from forest to mill? And then my second question, maybe if you can give us a little bit more clarity on these PPA charges. If you can explain a bit more on the recurring basis of this or how to think about this as we model going forward? Thank you.

A - Aires Galhardo {BIO 17954886 <GO>}

Thank you, Juan. It's Aires speaking. In terms of cash cost, as we mentioned, meetings ago, we have a trend for next year in our average wages. It is 106 kilometers, but we spent

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some -- a couple of figures. So I asked this average? What's the current now? As Walter mentioned, we are anticipating probably some fuels [ph] because we preserve our forests in some regions, including our average years in our forests. Then probably in several years -- in a couple of years, we will remain in the same aim, but it is some time to arrive.

A - Marcelo Feriozzi Bacci {BIO 17648865 <GO>}

Juan, this is Marcelo speaking. In terms of the PPA, we have two different effects here, one of them is a more lasting effect, which is depreciation that is going to go up for a longer period of time since the depreciation and amortization of the industrial assets and also of the biological assets is long-term. But we also had on this quarter a specific effect on inventories. Part of the purchase price was allocated to the existing inventories of Fibria at the end of last year. And as we sold those inventories and we had to recognize the cost adjusted to market value of those, this alone created an effect pretax of something around BRL1 billion. So part of the PPA effect is going to be repeated in the coming quarters. This effect on inventories is something that will happen this quarter and the next one. And with the next -- with normal flow of inventories that we have after Q2, this effect is not going to be there anymore.

Q - Juan Tavarez {BIO 15083199 <GO>}

Okay. Great. Thank you.

Operator

Next question from Andreas Bok, UBS.

Q - Andreas Bokkenheuser {BIO 7182883 <GO>}

Thank you very much. Just two quick questions for me. I'm sorry, I dialed in a little bit late. I'm just trying to understand the strategy. If I remember back on the last few quarters, the results calls you've hosted, I've got the sense that you told that the pulp market was pretty solid, that it was healthy, and you're mentioning today that demand is recovering, you're expecting pulp demand to grow 1.4 million tons, 1.5 million tons per year. So I'm thinking about that, and I'm thinking about the strategy of taking supply out of the market, taking 1 million tons, 1.5 million tons of downtime, which is equivalent to an entire year of demand. So why take supply out if the pulp market is in fact improving and getting a lot better? That's my first question.

And I guess my second question is there was a bit of recent news out during the week from Vancouver Pulp Week that you've mentioned -- obviously, you don't have to confirm this, but you've mentioned this strategy to your customers during Vancouver Pulp Week. So I'm just wondering what's the reaction seeing that if you take supply out of the market, it could effectively drive our pulp prices. So I'm just wondering what -- how are customers reacting to the strategy of yours? Those are my two questions. Thank you very much.

A - Walter Schalka {BIO 2099929 <GO>}

Andreas, thanks for your question. I'm going to start with the first question. And it's something that we have seen two different issues here. One thing is the structural growth, another one is some short-term effect on destocking of some of our customers. It's a minor adjustment on consumption on certain specific grades and geographic areas. We believe that the destocking of our customers creates a scenario or situation where we -- the demand growth of this year -- of the last, sorry, 12 months are not going to be at the same pace than before, and this creates a situation that our inventories were going up. And we understand that we do have enough inventory at this point of time. And with the production that we are going to have in the next couple of months would be enough to supply of our customer needs. Then customer needs is critical for us, we will supply all of their needs or all of their demand on the next 10 months -- next year as well. The second question, we are not going to comment on our customers' reactions.

Q - Andreas Bokkenheuser {BIO 7182883 <GO>}

All right. Thank you very much. Appreciate the response.

Operator

Next question from Antonio (inaudible), Bank of America.

Q - Unidentified Participant

Hi. Good afternoon. Just a follow-up on the question before. The first to Walter. Walter, could you be more specific regarding the lower production this year? How this would impact the synergy guidance and the capture that you have for 2019? And second, how also this production reduction -- and also, you were extending the maintenance. How this should impact the maintenance costs?

And third for Anibal, just maybe I'll try as a follow-up. If you can compare the outlook you provided during the Investor Day. What has changed on demand? And how surprised that you were expecting maybe price to move up in April and May onwards? And if you could point at the main changes at the last conversation there. Thank you.

A - Walter Schalka {BIO 2099929 <GO>}

Antonio, thank you very much for your question. This is Walter speaking here. I would like to clarify to all of you about the differentiation between synergies and short-term impact of our lower production. We have been moving in the direction of being able to capture the synergies that we expect on the first year. Just remember what we mentioned on the Investor Day that we expect to have the ballpark number between BRL800 million and BRL900 million a year on synergies, but in the first year would be around 40% of that. We will keep exactly the same target for this year, and we believe after three months of the merge of the two entities that we would be able to reach our expectations. It's very important this is not going to affect the situation where lower volumes increase a little bit our fixed costs. Then we are sharing with you every quarter how much would be our fixed cost variation compared with the previous quarter, but it's very important to mention that we are talking about some structural situation compared with short-term impact on our operations.

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

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Antonio, this is Carlos speaking. What we are facing right now is a kind of more challenging macroeconomic scenario mainly in Europe. And some uncertainty is coming from the trade war there in China, but again, we have not changed our view. Medium and long-term market fundamentals have not changed. We still have a very positive view for that for the next 2.5 to 3 years when the demand growth should outpace the supply growth.

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Q - Unidentified Participant

Got it. Thank you again.

Operator

Next question from Caio Ribeiro, Credit Suisse.

Q - Caio Ribeiro {BIO 18420483 <GO>}

Yes. Good afternoon, everyone. Thank you for the opportunity. So my first question is on the continued perspective that we're seeing for recycled fiber imports into China continuing to be restricted, right, and perhaps even trending towards zero. I just wanted to get a little bit of your perspective on how you see the market rebalancing and compensating for this lack of recycled fiber. And then my second question is regarding CapEx figures. I know you have already provided the guidance for 2019. But I just wanted to get a sense on where you see CapEx trending in 2020 onwards and whether you see it coming down or you expect similar run rates as 2019? Thank you.

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Caio, could you please repeat your question. I could not hear you very well.

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Q - Caio Ribeiro {BIO 18420483 <GO>}

Yes. So my first question was just on the recycled fiber import bans into China. I just wanted to get a little bit of your feeling of how you see the market compensating for this lack of recycled fiber?

A - Carlos Anibal de Almeida {BIO 19090865 <GO>}

Okay. Clear. Thank you for your question. So last year, we had a big drop on the waste paper imports. This year, Q1 '19 on Q1 '18, another drop of 15%. And we hear -- we have heard in China that the government is working to ban the waste paper by, let's say, 2020. So far we haven't seen over the last maybe 12 months any effect on the virgin fiber, but going to zero once they ban the waste paper imports, we believe that we're going to see some impact on the virgin fiber market. It is hard to quantify what that can be, but we believe we're going to see some.

A - Walter Schalka {BIO 2099929 <GO>}

Caio, on your CapEx question, our sustaining CapEx for this year is going to be BRL4 billion, and our vision, we do not have a number yet for the next coming years, is that this

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number is going to be lower, since we are going to have some synergies on the CapEx side as well. We will provide with information to you probably end of this year, after our budget. But very probably this number are going to be lower than BRL4 billion. On the remaining part, expansion and modernization of our operations and expand of our asset base in terms of forest and land, we will continue to invest, and this is going to be completely discretionary, and it will be dependent on the situation that we have right now. Right now we have just committed CapEx for the next coming years on the Q4 that is going to be Maranhao and Santos, the DP ports that we have, the only commitment that we have for the next coming years in terms of investments.

Q - Caio Ribeiro {BIO 18420483 <GO>}

Okay. Great. That's very clear. Thank you.

Operator

Next question comes from Milton [ph] Sullivan, XP System.

Q - Unidentified Participant

Hi guys. Thank you for the questions. My first question is again because of the PPA, I do not know if I'm making the right calculations here, so please correct me if I'm wrong. But since you guys said that you had increasing sales throughout the first quarter, right. So Jan and Feb with lower sales and March at normal sales, you had said that before. So my expectations when I looked at your receivables was for a big increase in receivables, because you would see receivables related to March versus normal sales, right? And I didn't see that. I actually saw receivables falling quarter-over-quarter. So my question is, did you have any amount of receivables discounted in the quarter? And how much was that? If you could disclose that to us.

And my second question is related to the production guidance. My question is when you say that your inventories are going to be lower or closer to normal at the end of the year, do you have an implied assumption that demand for pulp is going to increase? Or is that calculation based on current sales levels? And lastly, on strategy for Walter. Walter, please, I -- we understand that you guys believe that this is not a structural change in demand, but my question is if you could please comment because it seems to us that it's taking a little bit too long to recover. So let's talk hypothetically here. If it is a structural change in demand, would Suzano be willing to keep volumes low and utilization rates lower for longer? Or would the strategy be a little bit different? If you could comment a little bit on that for us, please. Thank you.

A - Marcelo Feriozzi Bacci {BIO 17648865 <GO>}

Hi Milton. This is Marcelo speaking. On the receivables side, what happens is that after the merger, we have to change a bit the way we manage the receivables because there is -- in some clients, especially in the biggest clients, some sort of accumulation of warrants between Suzano and Fibria. And in order to manage our credit exposure, we are selling more receivables for some specific names to be compliant with our credit policies. So it is a fact that we have been selling more receivables than in the past and that has impacted the receivable line exactly in the way that you described. We -- for strategic reasons, we

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are not going to disclose exactly how much we sold of receivables in the quarter and on the coming quarters.

A - Walter Schalka {BIO 2099929 <GO>}

Thank you very much for your question. Related with the first question of the production guidance that we are giving to our investors, this allows you to have a better understanding of our policy in terms of production for this year and forecast the results of our company. But on the other side, I'd like just to address what you mentioned that we are going to reduce the inventories to normal levels. We just mentioned that we are going to reduce inventories from the actual levels that we have right now, but we don't know the speed of the decrease in terms of inventories would depend on demand.

And talking about a bit about structural change, our -- in terms of what would be our view for the future, if we could run with lower utilization rates for the future, this will depend if you're seeing any structural change on demand comparing with our production and comparing with the growth that we are seeing in terms of consumption. If you see any major changes on the market for the future, perhaps we could change our policy. And we will be following this very close on the next quarters how we are going to proceed on that. We understand that our position is very clear. We want to create value for our shareholders, and we want to aim for lower volatility to our prices and to our results and to our customers as well I think would be a positive sign for everyone.

Q - Caio Ribeiro {BIO 18420483 <GO>}

Thank you.

Operator

We are now closing the question-and-answer session. I will pass the call back over to the company for the closing remarks.

A - Walter Schalka {BIO 2099929 <GO>}

Thank you very much for you to participate, everyone, on this call. I would just like to reinforce to you that our aim is always to create value for our shareholders. We have been working very diligently internally to attract the synergies of this huge combined operations. We are very pleased with the developments that we have right now. We understand that the short-term turbulence that we are seeing in the market do not affect our vision for the future. We continue to believe that we will keep creating value for our shareholders and we will -- and our team is highly motivated and engaged to find ways and to find alternatives to do it on every day. Thank you very much. Hope you have a nice weekend, and happy Mother's Day.

Operator

That does conclude the conference call of Suzano. Thank you very much for participating. Have a good weekend.

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