Equity Research

SUZANO

2Q23 Review: Persistent, even facing the ebb of pulp.

LatAm Pulp & Paper

Main takeaways:

(i) Pulp volume rises +2.4% q/q, with an improvement in Chinese demand, contrary to our more bearish approach on estimates; **(ii)** Realized pulp prices fall to US$571/t (-20,8% q/q), following the reference curve in China; **(iii)** Paper volumes continue to be below historical levels, but improving along with seasonality; **(iv)** New corrections in paper prices, moving towards a more normalized value; **(v)** EBITDA in strong decline, -35.3% q/q and -39.3% y/y, but above estimate (+10,4% vs. Genial Est); **(vi)** Foreign exchange hedge and dollar debt help to mitigate the effect on net income, that came +9.7% vs. Genial Est., practically flat q/q, even with a substantial drop in EBITDA; **(vii)** trading at an **EV/EBITDA 23E** of **6.7x**, we maintain our **BUY rating**, at a **12M Target Price** of **R$60.00**, which implies an **upside** of **+25.29%** for the shares.

Analysts

Igor Guedes
+55 (11) 3206-8286
igor.guedes@genial.com.vc

Lucas Bonventi
+55 (11) 3206-8244
lucas.bonventi@genial.com.vc

Renan Rossi
+55 (11) 3206-1457
renan.rossi@genial.com.vc

Company

SUZB3 BZ Equity
Buy

Price: R$ 48.40 (02-Aug-2023)
Target Price 12M: R$ 60.00

SUZ US Equity
Target Price 12M: R$ 12.60

Suzano released its 2Q23 results today, August 2nd of 2023, after the market closed. In a quarter in which the **sectoral conjuncture raised barriers to the formation of more positive figures**, the Company presented numbers in deceleration q/q and y/y, but in **better dynamics than our estimates**, which were more pessimistic regarding volumes and prices, so that **despite** being at a **-35,3% q/q contraction**, **EBITDA ends up exceeding our estimates**, while **exchange rate hedge via options** and dollarized debt **contributed to net income**.

2Q23 Review

Maintenance stoppage schedule does not limit pulp sales. Despite complying with the previously disclosed schedule for maintenance of production plants, which included during 2Q23 the stoppage in 4 relevant mills that together correspond for 4.5Mt of capacity, pulp volume surprised positively by being reported at 2.5Mt (+6.3% vs. Genial Est.), contrary to our estimates that contemplated declines, and showing an increase of +2.4% q/q, which occurred mainly due to a higher-than-expected demand in China.

International benchmarks falling bring retraction in pulp prices. After a quarter with sharp declines in the hardwood curve, averaging ~US$520/t vs. ~US$760/t in 1Q23, Suzano's realized price closed at US$571/t (-20.8% q/q; -21.3% y/y). Despite the double-digit sequential drop, the number came in better than expected, with the realized price standing at +US$10/t vs. Genial Est., reinforcing Suzano's ability to negotiate with its clients.

Table 1. Net Revenue Suzano (2Q23 vs. Genial Est.)

	2Q23	2Q23E		1Q23		2Q22	
(R$ millions)	Reported	Genial Est.	% R/E	Reported	% q/q	Reported	% y/y
Net Revenue	**9.160**	**8.513**	**7,6%**	**11.276**	**-18,8%**	**11.520**	**-20,5%**
Pulp	7.101	6.504	9,2%	9.201	-22,8%	9.508	-25,3%
Paper	2.058	2.008	2,5%	2.075	-0,8%	2.012	2,3%

Soure: Suzano, Genial Investimentos

Paper volume improving. Coming out of a negative seasonality, but still affected by the economic slowdown, especially in the printing and writing category and some packaging destined for the food industry, which suffer sightly from still high inflation at the top end, paper volumes improved due to the gain in exposure in paper for hygienic purposes. We see the Company's 2Q23 paper volumes at 294kt (+3.2% vs. Genial Est.), recovering q/q by rising +5.0%, despite the -9.3% y/y decline.

After sequential increases, paper prices are heading back to normal. With a realized price of R$7,002/t (-5.5% q/q; +12.9% y/y), Suzano's paper division suffered from short-term retractions, giving back part of the rise that was seen in recent quarters, in line with what was previously expected.

Revenues fell sharply, driven by pulp. On a consolidated net revenue of R$9.1bn (+7.6% vs. Genial Est.), the reported figure came in above expectations, but showing a decline of -18.8% q/q and -20.5% y/y, which is mainly reflective of a loss of revenue within the market pulp unit, which clocked in at R$7.1bn (-22.8% q/q; -25.3% y/y), due to lower realized prices. Meanwhile, the paper unit presented a more resilient dynamic, with stability q/q at R$2.0bn (+2.5% vs. Genial Est.), as the slightly more robust sales level, added to worse prices created a flat effect.

COGS/t ex. stop down slightly, despite lower dilution capacity. Reporting a COGS/t ex. stoppages for pulp at R$919/t (-0.3% vs. Genial Est.), Suzano had a slight -1.9% q/q cooling in its cash cost, driven by healthier price dynamics in inputs, especially chemicals, which accounted for a R$21/t share of the decline, and by the effect of the USD/BRL exchange rate reduction, responsible for a R$9/t cooling. Still, COGS/t on a year-on-year basis shows a +7.5% rise, influenced by a heavier cost in wood procurement, and lower fixed cost dilution capacity, in the face of a -5.6% y/y slowdown in direct pulp sales.

Higher maintenance costs, with relevant mill shutdowns. Considering maintenance, COGS/t including stoppages reached R$1,005/t (+3.3% q/q; +14.1% y/y), which implies an exclusive cost linked to maintenance of R$87/t (vs. R$55/t Genial Est.), sequentially above our expectations at +R$32/t. In the consolidated, total nominal cost came in at R$6.2bn, slightly higher than projected due to advanced downtime costs partially offsetting the effect of better pulp volume vs. estimates.

EBITDA suffering, but above estimates. In essence, market players priced in a high expectation that new capacity additions from global players would hit the breakeven level, causing an oversupply of the commodity, therefore leading to a sharp reduction in pulp prices in 1H23. With this scenario, it would be inevitable for us that Suzano could not escape a double-digit loss in EBITDA, which came in at R$3.9bn (-35.3% q/q; -39.3% y/y), feeling a sharp drop in its most representative unit, responsible for 81% weight in operational delivery.

Even so, the pulp unit's adjusted EBITDA was delivered at R$3.2bn (+10.4% vs. Genial Est.), above our expectations, given that we weighed pessimism in our assumptions, considering the more nebulous scenario for the commodity price. Even with a lower representation in the consolidated result, the paper division brought a result with a slightly more contained loss, given the resilience of paper vs. direct sale of market pulp. Nevertheless, the unit decelerated q/q, reaching R$729mn (-12.8% q/q; -10.9% y/y).

Table 2. EBITDA Suzano (2Q23 vs. Genial Est.)

(R$ millions)	2Q23 Reported	2Q23E Genial Est.	% R/E	1Q23 Reported	% q/q	2Q22 Reported	% y/y
Adjusted EBITDA	**3.919**	**3.632**	**7,9%**	**6.054**	**-35,3%**	**6.458**	**-39,3%**
Pulp	3.190	2.889	10,4%	5.218	-38,9%	5.640	-43,4%
Paper	729	743	-1,8%	836	-12,8%	818	-10,9%

Soure: Suzano, Genial Investimentos

Currency hedging policy helps net income. Due to **(i)** positions made via options in a zero cost collar, **(ii)** a debt raised ~85% in USD, and **(iii)** reversals of taxes and fees, Suzano had some positive effects running through the financial result, and that helped to partially offset the negative effect of the operational delivery on EBITDA in the bottom line, which was reported at R$5.0bn (+9.7% vs. Genial Est.), remaining practically sideways, with the superficial drop of -3.1% q/q.

Individually, the FX hedge positions mounted benefited from the fall in the USD/BRL exchange rate in the period, which averaged R$4.95 vs. R$5.20 in 1Q23, resulting in a R$1bn gain. On the other hand, its USD debt had its total amount in BRL decreased significantly, causing this R$3bn decrease to pass through the financial result. Therefore, both came as expected. But also facing an obstacle by a large update to the fair value of its biological assets by -R$1.2bn.

Table 3. Income Statement Suzano (2Q23 vs. Genial Est.)

(R$ millions)	2Q23 Reported	2Q23E Genial Est.	% R/E	1Q23 Reported	% q/q	2Q22 Reported	% y/y
Net Revenue	**9.160**	**8.513**	**7,6%**	**11.276**	**-18,8%**	**11.520**	**-20,5%**
COGS	(6.228)	(5.939)	4,9%	(5.969)	4,3%	(6.123)	**1,7%**
Adjusted EBITDA	**3.919**	**3.632**	**7,9%**	**6.054**	**-35,3%**	**6.303**	**-37,8%**
EBITDA Margin (%)	42,8%	42,7%	0,12p.p	53,7%	-10,9p.p	54,7%	-11,93p.p
EBIT	**3.068**	**1.801**	**70,4%**	**4.306**	**-28,8%**	**4.587**	**-33,1%**
EBIT Margin (%)	33,5%	21,2%	12,34p.p	38,2%	-4,7p.p	39,8%	-6,33p.p
D&A	(1.845)	(1.831)	0,8%	(1.748)	5,6%	(1.871)	-1,4%
Financial Result	4.536	4.182	8,5%	2.470	83,6%	(6.975)	-
Net Income	**5.078**	**4.629**	**9,7%**	**5.243**	**-3,1%**	**182**	**2693,4%**
Net Margin (%)	55,4%	54,4%	1,06p.p	46,5%	8,94p.p	1,6%	53,86p.p

Soure: Suzano, Genial Investimentos

Our Take on Suzano

We see the 2Q23 result being negatively influenced by the hardwood market environment, which showed strong declines after the **(i)** normalization of some supply setbacks, together with the **(ii)** expectation of several relevant projects with their start-ups and ramp-ups in the short to medium term. For us, this is the biggest reason for a double-digit loss in EBITDA, which was delivered at R$3.9bn (-35.3% q/q; -39.3% y/y). However, the numbers reported by Suzano came in higher than expected, for prices realized at +US$10/t vs. Genial Est, as well as better volumes vs. our pessimistic estimates, which considered the adverse scenario. In addition, the effect of the currency hedge on the financial result ended up helping net income to be less impacted, coming +9.7% vs. Genial Est., resulting in a feeling that, considering that we are not facing a bullish cycle for pulp, the 2Q23 result could have been much worse.

Cash flow generation surprises positively. Despite double-digit declines in EBITDA, the Company generated an adjusted free cash flow (excluding expansion projects) of R$5.2bn vs. +22.9% Genial Est., with operating cash generation well above our expectations, through the **release of R$2.7bn in working capital**, and R$1.3bn through derivatives. We were expecting a working capital release of R$1.5bn, so Suzano was able to unlock much more potential than our estimates. Conversely, the Company reached a **Net Debt/EBITDA of 2.0x**, increasing minimally **vs. the 1.9x** seen in the previous quarter, due to a lower EBITDA sequencing, being expunged out of the 12-month account in LTM.

Persistent results, even facing the ebb of pulp. Historically, the sector has gone through very cyclical moments, where the vector of reduction in the price of the commodity was canceled by opposite movements that contributed to withdraw or inhibit an increase in the supply of market pulp, such as **(i)** unexpected major maintenance, **(ii)** postponements of new projects, and **(iii)** logistical complexities. Therefore, in the long term, we see supply to be in line with demand, which could be a positive trigger for Suzano's shares in an event of a new potential supply constraint, as we highlighted in our last sector report (Pulp & Paper: After all, are the theses growth or value?).

Still, the short term seems to continue showing a very slow price recovery, with eventual readjustments, gradually. Suzano keeps making attempts to increase prices, in three months in a row (+US$30/t in June accepted totally; +US$30/t for July accepted partially; +US$20/t from August, to complete the partial made in the previous month). As such, realized prices are showing a trend very close to our estimates, heading towards ~US$520/t by the end of 2023. However, as pulp's spot q/q price declines were very intense in 2Q23, even if Suzano uses its large market power to pass through positive price adjustments, we believe this will not be enough to make we see a sequential increase in the next quarter. In our assessment, the average in 3Q23 should show a decline from the 2Q23 average, considering that the months of May and June accelerated the pace of price retraction in the final stage of the quarter, causing the average value of the quarter to not fully reflect the real magnitude of the slowdown.

In average, expectations are that **prices may get worse before they get better**. However, given our long-term estimate for China's BHKP curve to reach ~US$620/t by 2028, we continue to assess that the **natural competitive advantages** of its assets, **coupled with its scale**, ultimately ensure **satisfactory profitability even at times closer to the bottom of the commodity cycle**. Therefore, trading at an **EV/EBITDA 23E** of **6.7x**, we maintain our **BUY rating**, at a **12M Target Price** of **R$60.00**, which implies an **upside** of **+25.29%** for the shares.

Appendix: Suzano

Figure 1. Suzano – Income Statement in R$ Millions (Genial Est. 2023-2028)

Income Statement	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**37.244**	**38.356**	**45.639**	**48.378**	**50.255**	**51.146**
(-) COGS	(24.204)	(26.424)	(29.710)	(30.042)	(30.176)	(30.361)
Gross Profit	**13.040**	**11.931**	**15.928**	**18.336**	**20.079**	**20.786**
(-) Expenses	(3.262)	(3.319)	(3.793)	(3.898)	(4.037)	(4.101)
Adjusted EBITDA	**17.313**	**17.563**	**21.260**	**23.459**	**24.954**	**25.489**
(-) D&A	(7.541)	(8.951)	(9.124)	(9.021)	(8.912)	(8.804)
EBIT	**9.772**	**8.613**	**12.136**	**14.438**	**16.042**	**16.685**
(+/-) Financial Result	5.202	(4.162)	(3.035)	(3.965)	(2.187)	(865)
(-) Taxes	(3.389)	(1.007)	(2.060)	(2.370)	(3.136)	(3.580)
Net income	**11.586**	**3.443**	**7.041**	**8.103**	**10.719**	**12.240**
Profitability						
Net margin (%)	31,11%	8,98%	15,43%	16,75%	21,33%	23,93%

Figure 2. Suzano– Cash Flow in R$ Millions (Genial Est. 2023-2028)

Cash Flow (FCFF)	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**37.244**	**38.356**	**45.639**	**48.378**	**50.255**	**51.146**
(-) COGS	(24.204)	(26.424)	(29.710)	(30.042)	(30.176)	(30.361)
Adjusted EBITDA	**17.313**	**17.563**	**21.260**	**23.459**	**24.954**	**25.489**
EBIT	**9.772**	**8.613**	**12.136**	**14.438**	**16.042**	**16.685**
(-) Taxes	(3.389)	(1.007)	(2.060)	(2.370)	(3.136)	(3.580)
(+) D&A	7.541	8.951	9.124	9.021	8.912	8.804
(+/-) Δ WK	1.241	(368)	(907)	(346)	(202)	(120)
(-) Capex	(18.384)	(13.613)	(8.299)	(8.297)	(8.026)	(8.191)
FCFF	**-3.219**	**2.575**	**9.995**	**12.446**	**13.591**	**13.597**

Disclaimer

This report has been produced by the research department ("Genial Institucional Research") of Genial Institucional Corretora de Câmbio, Títulos e Valores Mobiliários S.A. ("Genial Institucional CCTVM"). Genial Institucional is a brand name of Genial Institucional CCTVM.

Genial Rating

	Definition	Coverage
Buy	Expected return above +10% in relation to the Company's sector average	**46%**
Neutral	Expected return between +10% and -10% relative to the Company's industry average	**44%**
Sell	Expected return below -10% in relation to the Company's sector average	**5%**
under Review	Under review	**5%**

This report may not be reproduced, retransmitted, displayed or re-published to any other person, in whole or in part, for any purpose, without the prior written consent of Genial Institucional CCTVM, which consent may be sought by contacting the principal analyst, who is going to be responsible for obtaining the Control Room´s approval. Genial Institucional CCTVM accepts no liability whatsoever for the actions of third parties in this respect.

This research report is for distribution only under such circumstances as may be permitted by applicable law. This research report is not tailored to the specific investment objectives, financial situation or particular needs of any specific recipient, even if sent only to a single recipient. This research report is not guaranteed to be a complete statement or summary of any securities, markets, reports or developments referred to in this research report. Neither Genial Institucional CCTVM nor any of its directors, officers, employees or agents shall have any liability, however arising, for any error, inaccuracy or incompleteness of fact or opinion contained in this research report or lack of care in this research report's preparation or publication, or any losses or damages which may arise from the use of this research report.

Genial Institucional CCTVM may rely on information barriers, such as "Chinese Walls" to control the flow of information within the areas, units, divisions, groups, or affiliates of Genial Institucional CCTVM

Investing in any of the non-U.S. securities or related financial instruments (including ADRs) discussed in this research report may present certain risks. Non-US securities mentioned, recommended, offered, or sold by Genial Institucional CCTVM or its affiliates are not insured by the Federal Deposit Insurance Corporation and are subject to investment risks, including the possible loss of the entire principal amount invested. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the U.S. Securities and Exchange Commission. Information on such non-U.S. securities or related financial instruments may be limited. Foreign companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect within the United States

The value of any investment or income from any securities or related financial instruments discussed in this research report denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related financial instruments.

ANALYST(S) DISCLOSURES AND CERTIFICATION

The analysts hereby certify that the views expressed in this research report accurately reflect their personal views about the subject securities or issuers and it was prepared in an independent manner, including with respect to the person and to Genial Institucional.

The analyst's compensation is, directly or indirectly, determined by income from Genial Institucional´s business and financial operations.

In addition, the analysts certify that no part of their compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

The compensation of the analyst who prepared this report is determined by research management and senior management (not including investment banking). Analyst compensation is not based on investment banking revenues, however, compensation may derive from the business and financial operations revenues of Genial Institucional CCTVM, its affiliates, parent companies and/ or subsidiaries as a whole, of which investment banking, sales and trading are a part. Compensation paid to analysts is the sole responsibility of Genial Institucional CCTVM.

The analysts **Igor Guedes, Lucas Bonventi and Renan Rossi** are the responsible for the content of this report and for meeting the requirements of Securities and Exchange Commission of Brazil (CVM) Instruction 598/2018.

Unless otherwise stated, the individuals listed on the cover page of this report are research analysts.

IMPORTANT DISCLOSURES FOR U.S. PERSONS

This research report was prepared by Genial Institucional CCTVM, a company authorized to engage in securities activities in Brazil. Genial Institucional CCTVM is not a registered broker-dealer in the United States (U.S.) and, therefore, is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. This research report is provided for distribution to "major U.S. institutional investors" in reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act.) Genial Institucional CCTVM distributes such reports in the U.S. pursuant to Rule 15a-6 and in this context the chaperoning party (Brasil Plural Securities LLC) and in certain instances such distribution is part (or viewed) as part of a soft dollar arrangement established and maintained by Brasil Plural Securities LLC. Genial Institucional CCTVM does not provide this report (or any research) to U.S. persons pursuant to any express or implied understanding that those U.S. persons will direct commission income to Genial Institucional CCTVM.

Any U.S. recipient of this research report wishing to effect any transaction to buy or sell securities or related financial instruments based on the information provided in this research report should do so only through Brasil Plural Securities LLC, a registered broker dealer in the United States with an office at 545 Madison Ave., New York, NY 10022, (212) 388-5600. Under no circumstances should any recipient of this research report effect any transaction to buy or sell securities or related financial instruments directly through Genial Institucional CCTVM.

Brasil Plural Securities LLC accepts responsibility for the content of this research report, subject to the terms set out below, to the extent that it is delivered to a U.S. person other than a major U.S. institutional investor.

The analyst whose name appears in this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA") and may not be an associated person of Brasil Plural Securities LLC and, therefore, may not be subject to applicable restrictions under FINRA Rules on communications with a subject company, public appearances and trading securities held by a research analyst account.

The disclosures contained in research reports produced by Genial Institucional CCTVM and distributed by Brasil Plural Securities LLC in the U.S. shall be governed by and construed in accordance with U.S. law. Additional information relative to the financial instruments discussed in this report is available upon request.