

KLABIN

3Q23 Review: Perfect is the enemy of good

LatAm Pulp & Paper

Main takeaways:

(i) Paper and packaging volume growing, due to the positive seasonality entering the semester, despite scheduled maintenance in cardboard; (ii) Kraftliner continues to suffer in price, with new corrections due to the international scenario; (iii) Pulp business division clocking in at with strong sales volume, after operational improvements in the stoppage made at Puma I in the previous quarter; (iv) By operating with a delay vs. commodity curve, and due to Europe having a slower fall, the realized price of pulp falls more strongly, but with better prospects for the future; (v) flat EBITDA q/q; (vi) Weak bottom line, after negative exchange rate variations affecting the financial result; (vii) **12M Target Price** maintained at **R\$26.50**, **BUY** rated, with an **upside** of **+19.64%**.

Klabin reported its 3Q23 results today. Operating figures **came in line expectations**, as the **paper business division showed a sequential recovery**, while **the pulp business continues to shrink**. The **net income level was lower than expected**, mainly due to the revision in biological assets (a non-operational indicator) and the financial expenses, as we are seen an **upper leverage** (3,2x Net Debt/EBITDA LTM), mainly because EBITDA LTM is contracting as well.

Although we had already expected a drop in biological assets, as we commented in our preview report ([Klabin 3Q23 Preview](#)), the retraction was even more intense than we had projected, causing net income to slow down to R\$258mn (-67% vs. Genial Est.). Even so, operationally the company showed resilience, with adjusted EBITDA clocked in at R\$1.3bn (-1.7% vs. Genial Est.), basically flat compared to last quarter, and in line with our estimate.

Table 1. Shipments Summary (3Q23 vs. Genial Est.)

(Thousand Tonnes - kt)	Reported	Genial Est.					
Summary (Shipments)	3Q23	3Q23E	% R/E	2Q23	% q/q	3Q22	% y/y
Kraftliner	102	106,1	-3,8%	97,8	4,4%	141	-27,7%
Cardboard	166	166,2	-0,3%	170,0	-2,5%	183	-9,2%
Corrugated boxes	226	228,8	-1,0%	216,2	4,8%	237	-4,4%
Sack Kraft	36	36,3	-1,2%	36,0	-0,4%	40	-9,2%
BHKP Pulp	315	294,3	7,0%	244,1	29,0%	295	6,6%
BSKP + Fluff Pulp	111	116,3	-4,5%	90,3	23,0%	116	-4,2%

Soure: Genial Investimentos, Klabin

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

(R\$ millions)	Reported	Genial Est.					
Income Statement	3Q23	3Q23E	% R/E	2Q23	% q/q	3Q22	% y/y
Net Revenue	4.400	4.485	-1,9%	4.293	2,5%	2.230	97,3%
Adjusted EBITDA	1.352	1.375	-1,7%	1.344	0,6%	2.311	-41,5%
Net Income	258	802	-67,8%	971	-73,4%	2.053	-87,4%

Soure: Genial Investimentos, Klabin

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Company

KLBN11 BZ Equity

Buy

Price: R\$ 22.15 (25-Oct-2023)

Target Price 12M: R\$ 26.50

Klabin's lack of more expressive growth in 3Q23 should not be seen as a necessarily bad news, since we believe that Suzano, its main peer in Brazil in terms of investors' capital allocation, will report results with a strong slowdown. Klabin's stable results seem better to us than a sharp drop, which is exactly what we expect to happen with Suzano in 3Q23. It's important to note that the sector's conditions are challenging. As we have been mentioning since the publication of the report that marked our assuming coverage in the sector, which is attached ([Pulp & Paper: Assuming Coverage](#)), we believe that Klabin's operating performance would be superior to Suzano's in the **short term**, due to **our preference for the paper business over direct pulp market sales**, exactly the main difference between the two investment theses.

Valuation and rating. For us, Klabin's 3Q23 came with a sequentially positive result for the paper business unit (~65% of revenue in the historical average), with a recovery in packaging sales, and with prospects for better pulp prices going forward, despite the weak performance in this quarter for this business division (~35% of revenue in the historical average). We like the figures presented, despite the weak net income. Investors should pay attention to the volatility of the biological assets data. Trading at a **24E EV/EBITDA of 6.8x** (vs. a historical average of 7.0x), we maintain our **BUY rating**, with a **12M Target Price of R\$26.50**, which implies an **upside of +19.64%**.

Straight to the point...

Stronger volume for pulp, while paper and packaging benefit from seasonality.

With pulp shipments at 425kt (+3.7% vs. Genial Est.), the maintenance of Puma I during the past quarter has helped with efficiency and the orders' accumulation to be shipped now for 3Q23. At the same time, paper and packaging are beginning to recover volume as a result of the positive seasonality of 2Hs, although the situation is still somewhat challenging. Corrugated boxes volume was reported at 226kt (-1.0% vs. Genial Est.), up +4.8% q/q (despite the -4.4% y/y drop).

Pulp prices still in correction stages, but with better prospects looking ahead.

Due to the strong relationship with the commodity curve in Europe, which is characteristic of Klabin's shipments, the realized price of both types of pulp (BHKP and BSKP) fell again in 3Q23. Hardwood (BHKP) clocked in at US\$530/t (-2.9% vs. Genial Est.), down -18.4% q/q, while BSKP + Fluff came in worse than expected at US\$940/t (-10.1% vs. Genial Est.), down -17.4% q/q. Even so, the new outlook for 4Q23 and 2024 is more optimistic, as we commented in our preview report.

In addition, we didn't see any major movements in paper prices in 3Q23, with most segments showing stability apart from kraftliner, which was reported at R\$3,400/t (-9.4% vs. Est. Genial), a drop of -14.8% q/q and -35.2% y/y. The international environment continues to be challenging, in which the increase in US exports unbalances international supply and demand.

COGS/t inc. stoppages downtrend q/q. COGS including maintenance stoppages was R\$1,520/t (-20.2% q/q; +7.3% y/y). Factors that helped the double-digit sequential reduction were: **(i)** shrinking wood costs, which surprised us. In addition to this factor, we observed the **(ii)** Monte Alegre stoppage, with a shorter number of days with suspended production and maintenance costs compared to Puma I, which was carried out last quarter, as we had expected.

Flat EBITDA q/q, with net income missing estimates. The 3Q23 result came with a slight increase of +2.5% q/q in net revenue, reaching R\$4.4bn (-1.9% vs. Genial Est.). Exactly as we expected, EBITDA clocked in at R\$1.3bn (+0.6% q/q; -41.5% y/y), stable on a sequential basis. Even so, some factors such as more negative net foreign exchange variations than expected and the variation in biological assets led net income to R\$258mn (-73.4% q/q; -87.4%), well below our estimates.

In detail!

Kraftliner sales recovering, but prices in free fall. Although the weak market dynamics of kraftliner indicate new production stops going ahead, 3Q23 volume stood at 102kt (+4.4% q/q; -27.7% y/y), in line with our expectations of a sequential improvement in the short term, due to the ramp-up of MP28, which is starting with containerboard production, with a small conversion of cardboard boxes in the short term.

We believe that the price situation for kraftliner is still very weak, due to a challenging international environment, in which the increase in US exports ends up unbalancing international supply and demand, bringing realized prices to R\$3,400/t (-9.4% vs. Genial Est.), down -14.8% q/q and -35.2% y/y.

Lower volumes of paperboard due to the scheduled maintenance stoppage. Scheduled to last 11 days, the stoppage at Monte Alegre (PR) took place in 3Q23 and was partially offset by the start of the MP28 ramp-up, resulting in a sales volume of 165kt (+0.6% vs. Genial Est.), down slightly by -2.5% q/q and -9.2% y/y. After the adjustments that are mostly applied in Q1, with some leftover for Q2, we didn't notice anything new in the sequential realization of prices in 3Q23, which continued to be stable at ~R\$5,500/t (-1.7% vs. Genial Est.).

Corrugated boxes entering positive seasonality, but with difficulties in continuing to pass on prices. With the seasonal increase in volume in 2H, in preparation for the holiday season, sales of corrugated paper were reported at 226kt (+1.3% vs. Genial Est.), with an increase of +4.6% q/q. As we said in our preview report, which is generally correlated with inflation and GDP and is constantly adjusted in price, corrugated boxes segment has found it difficult to maintain these periodic adjustments, causing a marginal price retraction to R\$5,850/t (-0.8% vs. Genial Est.), down -1.1% q/q; and a mild rise of +1.8% y/y.

Industrial bags with a drop in exports, but with a focus on added value. The volume of industrial bags was 35.9kt (-1.2% vs. Genial Est.), basically flat sequentially and a slightly larger drop on yearly basis, of -9.2% y/y. As a factor, we highlight the decrease in exports to Latin America, but this has been reflected in an improvement in the product mix, moving away from cement and towards multiple uses, such as feed sacks, coffee, flour and others. As a result, the realized price was R\$8,900/t (-1.6% q/q; +13.8% y/y), in line with our expectations.

Pulp in strong volume, above expectations. Our expectation was that pulp shipments would surpass the quarterly production capacity of ~400kt, and indeed occurred. Klabin shipments clocked in at 425k (+3.7% vs. Genial Est.). The increase in volume was mainly due to an improvement in demand in Asia, along with greater efficiency at the Puma I unit, following scheduled maintenance stoppages.

Table 3. Net Revenue Klabin (3Q23 vs. Genial Est.)

(R\$ Millions)	2Q23			3Q23E			2Q23			3Q22		
	Reported	Genial Est.	% R/E	Reported	% q/q	Reported	% q/q	Reported	% y/y			
Net Revenue	4.400	4.485	-1,9%	4.293	4,5%	5.488	-18,3%					
Paper	1.288	1.326	-2,8%	1.338	-0,9%	1.679	-21,0%					
Packaging	1.676	1.687	-0,7%	1.608	4,9%	1.674	0,8%					
Pulp	1.355	1.393	-2,7%	1.270	9,7%	2.016	-30,9%					
Wood	90	25	255,5%	38	-32,8%	50	-49,3%					
Others	-9	54	-116,7%	39	38,4%	69	-21,7%					

Source: Genial Investimentos, Klabin

Prices continued downtrend movement, but with positive expectations going forward. Both fibers saw a further retraction in price realization, with BHKP reaching US\$530/t in 3Q23 (-2.9% vs. Genial Est.), falling -18.4% q/q. BSKP + Fluff stood at US\$940/t (-10.1% vs. Genial Est.), down -17.4% q/q.

Revenue growing marginally. With consolidated revenues reported at R\$4.4bn (-1.9% vs. Genial Est.), the top line showed a slight growth of +2.5% q/q, with an improvement in the paper and packaging businesses (+4.2% q/q paper and +6.7% q/q packaging), although pulp fell (-3.7% q/q).

COGS/t ex. stoppages rises sequentially, according to estimates. Although the cost of wood, which represents a large part of its cash cost (~50% in the current quarter), fell by -8.9% q/q, the non-stop cost hit R\$1,417/t (+0.3% vs. Genial Est.), after an increase in all other parts, such as **(i)** chemicals, **(ii)** services and **(iii)** fuel.

Accounting for downtime costs, we see maintenance at the Monte Alegre plant with a negative impact of R\$103/t (-0.1% vs. Genial Est.), down on 2Q23, due to the more relevant maintenance at Puma I, consolidating a total cash cost of R\$1,520/t (-20.2% q/q; +7.3% y/y).

Flat EBITDA, with different dynamics between the units. The pulp business division brought in an EBITDA of R\$439mn (-10.8% vs. Genial Est.), coming in worse than our projection in the face of lower-than-expected realized prices. Even so, the segment posted a performance of +12.9% q/q, with shipments being the driver behind the number on a sequential basis, as expected. As for the paper and packaging division, EBITDA was R\$913mn (+3.4% vs. Genial Est.), down -4.5% q/q and -17.2% y/y. Combining the two units, Klabin reported consolidated EBITDA of R\$1.3bn in 3Q23 (+0.6% q/q; -41.5% y/y), in line with expectations.

Table 4. EBITDA Klabin (3Q23 vs. Genial Est.)

(R\$ Millions)	2Q23			3Q23E			2Q23			3Q22		
	Reported	Genial Est.	% R/E	Reported	% q/q	Reported	% q/q	Reported	% y/y			
Adjusted EBITDA	1.352	1.375	-1,7%	1.344	2,3%	2.311	-40,5%					
Paper & Packaging	913	883	3,4%	956	-7,6%	1.103	-20,0%					
Pulp	439	492	-10,8%	389	26,6%	1.208	-59,3%					

Source: Genial Investimentos, Klabin

Net income below estimates. With negative exchange rate variations impacting the financial result, the level of net income fell short of our forecasts, mainly due to a readjustment in biological assets, an indicator outside the operational scope, and excluded from adjusted EBITDA. Although a downtrend in biological assets variation had been projected by us, the fall was more intensified than our estimates, taking net income to R\$258mn (-73.4% q/q; -87.4% y/y), a sharp drop of -67% vs. Genial Est.

Table 5. Income Statement (3Q23 vs. Genial Est.)

(R\$ Millions)	2Q23			2Q23		3Q22	
	Reported	Genial Est.	% R/E	Reported	% q/q	Reported	% y/y
Net Revenue	4.400	4.485	-1,9%	4.293	4,5%	5.488	-18,3%
COGS	(3.240)	(3.207)	1,0%	(3.124)	2,7%	(3.169)	1,2%
Adjusted EBITDA	1.352	1.375	-1,7%	1.344	2,3%	2.311	-40,5%
EBITDA Margin (%)	30,7%	30,7%	0,07p.p	31,3%	-0,66p.p	42,1%	-11,45p.p
EBIT	631	990	-36,3%	1.125	-12,0%	2.474	-60,0%
EBIT Margin (%)	14,3%	22,1%	-7,74p.p	26,2%	-4,13p.p	45,1%	-23p.p
D&A	(869)	(762)	14,0%	(794)	-4,0%	(792)	-3,7%
Financial Result	(325)	65	-601,6%	156	-58,5%	319	-79,7%
Net Income	258	802	-67,8%	971	-17,4%	2.053	-60,9%
Net Margin (%)	5,9%	17,9%	-12,02p.p	22,6%	-4,73p.p	37,4%	-19,52p.p

Source: Genial Investimentos, Klabin

Our Take on Klabin

The scenario of volatility on the macro level continues, with both the paper/packaging and pulp units suffering in the still challenging environment. Even so, we see the paper and packaging business unit's distance itself from the pulp segment, which has a much more commoditized bias. Therefore, the results are more resilient and less volatile, which seems to us a good thing in this kind of environment. Even with the MP28 ramp-up taking place, the cost of wood fell sharply in 3Q23, but this was offset by the rise in other components, resulting in a non-stop cash cost that is still on the rise.

Perfect is the enemy of good. With EBITDA going flat, the company didn't deliver representative operational growth in 3Q23. However, our view is that stability at this challenging time shouldn't be seen as a bad thing, quite the opposite. We still have a very negative outlook for non-integrated producers in the very short-term, such as Suzano in 3Q23.

Looking ahead, we expect improved results from both Klabin units, but with different dynamics. For pulp, the design of the commodity curve points to price adjustments between 4Q23 and 2024, after a complicated year-start in this regard. On the other hand, the MP28 ramp-up should continue to deliver an increase on paperboard, which, as well helps as being more resilient in price dynamics, as practically all of its volume already contracted at defined prices, better than the total realized today, which is still heavily influenced by kraftliner. Therefore, trading at an **EV/EBITDA 24E** of **6.8x** (vs. a historical average of 7.0x), we maintain our **BUY rating**, with a **12M Target Price** of **R\$26.50**, which implies an **upside** of **+19.64%**.

Appendix: Klabin

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

Income Statement	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	18.435	19.629	20.522	21.281	21.849	22.277
(-) COGS	(12.592)	(15.239)	(16.684)	(16.817)	(16.220)	(15.793)
Gross Profit	7.189	4.951	4.405	5.037	6.207	7.068
(-) Expenses	(2.810)	(2.922)	(3.087)	(3.204)	(3.295)	(3.368)
Adjusted EBITDA	6.498	6.678	6.221	7.038	8.068	8.833
(-) D&A	(3.042)	(3.105)	(3.065)	(3.042)	(3.025)	(3.013)
EBIT	4.797	4.134	3.723	4.569	5.621	6.405
(+/-) Financial Result	201	(345)	(419)	(408)	(449)	(526)
(-) Taxes	(1.232)	(929)	(811)	(1.020)	(1.267)	(1.439)
Net income	3.788	2.884	2.517	3.165	3.930	4.464
Profitability						
Net margin (%)	20,55%	14,69%	12,27%	14,87%	17,99%	20,04%

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

Cash Flow (FCFF)	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	18.435	19.629	20.522	21.281	21.849	22.277
(-) COGS	(12.592)	(15.239)	(16.684)	(16.817)	(16.220)	(15.793)
Adjusted EBITDA	6.498	6.678	6.221	7.038	8.068	8.833
EBIT	4.797	4.134	3.723	4.569	5.621	6.405
(-) Taxes	(1.232)	(929)	(811)	(1.020)	(1.267)	(1.439)
(+) D&A	3.042	3.105	3.065	3.042	3.025	3.013
(+/-) Δ WK	(180)	(237)	(120)	(83)	(41)	(44)
(-) Capex	(5.351)	(3.408)	(3.155)	(3.187)	(3.218)	(3.230)
FCFF	1.076	2.665	2.702	3.321	4.121	4.705

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under Review	Under review	5%

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