genial | Equity Research

JBS
3Q23 Preview: From today's fragility to tomorrow's strength

LatAm Meatpackers

Main takeaways:

(i) We expect an average result; **(ii)** JBS Beef North America should continue with very tight margins; **(iii)** JBS USA Pork should surprise positively, with a normalization of the supply of pigs in the USA; **(iv)** JBS Australia and JBS Brazil should show slightly lower revenues given weaker sales prices in the international market; **(v)** The downtrend in grains prices should already favor JBS USA Pork and Seara, but the impact should only be partial for now; **(vi)** We see a gradual recovery in margins over the next few quarters; **(vii)** We reiterate our **BUY rating** with a **12M Target Price** of **R$30.00**, with **+39,53%** as an **upside.**

JBS will report its 3Q23 results on November 13th, and in this report we will present our expectations for the company's figures and compare them to market expectations. We expect results with mixed dynamics once again.

Negative dynamics. On the negative side, we believe that the main points will be **(i)** a scenario that continues to be difficult for JBS Beef North America, a segment that should continue to have very pressured margins due to the low availability of cattle in the US and **(ii)** lower beef and chicken prices on the international market, which should contribute to slightly deceleration in revenues and a small sequential margin compression at JBS Brazil, Seara and JBS Australia in 3Q23.

Positive dynamics. For the positive highlights, we would point out **(i)** JBS USA Pork possibly returning to its historical level of margins, in the high single digit range and **(ii)** good prospects for the coming quarters in all segments ex-JBS Beef North America. In addition to the expectation of a gradual improvements in figures of most of the company's segments over the next few quarters, we should also count on the approval and eventual completion of the dual listing process for the shares in the US in the beginning of 2024, a factor which, in our view, should help to unlock the company's value.

Valuation and rating. In addition, we continue to see a significant upside in relation to the current share price level, since JBS is trading at a multiple of **5.2x EBITDA 24E**, below the **historical average of 5.5x**. In addition, we see the outlook for the medium and long term as favorable for the company, especially with the turning point of the cattle cycle in the US in 2025, recomposing margins gradually until reaching that phase. While this doesn't happen, in the short term, we see the normalization of chicken supply and demand, as well as the supply of hogs in the US, and although the supply of cattle in the US is still restricted, the other end of the spread remains strong, with resilient demand for beef in the country. We are also seen a favorable cattle cycle in Brazil and Australia. As a result, the company's geographical diversification supports our **BUY rating** with a **12M Target Price** of **R$30.00**.

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Company

JBSS3 BZ Equity
Buy

Price: R$ 21.50 (09-Nov-2023)
Target Price 12M: R$ 30.00

3Q23 Preview

In 3Q23, we expect total revenues of R$98.6bn Genial Est (-0.4% y/y). We project EBITDA of R$6.1bn Genial Est., down -36.5% y/y, representing a compression of -3.5 p.p. y/y in EBITDA margin, which should reach 6.1%. For net income, our model is clocking in at R$1.6bn Genial Est (-59.2% y/y).

In relation to consensus. Our estimates are 5.6% above consensus in relation to net revenue and 0.1 p.p. above in terms of EBITDA margin.

JBS Beef North America with margins still under pressure. Following the dynamics of a still restricted cattle supply in the US, even with accelerated demand, the spread for 3Q23 should still exert sequential pressure. As a result, we see the EBITDA margin remaining flat. In relation to 2Q23, we saw the cutout price retreat slightly, while the cattle cost increased marginally, highlighting the more critical moment of the current cattle cycle vs. last year.

However, we believe that over the course of 3Q23, the company corrected some internal setbacks it had, both commercially and in relation to the White Bone plan (linked to initiatives to maximize cattle profitability), which should have offset the slight worsening in the industry and therefore enabled stable margins.

In our view, both in 4Q23 and throughout 2024, the cattle supply in the US will remain considerably soft, contributing to the segment's EBITDA margin still marking a low to mid-single digit figure. We see a slow recovery towards greater availability of cattle, and consequently margins, during next year up 2H25, when we probably going to observe a turning point of the cycle.

We expect stronger prices at JBS USA Pork. In our assessment, prices for the pork division are in a more favorable period in the US, considering a shorter cycle than cattle. We observed a significant advance in the cutout price in July, combined with lower grain prices, which have fallen in the spot price since the beginning of the year, but should only begin to benefit JBS operations now in 3Q23, due to the delay in the composition of inventories. Our estimates also point to an adverse scenario for agricultural commodities such as corn and soybeans, which may help to reduce the costs of raising hogs, along with an improvement in the supply of animals at the slaughter stage. The large harvests in Brazil and the premiums at the ports, which are still at a negative value, should keep grain prices down for the next few months.

As a result, we estimate strong margins for the segment, and strong sequential expansion, bringing the EBITDA margin into the high single digit range. For 2024, we expect the EBITDA margin to oscillate between mid and high single digit, with the segment ending the year with an EBITDA margin within the historical range presented by the segment (8% to 10%).

As for JBS Australia, we expect prices to slow down but margins to increase. With weaker beef sales prices on the international market, we should see a small sequential retraction in the segment's top-line, given that ~66% of the operation's beef production is destined for export. This drop in prices should also have had a slight impact on the segment's margins, which should show a slight compression compared to 2Q23.

In October, we already saw the cattle availability with better prospects than the 3Q23 average, and beef sales prices on the international market improving slightly. We estimate, for 4Q23, an EBITDA margin of high single digits and close to double digits. For 2024, we are estimating an EBITDA margin of around low double digits, making the segment one of the company's best in terms of margins next year.

JBS Brazil's positive cattle cycle shouldn't be enough to offset other weaker dynamics that we expect. JBS Brazil's segment revenue should feel the negative impact of weaker international sales prices. This momentary downtrend in prices (-4% a/a) was greater than the fall in the cattle cost, supported by the positive phase of the cycle. In addition, the leather segment continues to be with poor dynamics, with a weak automotive industry. To top it off, the Swift product line and stores will continue to be a margin detractor (with several stores at a mature stage and not reached breakeven yet). As a result, we are expecting a slightly more compressed EBITDA margin now in 3Q23 on a quarterly basis.

For 2024, we see the cattle cycle in Brazil remaining favorable, given the high availability of cattle by the atypical retention of females that occurred. If prices on the international market rise again, and the USD/BRL exchange rate remains favorable (~5 BRL/USD), we should see mid to high single digit margins over the quarters. We also see the segment benefiting from higher beef exports to the US (while the cycle remains negative there).

It's worth noting that we expect the cattle cycle in Brazil to turn around only in mid-2025. So, there's good ground ahead for higher margins for Brazilian slaughter plants in general. Therefore, given that the maturities of a representative number of Swift stores are shorter than the end of the bullish phase of cattle cycle, we believe that profitability will return to the business unit a little further down the line.

The fall in grain prices will help Seara, but for 3Q23 lower poultry prices will make it difficult to advance margins. We estimate slightly weaker revenues than in 2Q23, due to lower selling prices for chicken on the international market and lower volumes. In addition, with lower demand from the foreign market, we believe that there will be more chicken meat left on the domestic market, also pushing down prices on the domestic market.

It's worth mentioning that when chicken prices fall down, the tendency is for people to consume more fresh chicken than processed meat, such as sausage (where JBS has higher margins), further impoverishing the segment's profitability. However, we believe that the downtrend in grain prices should already benefit the operation this quarter, although the impact is not yet complete due to hedging issues and the fact that the company still has high average inventory costs. We estimate mid-single digit EBITDA margin in 3Q23, but we expect further advances in profitability over the next few quarters.

As a result, we see the segment showing a gradual recovery in margins, with the drop in grains benefiting results even further, until the operation returns to its historical EBITDA margin level (10 to 12%).

Table 1. Income Statement JBS (3Q23 Genial Est.)

(R$ millions)	3Q23E Genial Est.	2Q23 Reported	% q/q	3Q22 Reported	% y/y
Net Revenue	**98.579**	**89.383**	**10,3%**	**98.928**	**-0,4%**
COGS	(86.434)	(79.496)	8,7%	(82.692)	4,5%
Gross Profit	**12.145**	**9.887**	**22,8%**	**16.236**	**-25,2%**
Gross Margin (%)	12,3%	11,1%	1,26p.p	16,4%	-4,09p.p
EBITDA	**6.057**	**4.470**	**35,5%**	**9.546**	**-36,5%**
EBITDA Margin (%)	6,1%	5,0%	1,14p.p	9,6%	-3,51p.p
Net Income	**1.638**	**-264**	**-**	**4.014**	**-59,2%**
Net Margin (%)	1,7%	-0,3%	-	4,1%	-2,4p.p

Source: Genial Investimentos, JBS

Our Take on JBS

Despite mixed dynamics in our projections for 3Q23, with most business units facing some challenges, our estimates are for incremental improvements for 2024 and 2025. Given the ~20% drop in share price during 1H23, even though JBS's current trading value has shown a recovery since September, we still believe the company was extremely undervalued.

From today's fragility to tomorrow's strength. As investors react very much to the short term, and the most representative improvements are only likely to happen from next year onwards, we believe that there may be a balance in the shares prices as a result of a slightly weaker figures in 3Q23, after the recent rise. Even so, we maintain our more positive bias looking a little further ahead. We project a sequential recovery in consolidated margins over the next few quarters, driven by **(i)** normalization of global chicken supply and demand; **(ii)** normalization of US pork supply; **(iii)** resilient US beef demand and **(iv)** a favorable cattle cycle in Brazil and Australia.

We also see the process of dual listing of the company's shares as interesting for unlocking the company's value in the medium and long term, and, in our view, its approval as a trigger for the appreciation of the shares in the short term. We see the company trading at **5.2x EBITDA 24E**, below the historical average of 5.5x, and we continue to see a relevant upside in relation to the current screen price. We therefore reiterate our **BUY rating** with a **12M Target Price** of **R$30.00**.

Appendix: JBS

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

Income Statement	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**366.791**	**374.002**	**394.316**	**455.465**	**463.609**	**481.169**
(-) COGS	(324.608)	(317.344)	(333.332)	(384.967)	(388.460)	(400.258)
Gross Profit	**42.183**	**56.658**	**60.984**	**70.498**	**75.149**	**80.911**
(-) Expenses	(22.197)	(29.491)	(33.647)	(41.007)	(46.155)	(45.672)
Adjusted EBITDA	**19.986**	**27.167**	**27.336**	**29.492**	**28.994**	**35.238**
(-) D&A	(10.817)	(9.770)	(7.816)	(6.595)	(2.443)	(2.443)
EBIT	**9.169**	**17.397**	**19.520**	**22.897**	**26.551**	**32.796**
(+/-) Financial Result	2.698	5.758	5.863	7.837	7.896	7.983
(-) Taxes	(4.160)	(7.873)	(8.630)	(10.450)	(11.712)	(13.865)
Net income	**7.708**	**15.282**	**16.753**	**20.284**	**22.735**	**26.914**
Profitability						
Net margin (%)	2,10%	4,09%	4,25%	4,45%	4,90%	5,59%

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

Cash Flow (FCFF)	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**366.791**	**374.002**	**394.316**	**455.465**	**463.609**	**481.169**
(-) COGS	(324.608)	(317.344)	(333.332)	(384.967)	(388.460)	(400.258)
Adjusted EBITDA	**19.986**	**27.167**	**27.336**	**29.492**	**28.994**	**35.238**
EBIT	**9.169**	**17.397**	**19.520**	**22.897**	**26.551**	**32.796**
(-) Taxes	(4.160)	(7.873)	(8.630)	(10.450)	(11.712)	(13.865)
(+) D&A	10.817	9.770	7.816	6.595	2.443	2.443
(+/-) Δ WK	178	(418)	(2.200)	(2.657)	(363)	(794)
(-) Capex	(8.814)	(9.770)	(7.816)	(6.595)	(2.443)	(2.443)
FCFF	**7.190**	**9.106**	**8.690**	**9.790**	**14.476**	**18.137**

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Buy	Expected return above +10% in relation to the Company's sector average	**49%**
Neutral	Expected return between +10% and -10% relative to the Company's industry average	**41%**
Sell	Expected return below -10% in relation to the Company's sector average	**5%**
under Review	Under review	**5%**

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