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MINERVA

3Q23 Review: It rained, but the result was drained

LatAm Meatpackers

Main takeaways:

(i) We saw a weak result, with net revenue lower than expected, due to poor dynamic on sales prices in both foreign and domestic markets, and margins slightly lower than we had estimated; **(ii)** Brazil was the main positive highlight, due to the more favorable cattle cycle; **(iii)** Paraguay was the main negative highlight, being affected by weather problems in the country (excessive rain); **(iv)** We remain optimistic about China's structural demand for beef in the medium and long term, but in the short term we see a demand that should not sustain a high price level; **(v)** We believe that Paraguay should once again shine in the company's results if the weather problem ceases; **(vi)** Minerva is trading at **4.0x EV/EBITDA 24E**, way below historical average of 5.4x EV/EBITDA. So, we reiterate our **BUY rating** with a **12M Target Price** of **R$14.00,** giving the shares an **upside** of **+77.66%**.

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Company

BEEF3 BZ Equity
Buy

Price: R$ 7.88 (08-Nov-2023)
Target Price 12M: R$ 14.00

Minerva released its 3Q23 results today, after the market closed. It was a weak quarter, considering that **net revenue came in below our expectations** and we were already more pessimistic than consensus. With a more impoverished revenue dynamic and similar costs, the EBITDA margin was also below our projections. On a quarterly basis, there was a small increase in volume (+5.5% q/q in the foreign market and +7.6% q/q in the domestic market), but sales prices were lower (-8.3% q/q in the foreign market and -5.6% q/q in the domestic market).

In this case, **the increase in volume did not offset the downtrend in prices**, causing revenue to shrink. As for the EBITDA margin, we saw a small expansion both year-on-year (+0.5 p.p. y/y) and on quarterly basis (+0.3 p.p. q/q), made possible by the more positive cattle cycle in Brazil. **Brazil** was the quarter's main **positive highlight**, due to the **favorability of the cycle**, marked by a high availability of cattle and, consequently, low acquisition costs for animals at the slaughter stage. **Paraguay, on the other hand, was the main negative highlight**, due to atypical weather problems in the country in 3Q23. Excessive rainfall made it difficult to transport livestock cargo to the slaughter plants, significantly reducing volume.

Valuation and rating. Although we classify the 3Q23 result as discouraging, we try to look at other characteristics that make us believe that Minerva's performance tends to be better than its peers in the short term. We ascertained a **considerable discount** when we see that Minerva is trading at **4.0x EV/EBITDA 24E** (vs. historical average of 5.4x EV/EBITDA). We expect that **(i)** the positive cattle cycle in Brazil will continue to favor margins; **(ii)** the company will once again benefit from the positive cycle in Paraguay, after the weather adversities that were atypical and exclusively affected this quarter; **(iii)** the volume of beef exports to the US will grow, given the negative cattle cycle in the country and **(iv)** Chinese structural demand for beef will continue to grow in the medium and long term. We therefore reiterate our **BUY rating** for the company's shares, with a **12M Target Price** of **R$14.00**.

Net revenue was reported at R$7.1bn (-6.0% vs. Genial Est), down -16.2% y/y. EBITDA stood at R$714mn (-9.4% vs. Genial Est.), down -11.5% y/y. As a result, the company achieved an EBITDA margin of 10.1% (-0.4 p.p. vs. Genial Est.), which despite being below expectations, achieved growth of +0.5 p.p. y/y. The slight margin expansion reflected lower costs, mainly due to the greater availability of cattle in Brazil. Finally, net income was R$141mn (-35.3% vs. Genial Est.), marking a slowdown of -0.4% y/y, and consolidating a weaker performance delivery than we were expecting.

Positive points. The main positive highlights of 3Q23 were **(i)** the positive cattle cycle in Brazil, which enabled a margin expansion of +0.3 p.p. q/q and +0.5 p.p. y/y; **(ii)** Net revenue growth in Uruguay (+2.1% q/q; +29.5% y/y), due to a greater boost in volumes (+5.2% q/q; +63.5% y/y), despite the tighter supply of cattle putting pressure on costs; and **(iii)** the viability of the strategy of exporting a greater volume of beef to the US, which is suffering from the unfavorable cattle cycle, pushing up COGS. The cuts' prices are also up driven by strong demand. By offering a product that originates in a country where the cost of slaughter is lower, the sales margin tends to rise. We are optimistic about that.

Negative points. On the negative side, we saw **(i)** a drop in average beef sales prices (-8.3% q/q on the foreign market and -5.6% q/q on the domestic market), damaging net revenue, which slowed by -2.5% q/q, despite higher volumes (+5.5% q/q on the foreign market and +7.6% q/q on the domestic market); **(ii)** even weaker volumes in Argentina (-9.3% q/q; -11.8% y/y), impacted by the country's economic and political volatility; **(iii)** Paraguay with discouraging figures, delivering anemic revenue (-23.4% q/q; -28.5% y/y), as a result of the climatic problem of excessive rainfall faced in the region in 3Q23; **(iii)** Revenue in Brazil with timid growth on a quarterly basis (+3.9% q/q), despite strong acceleration in volumes (+26.2% q/q), due to sales pricing with impoverished dynamics.

Chinese structural demand should continue to grow in the medium and long term, but in the short term it may face bumps. Although we saw stronger demand in July, it weakened significantly in August. There was also a drop in export volumes, with a small rebound in September. In our view, the RMB/USD exchange rate is one of the factors that helps explain this short-term volatility.

In the short term, we see demand not being strong enough to sustain higher beef sales prices. We therefore estimate that in the coming quarters, even with Chinese demand helping to contribute to sequentially higher export volumes, sales prices should remain close to stable. However, in the medium and long term, we remain optimistic due to factors such as **(i)** the westernization of demand for beef protein in China; **(ii)** the expansion of the Chinese middle class and **(iii)** beef consumption per capita in China is still well below the world average, with ample room for growth (~4kg per capita vs. ~15kg OECD average).

More focus on export strategy to the US. In our view, the scenario of low cattle availability, and consequently higher costs, combined with a resilient demand for beef in the US market, offers a great opportunity for Minerva to benefit as it can **(i)** increase the volume of processed beef exported from Brazil and **(ii)** export a higher volume of premium cuts from Uruguay. This dynamic could help Minerva to grow its top line.

Table 1. Income Statement Minerva (3Q23 vs. Genial Est.)

(R$ millions)	3Q23 Reported	3Q23E Genial Est.	% R/E	2Q23 Reported	% q/q	3Q22 Reported	% y/y
Net Revenue	**7.068**	**7.517**	**-6,0%**	**7.277**	**-2,9%**	**8.438**	**-16,2%**
COGS	(5.591)	(6.057)	-7,7%	(5.765)	-3,0%	(6.779)	-17,5%
Gross Profit	**1.478**	**1.460**	**1,2%**	**1.512**	**-2,3%**	**1.659**	**-10,9%**
Gross Margin (%)	20,9%	19,4%	1,48p.p	20,8%	0,13p.p	19,7%	1,24p.p
EBITDA	**714**	**788**	**-9,4%**	**711**	**0,4%**	**806**	**-11,5%**
EBITDA Margin (%)	10,1%	10,5%	-0,39p.p	9,8%	0,33p.p	9,6%	0,54p.p
Net Income	**141**	**218**	**-35,3%**	**121**	**16,5%**	**142**	**-0,4%**
Net Margin (%)	2,0%	2,9%	-0,91p.p	1,7%	0,33p.p	1,7%	0,32p.p

Source: Minerva, Genial Investimentos

Our Take on Minerva

For the next few quarters, we project a small increase in top line, driven more by the volume variable than the price, given that beef sales prices should remain stable in the short term. We believe that the company's positive highlights should continue to come mainly from Brazil.

It rained, but the result was drained. We believe that the main factor that led us to classify the result as negative was the excessive rainfall, which hampered the logistics of live cargo to slaughterhouses in Paraguay. Although we were aware of this situation, and mentioned this dynamic in our results preview, which is attached below (3Q23 Preview: Just a scratch...), the reduction in volume was more intense than our projections. Minerva delivered a shipment volume of 51.4Kt (-5.3% vs. Genial Est.) through its plants in Paraguay, which implies a reduction of -17.2% y/y.

We have to consider that the biggest disappointment in 3Q23 is linked to a one-off dynamic. This is because the company has already confirmed that logistics to the slaughter plants have been re-established, given the normalization of the climate problem of excessive rainfall in Paraguay. Rainfall in September and October exceeded 16x the historical average, caused by the abnormal rise in temperature linked to the El Niño phenomenon. We therefore believe that the country will once again shine in the company's results as the situation has settled down.

In addition, back to commenting on the main topic surrounding investors' discussions today when it comes to Minerva, related to the process of acquiring Marfrig's 16 plants for R$7.5bn. Undoubtedly, we believe that this dynamic has brought an additional dose of uncertainty to the investment thesis. This is due to the lack of confidence in the assets' real need for working capital, which are supposed to be plug-and-play. in addition, investors seem to be extremely concerned about the debt increase, pulling up the company's leverage, reaching **3.3x Net Debt/EBITDA 23E** vs. 2.5x in our previous estimates before the acquisition.

We have seen some short positions being structured. We believe that investors have set up short positions in the company's shares and any slightest reason to deviate from consensus expectations could create considerable selling pressure. So, we expect a negative reaction from investors tomorrow. Even if this came up to be true, and the stock prices were to fall very sharply, **the move would not be rational**.

But why are we still bullish? We ascertained a considerable discount when we see that Minerva is trading at **4.0x EV/EBITDA 24E** (vs. historical average of 5.4x EV/EBITDA). We are aware the uncertainties related to the acquisition and for the increase in the company's leverage, which already this quarter showed signs of rising, going to **2.8x Net Debt/EBITDA LTM** (vs. 2.2x in 3Q22, and basically stable vs. 2Q23).

However, we believe that Minerva is still currently positioned with the **most favorable operation dynamics among peers in short term**. We list them as: **(i)** the favorable cattle cycle in Brazil and Paraguay, with a possible inflection in Uruguay (which we see occurring at the end of 1H24); **(ii)** long-term structural Chinese demand, which should ensure growth in export volumes and **(iii)** a higher volume of exports to the US market.

As the figures delivered by the company were weaker than the market had expected, and as we said, we believe that the **shares could face selling pressure tomorrow**, but trigged to an event that will not be repeated. From a rational point of view, we continue to see a **relevant asymmetry between the price and the fair value of the company.** So, we reiterate our **BUY rating**, with a **12M Target Price** of **R$14.00**.

Appendix: Minerva

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

Income Statement	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**28.110**	**29.841**	**32.303**	**33.112**	**34.244**	**35.986**
(-) COGS	(22.662)	(23.523)	(25.817)	(26.588)	(27.714)	(29.028)
Gross Profit	**5.447**	**6.318**	**6.487**	**6.525**	**6.530**	**6.958**
(-) Expenses	(2.794)	(2.995)	(3.245)	(3.258)	(3.380)	(3.576)
Adjusted EBITDA	**2.653**	**3.322**	**3.242**	**3.267**	**3.150**	**3.382**
(-) D&A	(537)	(458)	(494)	(509)	(515)	(517)
EBIT	**2.117**	**2.864**	**2.748**	**2.758**	**2.635**	**2.865**
(+/-) Financial Result	(1.445)	(1.649)	(1.299)	(1.126)	(1.418)	(1.331)
(-) Taxes	(94)	(199)	(237)	(267)	(199)	(251)
Net income	**578**	**1.017**	**1.212**	**1.365**	**1.018**	**1.283**
Profitability						
Net margin (%)	2,05%	3,41%	3,75%	4,12%	2,97%	3,57%

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

Cash Flow (FCFF)	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**28.110**	**29.841**	**32.303**	**33.112**	**34.244**	**35.986**
(-) COGS	(22.662)	(23.523)	(25.817)	(26.588)	(27.714)	(29.028)
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EBIT	**2.117**	**2.864**	**2.748**	**2.758**	**2.635**	**2.865**
(-) Taxes	(94)	(199)	(237)	(267)	(199)	(251)
(+) D&A	537	458	494	509	515	517
(+/-) Δ WK	2	(91)	7	(10)	(1)	(34)
(-) Capex	(1.356)	(1.139)	(741)	(610)	(566)	(517)
FCFF	**1.206**	**1.893**	**2.271**	**2.379**	**2.383**	**2.580**

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	Definition	Coverage
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%**
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under Review	Under review	**5%**

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