Equity Research

SLC AGRICOLA

4Q23 review: Not bad, but not good enough.

LatAm Agribusiness

Main takeaways:

(i) We saw solid revenue, with a small drop year-on-year, and an EBITDA margin above our projections; **(ii)** Falling agricultural commodities should continue to be a headwind to the company's operations at least of couple of quarters; **(iii)** Higher cotton prices helped to sustain the company's operations; **(iv)** Negative marking of the variation in the fair value of the biological assets of the first soybean crops strongly damaged the bottom line; **(v)** Adjustments to its planting mix, cutting supply, could **help to mitigate demand imbalance** if other peers (including small producers) adopt the same idea; **(vi)** We reiterate our **BUY rating** with a **12M Target Price** of **R$23.50**.

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Company

SLCE3 BZ Equity
Buy

Price: R$ 19.35 (06-Mar-2024)
Target Price 12M: R$ 23.50

SLC delivered a solid quarter in terms of revenue (despite bad conditions for price realizations), with a top-line above our expectations (+11.4% vs. Genial Est.), and an interesting performance regarding EBITDA margin, also above our projections (+3.7p.p. vs. Genial Est.), despite the headwinds faced. As a result, the company achieved revenues down slightly year-on-year (+16.4% q/q; -1.4% y/y), due to slightly lower land productivity, but a good EBITDA margin (+5.2 p.p. y/y; +1.8 p.p. y/y). We attribute this performance to the **downward trend** in the price of the main commodities (**corn and soybeans**), partially **offset by better cotton prices**.

The company reported net revenue down -1.4% y/y, clocking in at R$1.9bn (+11.4% vs. Genial Est.), and EBITDA of R$673mn (+24.5% vs. Genial Est.), accelerating +3.9% y/y, representing an EBITDA margin of 35.1% (+3.7p.p. vs. Genial Est.), expanding +1.8p.p. y/y. We would point out that in the main operating metrics, **SLC's performance exceeded our estimates**.

Table 1. Income Statement SLC (4Q23 vs. Genial Est.)

(R$ millions)	4Q23A Reported	4Q23E Genial Est.	% R/E	3Q23A Reported	% q/q	4Q22A Reported	% y/y
Net Revenue	**1.919**	**1.723**	**11,4%**	**1.648**	**16,4%**	**1.946**	**-1,4%**
COGS	(1.785)	(1.200)	48,8%	(1.062)	68,1%	(1.389)	28,5%
Gross Profit	**134**	**523**	**-74,4%**	**586**	**-77,2%**	**557**	**-76,0%**
Gross Margin (%)	7,0%	30,4%	-23,39p.p	35,6%	-28,61p.p	28,6%	-21,66p.p
EBITDA	**673**	**541**	**24,5%**	**492**	**36,9%**	**648**	**3,9%**
EBITDA Margin (%)	35,1%	31,4%	3,7p.p	29,8%	5,25p.p	33,3%	1,78p.p
Net Income	**(153)**	**182**	**-184,1%**	**158**	**-196,8%**	**132**	**-215,5%**
Net Margin (%)	-8,0%	10,6%	-18,54p.p	9,6%	-17,56p.p	6,8%	-14,78p.p

Soure: SLC, Genial Investimentos

Valuation and rating. Although the situation remains challenging, with a continuing downward trend in soybean and corn prices, since the reduction in planted area by some producers has not yet had the desired effect on prices, we still maintain an optimistic bias considering that SLC has an exposure to cotton, which helps to hold back the fall in other commodities. In addition, we see the company trading at an **EV/EBITDA 24E** of **6.2x** (below the historical average of 6.7x). We therefore reiterate our **BUY rating** with a **12M Target Price** of **R$23.50.**

4Q23 Review

Despite mostly operational lines above expectations, and even with an EBITDA margin expansion, the company was unable to avoid a loss, that ended up being of -R$153mn (-184.1% vs. Genial Est.), down -215.5% y/y, due to a strong negative mark-to-market impact on the fair value variation of biological assets related to first soybean plantations.

Headwinds hampered the consolidated result. The challenging scenario continues in the agricultural sector, and SLC faced setbacks such as **(i)** corn and soybean prices remaining on a downward trend; (**ii**) lower soybean productivity; **(iii)** delays in cotton shipments at ports and **(iv)** negative marking to market effect about the change in the fair value of the biological assets, related to first planted soybean crops, which suffered from the drought in Mato Grosso (MT). All these factors were decisive for the gross result of R$423mn, with the reversal of net income into a loss in the bottom line.

In our view, the downward trend in soybeans and corn should persist over the next few quarters, since we don't see any global indicators that suggest a price recovery in the short and medium term. As we have commented in past reports, at the end of last year we believed that the reduction in the planted area by some producers in Brazil could cause commodity prices to rise due to a better balance of supply and demand.

However, even with that reduction taking place, corn and soybean prices are still below the historical average of recent years. This situation is likely to negatively affect the operations of SLC and other companies in the sector.

The cotton crop has made a positive contribution. Unlike soybeans and corn, cotton has sustained good prices on the international market, which contributed positively to the company's operations in 4Q23. We continue to be optimistic about cotton, due to **(i)** resilient demand, driven by the high consumption of clothing in the US and the recovery of the industry in Asia; **(ii)** the low productivity of the current crop in the US and **(iii)** possible climate problems, resulting from La Niña (from 2Q24), in the US state of Texas, the country's main cotton producer, which should contribute to the commodity continuing to be traded at a good price level.

Our Take on SLC

We believe that there may be good opportunities to buy land. With a scenario of tight margins for producers, it is likely that opportunities will arise for both leasing and purchasing agricultural land. We believe that publicly traded companies in the sector, which have greater access to the capital markets for leverage, could particularly benefit from opportunities to buy land at more attractive terms.

Smaller producers may suffer more from the precarious profitability situation of corn, soybeans and cattle and lower their demands in terms to negotiate land values. We are proponents of the idea that the time is not ripe for SLC to sell land (revenues from land sales are expected to fall in the 2024/25 harvest as well), but rather to look for good opportunities and close attractive deals, anticipating the turn of the cycle (which will come at some point).

Adverse weather conditions have contributed to changes in the mix. Due to difficult weather conditions that impacted the planting window, SLC announced adjustments to its planting mix, reducing the soybeans planted area in order to improve margins in the 1st cotton crop. With these adjustments, soybeans were reduced by -5.0%, 1st crop of cotton increased by +18.5%, 2nd crop cotton reduced by -15.8% and 2nd crop corn reduced by -6.5%. We welcome this move since, although there is still no effect on price recovery, other producers may adopt this approach and reduce supply in order to rebalance profitability conditions, which could cause a trigger down the road.

Not bad, but not good enough. Although the company's operational lines performed better than expected and the EBITDA margin expanded y/y, it still recorded a loss of -R$153mn (-184.1% vs. Genial Est.). Despite the challenges expected for corn and soybeans over the course 1H24, with their prices falling, as well as land productivity, we maintain an optimistic bias for sugar and cotton. We also see the company trading at an **EV/EBITDA 24E** of **6.3x**, compared to a historical average of 6.7x. We therefore reiterate our **BUY rating**, with a **12M Target Price of R$23.50**, which indicates an important **upside** of **+21,45%**.

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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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