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MINERVA

2Q24 Review: Airplane without a wing

LatAm Meatpackers

Main takeaways:

(i) Exports to the US boost revenue: R$7.7bn (-2.3% vs. Genial Est.), accelerating +6.1% q/q and +5.2% y/y; **(ii)** cattle availability in Brazil generates good opportunity to improve shipments y/y; **(iii)** Alignment of stars for Minerva's operation: **EBITDA of R$745mn** (+2.3% vs. Genial Est.), composing a increase of +18.4% q/q and +4.7% y/y; **(iv)** Podium for Paraguay: Revenues on region growing +39.0% q/q; +3.3% y/y; **(v) R$404mn** of **FCF** generation in 2Q24; **(vi)** Successful hedge operation; **(vii)** Risk of cycle mismatch in 26/27; **(viii)** Acquisition of Marfrig's assets held down the shares; **(ix)** We believe that the **uncertainties about the acquisition** are **already reflected in the share price**. In addition, we consider the **company to be undervalued**, as its well positioned to collect favorable operating performance dua to its high exposure on Brazil positive cattle cycle. Therefore, we reiterate our **BUY rating**, with a **12M Target Price** of **R$9.00**, setting up an **upside** of **+29.68%**.

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Company

BEEF3 BZ Equity
Buy

Price: R$ 6.94 (07-Aug-2024)
Target Price 12M: R$ 9.00

Minerva released its **2Q24 on August 7th, after the market closed**. In summary, we understand that the investment thesis linked to the **creation of beef export platform** can be seen as the centerpiece of the quarter's performance. Minerva reported net revenue of R$7.7bn (-2.3% vs. Genial Est.), representing an increase of +6.1% q/q and +5.2% y/y, driven by the **high representativeness of exports**, which totaled 61.4% of the top line. The company achieved **EBITDA of R$745mn** (+2.3% vs. Genial Est.), with growth of +18.4% q/q and +4.7% y/y. As a result, the company achieved a **margin of 9.7%,** in line with our projections, equivalent to an **expansion of +0.3p.p. y/y**.

That margin expansion was derived by the favorable dynamics for the company, which acquires cattle in a cycle of high availability in Brazil and sells on the foreign market exposed to a negative cycle, also taking advantage of a significant **appreciation of the USD/BRL exchange rate**. Finally, the company reported a net income of R$95m (vs. R$11m Genial Est.), a contraction of -20.9% y/y, but reversing the loss of the previous quarter.

The **exchange rate variation** generated **impacts on FCF** through accounts receivable, which consumed -R$790mn in **working capital** and also a negative effect of -R$1.0bn on debts held in USD, which were successfully offset by the company's hedging policy, constituting +R$1.1bn.

Valuation and rating. In 2Q24, Minerva registered a remarkable growth in net revenue, reaching R$7.7bm (-2.3% vs. Genial Est.), an increase of +6.1% q/q and +5.2% y/y. This performance **was largely driven by exports**, which accounted for 61.4% of total revenue, benefiting from the negative cattle cycle in the US (tight supply of cattle). Countries such as Brazil and Paraguay, newly eligible to export to the US, took advantage of this opportunity, significantly increasing their sales. Exports to the NAFTA region also increased, reflecting a successful foreign market strategy.

Minerva reported an EBITDA of R$745mn (+2.3% vs. Genial Est.), accelerating +18.4% q/q and +4.7% y/y. The positive operating delivery is due to the **favorable dynamics of cattle acquisition** in a cycle of **high availability in Brazil**, while sales benefited from a negative cycle in the foreign market, especially the US, and the appreciation of the USD/BRL exchange rate. The company managed to balance the challenging seasonality in Brazil with effective operations abroad. We are concerned about the **potential mismatch of cattle cycles between the US and Brazil in 2026/2027**. Currently, the cattle cycle in Brazil is positive, but the expectation is that it will reverse before the negative cycle in the US ends. If this occurs, both countries could face negative cycles simultaneously, putting **pressure on the global beef spread** due to the reduction in cattle supply. However, **in the short term, Minerva continues to benefit from a favorable operating scenario** due to its strong exposure to the Brazilian and Paraguayan markets.

The **acquisition of Marfrig's assets**, currently **under evaluation by CADE**, is a critical issue for the company. The transaction is considered expensive by the vast majority of investors (~9.5x EV/EBITDA) and **raises concerns about taking advantage of the positive cycle window in Brazil before it turns negative**. The uncertainty over the approval has already limited the appreciation of Minerva's shares, keeping them in a sideways movement. In addition, the political and economic complexity in Uruguay, where part of the acquired assets is located, adds an additional layer of uncertainty.

CADE's decision will significantly influence the response of the Uruguayan antitrust body (CPDC), making the outcome even more unpredictable. Even so, we believe that the **uncertainties** surrounding the acquisition **are already reflected in the share price**. In addition, we consider the **company to be undervalued**, as its well positioned to collect favorable operating performance dua to its high exposure on Brazil positive cattle cycle. Therefore, we reiterate our **BUY rating**, with a **12M Target Price** of **R$9.00**, setting up an **upside** of **+29.68%**.

2Q24 Review

Table 1. Income Statement Minerva (2Q24 Genial Est.)

(R$ millions)	2Q24 Reported	2Q24E Genial Est.	% R/E	1Q24 Reported	% q/q	2Q23 Reported	% y/y
Net Revenue	**7.666**	**7.847**	**-2,3%**	**7.187**	**6,7%**	**7.276**	**5,4%**
COGS	(6.001)	(6.240)	-3,8%	(5.758)	4,2%	(5.764)	4,1%
Adjusted EBITDA	**745**	**728**	**2,3%**	**629**	**18,4%**	**711**	**4,7%**
EBITDA Margin (%)	9,7%	9,3%	0,44p.p	8,8%	0,96p.p	9,8%	-0,06p.p
EBIT	**571**	**612**	**-6,6%**	**477**	**19,9%**	**571**	**0,0%**
EBIT Margin (%)	7,5%	7,8%	-0,35p.p	6,6%	0,82p.p	7,9%	-0,4p.p
D&A	149	116	29,1%	152	-1,9%	140	6,9%
Financial Result	(493)	(595)	-17,2%	(627)	-21,4%	(427)	15,4%
Net Income	**95**	**11**	**758,0%**	**(186)**	**-**	**121**	**-20,9%**
Net Margin (%)	1,2%	0,1%	1,1p.p	-2,6%	3,84p.p	1,7%	-0,41p.p

Source: Minerva, Genial Investimentos

Exports to the US boost revenue. One of the highlights of 2Q24 was the growth in net revenue (+6.1% q/q; +5.2% y/y), reaching R$7.7bn (-2.3% vs. Genial Est.), driven by the representativeness of exports, which accounted for 61.4% of the top line. We understand that this was due to the negative cattle cycle in the US, which is facing a restricted supply. Countries such as Paraguay, which was recently authorized to export to the US, and Brazil benefited from this situation and made a good volume of shipments. Sales on the foreign market stood at 218.9Kt (+7.7% q/q; +10.4% y/y), while on the domestic market they were reported at 143.8Kt (+0.6% q/q; +24.1% y/y). It's worth mentioning that the NAFTA region increased its share of exports by +7p.p q/q.

Gold medal for Brazil. The high availability of cattle in Brazil during 2Q24 led Minerva to partially offset the more challenging seasonality of the period, although it did not escape a sequential slowdown. The region showed a decline of -4.4% q/q, but with an increase of +2.9% y/y in gross revenue. Shipments, on the other hand, fell slightly sequentially by -3.4% y/y, but we saw a strong rise of +24.5% y/y, which was consolidated by the greater appetite for exports, as we've already mentioned.

Podium for Paraguay. Paraguay and Uruguay were the countries with the most positive quarter-on-quarter variations. While Paraguay managed to increase its level of exports to the US, for example, Uruguay managed to access more premium markets, such as Japan and Korea. As a result, we see Paraguay's gross revenue reported at R$1.3bn (+39.0% q/q; +3.3% y/y) and Uruguay's R$909mn (+22.5% q/q; +15.0% y/y).

Alignment of stars for Minerva's operation. Minerva reported EBITDA of R$745mn, (+2.3% vs. Genial Est.), in line with our projection and up +18.4% q/q and 4.7% y/y. We believe that the secret to this increase lies in the very favorable dynamics for the company, which acquires cattle in a cycle of high availability in Brazil and sells them on the foreign market exposed to a negative cycle, also taking advantage of a significant appreciation in the USD/BRL exchange rate. This situation is the basis for the investment thesis in Minerva, consolidating a beef export platform and arbitraging price through different positions in the cattle cycle.

Successful hedge operation, but net income still anemic. The USD/BRL EoP exchange rate reached R$5.56 (vs. R$5.00 in 1Q24), accelerating +11.3% q/q. However, Minerva has a policy of keeping at least 50% of its foreign currency debt (~76% of gross debt) protected through hedging operations. Therefore, in the quarter, the company faced a significant negative impact from the exchange rate variation (-R$1.0bn) but achieved greater positive effects from the derivative operation (+R$1.1bn). As a result, the reported financial result was -R$493mn (-21.4% q/q; +15.4% y/y). Therefore, net income stood at R$95mn, a contraction of -20.9% y/y, but reversing the loss of 1Q24.

Our Take on Minerva

Risk of cycle mismatch on 26/27. The current market outlook indicates a possible extension of the negative cattle cycle in the US until 2026, or it could last until the beginning of 2027 even. If this forecast comes true, the chances of a mismatch at the turn of the cycle between the US and Brazil will increase, which could harm the strategies of companies such as JBS (to a greater extent) and Minerva (to a lesser extent).

Currently, the cattle cycle in Brazil is positive, but we believe that it will reverse to negative before the cycle in the US changes from negative to positive. In other words, there is a strong possibility that the time windows of the cycles will mismatch, resulting in both countries facing negative cycles simultaneously. If this occurs, global beef spreads could come under pressure due to the reduction in the supply of cattle, especially females, which impacts reproduction. However, as this mismatch is expected to occur later in the short term, Minerva continues to enjoy a favorable operating momentum due to its strong exposure to Brazil and Paraguay.

R$1.5bn of FCF in the last 12M. During 2Q24, the company generated **+R$404mn in cash flow (FCF)**, in line with our expectations, and closed 1H24 with +R$771m. Our analysis suggests that during 2Q24 the company suffered from a **more pressured working capital dynamic** compared to the sequential movement, impacted by the accounts receivable line, which consumed -R$790mn, due to the exchange rate variation in the period and growth in external sales.

The acquisition of Marfrig's assets has prevented the stock from reaching a higher ground. The pending approval of Minerva's acquisition of Marfrig's assets continues to be a critical point. Minerva is still awaiting clearance from the antitrust agency in Brazil (CADE), and Paraguay, where 3 of the 16 assets are located, has already rejected the acquisition. In Brazil, which includes 11 plants, the evaluation process by CADE, which has been underway for almost a year, is causing growing concern among investors.

The speed of the process (or the lack of it) can be interpreted as a reduction in uncertainties related to the **EBITDA that Minerva will be able to generate** when it takes over the plants, since the company claims that its **degree of efficiency as an operator will be greater than what Marfrig was achieving** in the same set of assets, which **raises a degree of skepticism among investors**.

In addition, there is the question of whether Minerva will be able to take advantage of the positive cattle cycle in Brazil before the cycle turns negative and the cost of cattle increases. The acquisition is seen by many as an expensive operation, with an EV/EBITDA multiple of ~9.5x. Even though it is going through a more positive operational period, **the company has not been able to translate this operational improvement into an increase in the value of its shares**, given the uncertainties surrounding the deal with Marfrig.

What is the situation like for the three plants in Uruguay with the CPDC rejecting the acquisition? The situation in Uruguay, where 3 of the 16 plants included in the acquisition package are located, is complex and involves more than just economic considerations. Both Minerva and Marfrig are industry leaders in the region, and the merger would result in significant market concentration. The 2024 election year in Uruguay adds a delicate political layer to the issue. Thus, the transaction is not only seen from an economic perspective, but also as a politically sensitive issue.

Uruguay's intense bureaucratic structure, with several influential associations, such as those of farmers and supermarkets, creates a political scenario that Minerva did not initially foresee. It is therefore expected that the CPDC (Uruguay's antitrust body) will only re-evaluate the decision after CADE's position in Brazil. If CADE approves the agreement with remedies (our base scenario), and Uruguay does not impose conditions, this could be seen as a failure to protect the local market, especially in a context of economic fragility.

A plane without a wing. Following this reasoning, if CADE imposes remedies on the agreement, the CPDC can opt for similar or stricter measures to avoid appearing lenient. Therefore, waiting for the Brazilian antitrust body's decision puts Uruguay in a position of direct comparison, amplifying the political impact of the decision. In short, the situation is especially delicate because Minerva did not anticipate the degree of political sensitivity involved.

We believe that the **uncertainties surrounding the acquisition are already reflected in the share price**. In addition, we consider the **company to be undervalued**, as its well positioned to collect favorable operating performance dua to its high exposure on Brazil positive cattle cycle. Therefore, we reiterate our **BUY rating**, with a **12M Target Price** of **R$9.00**, setting up an **upside** of **+29.68%**.

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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under Review	Under review	**5%**

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