Equity Research

JBS

2Q24 Preview: It's not a short-lived success

LatAm Meatpackers

Main takeaways:

(i) A still challenging scenario for **Beef North America**; **(ii)** We anticipate solid margins in **JBS USA Pork**; **(iii) PPC**, which has already released its results, showed consistent improvement; **(iv) JBS Australia** is benefiting from increased American imports; **(v) JBS Brazil**: Strong USD/BRL with a positive cattle cycle is margin in the vein; **(vi)** Completion of dual listing by the end of the year; **(vii) USDA report from October**: We dissected the content and drew our conclusions. A priori, there is an ongoing increase in beef production in the U.S., suggesting that the domestic market may become even more competitive, putting **pressure on JBS USA Beef margins**. The negative cattle cycle is expected to remain until the end of 2026 and **possibly extend into early 2027**. If this forecast materializes, the chances of a **misalignment in the cycle shift between the U.S. and Brazil** increase; **(viii)** However, as this misalignment is expected to occur later, in the short term, JBS can still enjoy the current scenario, consolidating **good operational results**; **(ix)** In the short term, we see a very favorable scenario for JBS due to **the more diversified case we have under coverage**, whether by **geographic region** or by **different proteins**. Thus, trading at an **EV/EBITDA 25E** of **5.7x** (vs. historical 6.2x), we reiterate our **BUY rating** and **raise** our **12M Target Price** to **R$40.00** (vs. R$35.00 previously), reflecting an **upside** of **+19.44%**.

Analysts

Igor Guedes
+55 (11) 3206-8248
igor.guedes@genial.com.vc

Rafael Chamadoira
+55 (11) 3206-8246
rafael.chamadoira@genial.com.vc

Iago Souza
+55 (11) 3206-8245
iago.souza@genial.com.vc

Company

JBSS3 BZ Equity
Buy

Price: R$ 33.49 (12-Aug-2024)
Target Price 12M: R$ 40.00

JBS will report its **2Q24 results on August 13**, and in this report, we will present our expectations for the company's figures. Once again, we project a **sequentially higher profitability quarter**. We project an **expansion** of the **consolidated EBITDA margin to 8.2% Genial Est.** (+0.96p.p. q/q; +3.17p.p. y/y). On the **positive side**, we expect to see favorable dynamics in most of the company's segments, **mainly PPC, Seara, and USA Pork**. However, on the **negative side**, we still see a very challenging scenario for **JBS Beef North America**, with the unfavorable cattle cycle strongly pressuring margins.

In 2Q24, we estimate total **net revenue** of **R$98.1bn Genial Est.** (+10.1% q/q; +9.8% y/y). We project an **EBITDA** of **R$8.0bn Genial Est.**, with an increase of +24.7% q/q and +79.4% y/y, representing an expansion of +3.17p.p. y/y in the **EBITDA margin**, which should therefore reach **8.2%**. Finally, for **net income**, we estimate in our model a figure of **R$2.2bn Genial Est.**, reflecting an expansion of +0.25p.p q/q in the net margin (2.3% vs. 2.0% in 1Q24).

Valuation and rating. The scenario for the **JBS USA Beef** segment remains under pressure in 2Q24, with JBS facing difficulties due to the **unfavorable cattle cycle and a demand below expectations** during the beginning of the quarter, which should have been boosted by the start of the **barbecue season**. Despite the company's initiatives, such as the White Bone program and efforts in cost reductions, the **EBITDA margin** for this segment is expected to remain low, **close to breakeven**, with a projection of just 0.2% Genial Est., representing a nominal EBITDA of R$45mn Genial Est. (vs. -R$49mn in 1Q24 and +R$433mn in 2Q23). The migration of US consumers to cheaper proteins such as chicken and pork (the so-called **trade down**) in an attempt to escape inflation and the lower economic activity also adds a complexity factor to the Beef segment's performance, keeping the **challenging environment** with figures that should remain sluggish for some time.

In **Brazil**, the scenario is more favorable for JBS, with the **positive cattle cycle** and the **high USD/BRL exchange rate boosting margins**, especially in the Friboi division, which has **50% of its production focused on exports**. The resumption of exports to China and the accreditation of new plants contributed to an expectation of increased EBITDA margins, which should be in the mid to high single digits, with a projection of R$811mn Genial Est. (+261% q/q; +200% y/y). The **(i)** diversification of operations through different proteins **(ii)** especially through Seara with the momentum in chicken, and **(iii)** the appreciating FX rate are factors that should mitigate the challenges faced in other segments (leather and Swift stores), supporting a solid performance in 2Q24.

According to our analysis of the **USDA's August report** released yesterday, we understand that the **negative cattle cycle in the U.S**. could extend until the end of 2026, **potentially prolonging until 2027**, which implies a long-term challenge for JBS USA Beef. On the other hand, the **decline in grain prices** (soybeans and corn) should continue to **benefit the margins of PPC, JBS USA Pork, and Seara exports** (with reduced risk from Newcastle disease), all divisions that have already shown good margins since the last quarter. **JBS Brazil**, on the other hand, continues to take advantage of the **positive cattle cycle**, but the forecast of a **misalignment between the cattle cycles in the U.S. and Brazil in the future** (around 2026) could create a challenging environment for the company in the long term.

However, as this **misalignment is expected to occur later**, in the short term, JBS can still enjoy the current scenario, consolidating **good operational results**. Since we know that the coverage of the meatpacking sector has a commodity nature and that investors linked to essentially cyclical theses usually focus more on the short term, we see a very favorable scenario for **JBS due to the more diversified case we have under coverage**, whether by **geographic region or by different proteins**. Thus, trading at an **EV/EBITDA 25E** of **5.7x** (vs. historical 6.2x), we reiterate our **BUY rating** and raise our **12M Target Price** to **R$40.00** (vs. R$35.00 previously), reflecting an **upside** of **+19.44%**.

2Q24 Preview

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

(R$ Millions)	2Q24E Genial Est.	1Q24 Reported	% q/q	1Q24 Reported	% y/y
Net Revenue	**98.124**	**89.147**	**10,1%**	**89.383**	**9,8%**
COGS	(84.495)	(77.466)	9,1%	(79.495)	6,3%
Adjusted EBITDA	**8.017**	**6.429**	**24,7%**	**4.470**	**79,4%**
EBITDA Margin (%)	8,2%	7,2%	0,96p.p	5,0%	3,17p.p
EBIT	**5.116**	**3.548**	**44,2%**	**1.540**	**232,3%**
EBIT Margin (%)	5,2%	4,0%	1,23p.p	1,7%	3,49p.p
D&A	2.901	2.881	0,7%	2.930	-1,0%
Financial Result	(1.731)	(1.727)	0,2%	(1.668)	3,8%
Net Income	**2.234**	**1.807**	**23,6%**	**(198)**	**-**
Net Margin (%)	2,3%	2,0%	0,25p.p	-0,2%	2,5p.p

Source: JBS, Genial Investimentos

Still a challenging scenario for Beef in North America. The scenario for JBS USA Beef remains tough for meatpackers. Although the 2Q normally benefits from the positive seasonality of the barbecue season, demand at the beginning of 2Q24 (April and May) fell short of expectations, with some recovery only in June. The prospect of an improvement in the EBITDA margin is limited due to the continued unfavorable cattle cycle, which has not shown significant relief from one quarter to the next. Therefore, we expect the EBITDA margin to remain in the low single digits or even close to breakeven, with no significant advances compared to 1Q24. We estimate a margin of 0.2% and a nominal EBITDA of R$45mn Genial Est. (vs. -R$49mn in 1Q24 and +R$433mn in 2Q23).

What is being done to mitigate? It is important to highlight the initiatives that JBS has undertaken, such as the White Bone program and cost reductions, which may offer some support to profitability. Still, the combination of a not-so-robust seasonal demand as expected and the tight cycle suggests that 2Q24 results should remain flat, with a balance between positive and negative factors. Moreover, we are witnessing the trade down of proteins, that is, a migration of demand in the U.S. to cheaper proteins like chicken and pork, which could further affect the Beef segment's performance in the short term. In summary, the scenario continues to reflect unimpressive numbers, with an expectation of stable performance and no major surprises in 2Q24. On the other hand, we understand that the great competitive advantage of the investment thesis in JBS is the diversification of both proteins and geographies. Therefore, the trade down is beneficial for the consolidated result since other business divisions, such as PPC and USA Pork.

We expect solid margins in JBS USA Pork with EBITDA expansion. We expect JBS USA Pork to maintain solid figures in 2Q24, with EBITDA margin reaching 10%. The demand for pork should continue to be favored by the trade down, with consumers opting for more affordable proteins, which should sustain margins in the quarter at satisfactory levels. Additionally, the barbecue season brings a positive seasonal boost to demand, and the decline in grain prices continues to benefit the segment. Thus, JBS USA Pork should present robust performance, driving EBITDA to R$1.0bn Genial Est. (+66.9% q/q; +165.3% y/y).

PPC, which has already released its results, showed consistent improvement. Pilgrim's Pride Corporation (PPC), JBS's subsidiary for chicken meat sales focused on North America, reported solid results in 2Q24, with net sales of US$4.6bn, representing an increase of +5.8% y/y. The company recorded an operating profit of US$440.8mn and net income of US$326.5mn, driven by improved operating margins and production efficiencies. The U.S. division stood out with improvements in operational efficiency and lower input costs, while Europe showed significant growth in adjusted EBITDA, reflecting optimization in the relationship with key customers. We project going forward a sequential expansion of margins for the segment enabled by **(i)** a more balanced global supply in chicken; **(ii)** strong demand, and **(iii)** low grain prices (soybeans and corn) benefiting PPC on the cost side. Thus, we should see the operation delivering an EBITDA margin in the high single digits and potentially low double digits.

JBS Australia riding on increased US imports. For 2Q24, we expect JBS Australia to continue performing well, with EBITDA margin remaining at high levels, driven by a favorable cattle cycle and strong international demand. We note that U.S. beef imports from Australia increased significantly, strengthening the operation. Furthermore, the company is investing in an initiative to transfer skilled labor from Brazil to Australia, which could enhance efficiency and add value to cuts, although this process is gradual due to language barriers. For 2Q24, we calculate EBITDA at R$842mn Genial Est. (+37.1% q/q; +18.5% y/y).

JBS Brazil: Strong USD/BRL with a positive cycle is margin in the vein. We expect JBS Brazil to continue benefiting from the positive cattle cycle, which will bolster the foundations of the Friboi division's EBITDA margin. Furthermore, the business unit is composed 80% of Friboi, which is exposed 50% to exports. With the strong appreciation of the USD/BRL exchange rate during 2Q24 and the resumption of exports to China after the accreditation of 10 new plants, the segment should see an increase in margins that historically grow between +200-300bps from 1Q to 2Q. Additionally, we are witnessing a slight recovery in the automotive sector, which favors higher demand for leather, one of the side businesses of the Brazil division that was previously reducing Friboi's good performance margin.

Therefore, we expect JBS Brazil's EBITDA margin to remain in the mid-single digits, with potential to reach high single digits if Chinese demand for beef exceeds expectations. For now, we are working with the premise of a reduction in y/y shipments to China in 2H24.

The diversification of operations and the favorable environment in the USD/BRL exchange rate composition should help mitigate the challenges in less profitable segments (leather and Swift stores), supporting solid performance in 2Q24. We project EBITDA of R$811mn Genial Est. (+261% q/q; +200% y/y).

Seara: it's not a short-lived success. For 2Q24, Seara should continue to perform solidly, benefiting from a very positive scenario for the chicken segment, both for domestic consumption and for the export market. With lower grain costs and strong demand, as well as the global normalization of poultry supply, the spread is quite robust and continues to gain traction sequentially. The EBITDA margin should remain strong, reflecting the good momentum. Our model points to EBITDA of R$1.4bn Genial Est. (+19.1% q/q; +238.2% y/y).

Our Take on JBS

Completion of dual listing by the end of the year. We foresee that the process of dual listing JBS shares will only be completed by the end of 2H24. Although the company is facing lawsuits in the U.S. related to greenwashing allegations, which we see more as noise than a substantial problem, these cases may generate additional questions from the Securities Exchange Commission (SEC), possibly delaying the listing of the shares in the U.S. Conversely, in conversations we had with the company, their version of the facts is that the process is quite bureaucratic and is a replica/rebuttal process in sending documents to the SEC until there are no further comments. Recently, the company issued the 20-F report as well as F-4, which can be seen as progress towards the SEC's authorization for the primary listing of shares on the NYSE.

August USDA: Protein trade down intensifies. The USDA report released yesterday, August 12, points to trends that may impact JBS's operations in a mixed way in the coming quarters. The continued decline in grain costs should **benefit the margins** of **PPC, JBS USA Pork, and Seara exports** (with reduced risk of Newcastle disease), maintaining the competitiveness of these segments throughout the year. However, the forecast of an increase in beef production in the U.S. suggests that the domestic market may become even more competitive, putting **pressure on JBS USA Beef margins**, which will have to face this challenge with operational efficiency to preserve profitability.

On the other hand, the strong projected demand for the chicken market, both domestically and in exports, indicates that **Seara will continue to be in an advantageous position**, taking lead position in the poultry market momentum. These factors should be reflected in continued solid results for Seara and JBS USA Pork, while JBS USA Beef may face a more challenging environment, requiring strategic adjustments to mitigate the impacts of increased supply in the American market.

Risk of cycle mismatch at 26/27. The market outlook is for a possible extension of the negative cycle in the US until 2026, which could last until the beginning of 2027. If this does happen, the chances are increasing that there will be a cycle mismatch between the US and Brazil, which could harm the theses of JBS (to a greater extent) and Minerva (to a lesser extent). Now, we're looking at a stronger possibility of a **mismatch** of time windows in the **cycle reversal**, and both regions being faced with negative cattle cycles at the same time. If this really happens, we could see global beef spreads under more pressure, due to the reduction in the supply of cattle, especially females, impacting reproduction and the future supply of calves.

It's not a short-lived success. However, as this misalignment is expected to occur later, in the short term, JBS can still enjoy the current scenario, consolidating good operational results. Since we know that the coverage of the meatpacking sector has a commodity nature and that investors linked to essentially cyclical theses usually focus more on the short term, we see a v**ery favorable scenario for JBS** due to the **more diversified case we have under coverage**, whether by **geographic region** or by **different proteins**. Thus, trading at an **EV/EBITDA 25E** of **5.7x** (vs. historical 6.2x), we reiterate our **BUY rating** and **raise** our **12M Target Price** to **R$40.00** (vs. R$35.00 previously), reflecting an **upside** of **+19.44%**.

Appendix: JBS

Figure 1. JBS – Income Statement in R$ Millions (Genial Est. 2024-2028)

Income Statement	2024E	2025E	2026E	2027E	2028E
Net Revenue	**364.480**	**384.310**	**443.792**	**451.498**	**468.352**
(-) COGS	(316.631)	(331.783)	(381.843)	(381.399)	(385.844)
Gross Profit	**47.849**	**52.527**	**61.949**	**70.100**	**82.508**
(-) Expenses	(28.158)	(32.328)	(39.534)	(43.696)	(44.230)
Adjusted EBITDA	**19.691**	**20.199**	**22.415**	**26.404**	**38.278**
(-) D&A	(10.007)	(8.005)	(6.754)	(2.502)	(2.502)
EBIT	**9.685**	**12.194**	**15.660**	**23.902**	**35.776**
(+/-) Financial Result	(4.917)	(4.858)	(2.864)	(2.916)	(2.893)
(-) Taxes	(1.621)	(2.494)	(4.351)	(7.135)	(11.180)
Net income	**3.147**	**4.842**	**8.445**	**13.851**	**21.703**
Profitability					
Net margin (%)	0,86%	1,26%	1,90%	3,07%	4,63%

Figure 2. JBS – Cash Flow in R$ Millions (Genial Est. 2024-2028)

Cash Flow (FCFF)	2024E	2025E	2026E	2027E	2028E
Net Revenue	**364.480**	**384.310**	**443.792**	**451.498**	**468.352**
(-) COGS	(316.631)	(331.783)	(381.843)	(381.399)	(385.844)
Adjusted EBITDA	**19.691**	**20.199**	**22.415**	**26.404**	**38.278**
EBIT	**9.685**	**12.194**	**15.660**	**23.902**	**35.776**
(-) Taxes	(1.621)	(2.494)	(4.351)	(7.135)	(11.180)
(+) D&A	10.007	8.005	6.754	2.502	2.502
(+/-) Δ WK	(1)	(4.655)	(2.757)	(385)	(829)
(-) Capex	(10.007)	(8.005)	(6.754)	(2.502)	(2.502)
FCFF	**8.062**	**5.045**	**8.553**	**16.382**	**23.767**

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