MINERVA

3Q24 Review: Slaughtering margins

LatAm Meatpackers

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Company

BEEF3 BZ Equity
Neutral

Price: R$ 5.90 (06-Nov-2024)
Target Price 12M: R$ 6.80

Main takeaways:

(i) Net revenue of **R$8.5bn**, highlighted this quarter, driven by stronger volumes and **BRL/USD depreciation**. **(ii) Brazil** and **Paraguay** remain the main export countries. **(iii) COGS** reflects the impact of rising cattle prices, resulting in a flat q/q **EBITDA margin** of **9.6%**. **(iv)** The company reported a **FCFE** of **R$667mn** (+65% q/q), supported by **R$625mn** in **working capital release**, lower **CAPEX**, and **EBITDA** above expectations (+5,6% vs. Genial Est.); **(v)** The acquisition deal was barred again in Uruguay, so we exclude it from our estimates. **(vi)** We are projecting an **incremental EBITDA** of **+R$819mn** (vs. R$1.5bn Minerva target) from the consolidation of the Marfrig's 13 assets (ex. 3 plants in Uruguay); **(vii)** The cycle reversal in Brazil creates a more challenging scenario from now on, compressing margins with a deleveraging process taking long to occur than anticipated by the management (12-18 months). We estimated **3.5x Net Debt/EBITDA 25E** and the company fully returning to pre-deal leverage only by 2H26; **(viii)** With an eye on **more compressed margins** of **-0.5p.p 25E**, with the reversal of the cattle cycle in Brazil, **we don't see enough catalysts** in the short term for a recovery in share prices, after a long period of decline since the deal announcement with Marfrig in 2023. We are therefore **downgrading** the company's rating to **NEUTRAL**, with a **Target Price 12M** of **R$6.80**, indicating an **upside** of **15.25% upside**.

Minerva reported its **3Q24 results yesterday**, November 6, after the market closed. We believe that the figures released for the quarter were **mainly positive**, slightly beating our estimates and the consensus. Even so, as the **purchasing cost for cattle is rising very quickly**, we are concerned about the company's ability to maintain margins at these levels in 2025. We have therefore decided to **downgrade** our **rating to NEUTRAL** (vs. Buy previously), with a **12M Target Price** of **R$6.80** (vs. R$9.00 previously), indicating an **upside** of **+15.25%**.

Table 1. Income Statement Minerva (3Q24 vs. Genial Est.)

(R$ million)	3Q24 Reported	3Q24E Genial Est.	% R/E	2Q24 Reported	% q/q	3Q23 Reported	% y/y
Net Revenue	**8.501**	**7.845**	**8,4%**	**7.666**	**10,9%**	**7.068**	**20,3%**
COGS	(6.727)	(6.110)	10,1%	(6.001)	12,1%	(5.590)	-20,3%
Adjusted EBITDA	**813**	**770**	**5,6%**	**745**	**9,1%**	**714**	**13,9%**
EBITDA Margin (%)	9,6%	9,8%	-	9,7%	-0,1p.p	10,1%	-0,5p.p
EBIT	**648**	**620**	**4,5%**	**595**	**8,9%**	**575**	**12,8%**
EBIT Margin (%)	7,6%	7,9%	-	7,8%	-	8,1%	-
Dep. & Amort.	165	150	10,0%	149	10,4%	139	18,7%
Financial Result	(565)	(470)	20,2%	(493)	14,7%	(536)	5,4%
Net Income	**94**	**90**	**4,4%**	**96**	**-1,6%**	**141**	**-33,3%**
Net Margin (%)	1,1%	1,1%	-	1,2%	-0,1p.p	2,0%	-0,9p.p

Source: Minerva, Genial Investimentos

Turning to the dynamics of 3Q24, performance was driven by **(i)** an increase of +6.0% q/q and +15.2% y/y in **shipments**, which reached **384.4Kt** (+3.8% vs. Genial Est.), with **exports standing out**, mainly to the US and China, offsetting the more depreciated prices. The conversion factor in the high USD/BRL exchange rate in the period helped to mitigate the contraction in sales prices. In addition, **(ii)** the domestic market strengthened, with slightly higher realized prices.

The company achieved **Net revenue** of **R$8.5bn** (+8.4% vs. Genial Est.), up +10.9% q/q and +20.3% y/y. Adjusted **EBITDA** clocked in at **R$813mn** (+5.6% vs. Genial Est.), and although it grew by +9.2% q/q and +13.9% y/y, the **margin fell slightly to 9.6%** (-0.1p.p q/q; -0.5p.p y/y). The factors that worry us the most are the signs, already partially apparent in this quarter, that the **price increase of the arroba of cattle puts pressure on costs**. Our understanding is that subsequent results will show a potentially stronger pace of margin contraction. **Net income** reached **R$94mn** (-1.6% q/q; -33.3% y/y), showing a slowdown due to a slightly more pressured financial result.

Valuation and rating. Precisely due to concerns about a larger-scale contraction in margins in the coming quarters, we are **downgrading** our **rating** to **NEUTRAL** (vs. Buy previously), with a **12M Target Price** of **R$6.80** (vs. R$9.00 previously), indicating an **upside** of **+15.25%**. We believe that, even though the company has finally announced the closing of the transaction for the purchase of 11 Marfrig slaughter plants in Brazil (of the set of 16 assets announced in 2023), the **(i)** delay for CADE's approval and **(ii)** macro situations putting **USD/BRL exchange rate at high levels**, which encouraged a basically record increase in exports, led to a delay in taking advantage of the positive cattle cycle we were witnessing until June. Afterwards, we observe a **rapid reduction in the cattle supply being slaughtered**, starting now the cycle reversal path.

This situation, in turn, has put intense pressure on beef arroba prices over the last 2M. Soon, **costs will inevitably be higher**, and even with the substantial increase in slaughter capacity when consolidating assets, the **EBITDA margin should contract**, according to our current projections, by **-0.5p.p. y/y** in **25E** and the pace of deleveraging after capturing synergies will be pushed forward. For more details on our downgrade, **we recommend reading the "Our Take" section** at the end of the report.

3Q24 Review

Revenue triggers. Net revenue was reported at R$8.5bn (+10.9% q/q; +20.3% y/y), exceeding expectations (+8.4% vs. Genial Est.), even with a drop in realized prices in the foreign market of -7.2% y/y, partially offset by an increase of +2.5% y/y in the domestic market. We also saw exceptional growth in sales volume (+6.0% q/q; +15.2% y/y). Among the main points, we would highlight **(i)** an increase in the share of exports to the NAFTA region, especially the US, due to the continued negative cattle cycle in the region, making importers more eager to look in regions where the cattle cost is negotiated at lower prices, as was the case in Brazil. In addition, we believe that the **(ii)** anticipation of the Chinese New Year to January/25, ended up heating up sales to China at the end of 3Q24; as well as the **(iii)** favorable seasonality typical of the period for the domestic market; and **(iv)** the advantageous USD/BRL exchange rate, with an increase of +6.33% q/q, were factors that guided the robust shipments figures.

Main countries dynamics. The increase in sales was driven by improved performance in Brazil and Paraguay, the main origination countries, favored by a positive cycle. Australia also improved, reflecting a favorable cycle, while in Colombia we saw an increase in shipments, but continues to show low results due to political instability. Argentina remained with no signs of profitability, and Uruguay recorded worsening margins due to the negative cycle in the region.

COGS are already pointing to further margin contraction. Despite the increase in net revenue, we saw the EBITDA margin stay flat in the quarterly comparison (-0.1p.p q/q) and contract by -0.5p.p y/y, reflecting the higher level of costs due to the rise in cattle prices. This already reflects the problems that Minerva will face with the process of cattle cycle reversing that is taking place between the end of this year and 2025.

Our Take on Minerva

Robust FCFE generation. The company reported a **FCFE** of **R$667mn** (+18% vs. Genial est.), growing **+65% q/q**, driven by a working capital release of R$625mn (+7.6% q/q), above expectations, alongside a **CAPEX** slowdown to **R$147mn** (-28% q/q). The **EBITDA**, slightly above our projections, also contributed to this robust FCF generation.

Deal with Marfrig is blocked in Uruguay. On October 30, the company announced that the acquisition process for the **3 slaughter plants** in **Uruguay** from the **16-asset** package purchase from Marfrig was denied by the **CPDC** (antitrust body), reflecting concerns over significant market concentration that this deal would create, given that Minerva is already a sector leader in the region. The company has shown an intention to appeal again, as the decision remains subject to further appeals. However, after two negative opinions from the CPDC, we believe the deal is unlikely to materialize and have not factored it into our incremental **EBITDA** estimates.

Where there's a will, there's no way. In our projections, we estimate an **incremental annualized EBITDA** of **+R$819mn Genial est.** for the **13 plants** (11 in Brazil, 1 in Argentina, and 1 in Chile). According to our estimates, this represents **~60%** of Minerva's target **EBITDA** of **R$1.5bn ex. Uruguay** and is **+9.2%** above Marfrig's indication (**R$750mn**). We believe market consensus is **underestimating** the company's operational capacity by not including any potential upside from Marfrig's disclosed figure in projections.

We view it as more realistic to aim for a middle-ground scenario between Marfrig's market communication and what Minerva claims it could achieve by operating the plants. Among the assumptions we used, we have particular concern about the current cycle moment, which shows clearer signs of reversal, with cattle **arroba prices** reaching **R$325** last week (vs. ~R$215 at the low of this cycle in June). Thus, we believe Minerva will likely not reach the incremental EBITDA indicated by management.

The company may revise plant's EBITDA downward. We perceive that investor fears have materialized, specifically that the company acquired a set of assets by paying a price at the top of a positive cattle cycle. This cycle is already reversing, with the cattle arroba price rising **+50% in ~5M**, significantly increasing cattle acquisition costs and reducing plant profitability in the new cycle phase. In recent conversations, we got the impression that Minerva might be planning to revise its **incremental EBITDA** target downward, given the cattle price setback and macro conditions differing from initial assumptions.

It's also worth noting that even if the company decides to make this adjustment, we assess that consensus is already not pricing in the ability of the company to capture **synergies** and increase asset efficiency to the point of reaching the initially disclosed **R$1.5bn**. Therefore, any downward revision to this guidance is already somewhat priced in by the market.

Cycle reversal in Brazil is already underway. Three factors are pressuring cattle prices: **(i)** the increase in **calf prices** and **(ii)** a reduced female slaughter rate, which signals a **high female retention** level in 2025. Additionally, we see the **(iii) USD/BRL exchange rate** at significant levels as an incentive to direct more volume to exports, which, combined with a resilient domestic market, has prominently increased the number of slaughters. In **3Q24**, around **7.5mn cattle** were slaughtered in **Brazil** (**+3% q/q; +12% y/y**). The increased slaughter pace is reducing cattle availability, and with a lower supply of mature animals, cattle **arroba prices** are starting to rise. Although the company argues that high availability still exists, we believe the data signals otherwise.

Beef exports are likely to hit a record. We expect **beef exports** in **2024** to exceed **3Mt carcass equivalent (TEC)**. By the end of September, shipments had already reached **2.7Mt**, marking the highest volume recorded for this period. We see slaughter schedules shortening as exporters increase cattle purchases. As a result, **Brazil** is on track to set a new record for **beef shipments**, which is certainly reducing cattle availability, accelerating the cycle reversal.

Where is the cattle arroba price headed? As we noted, while cattle availability was indeed high until mid-year, the current macro scenario—driven by the **USD/BRL exchange rate** and producers facing tight margins in sales to **slaughterhouses**—is reducing cattle supply and increasing arroba prices, which we estimate will average around **R$330 25E** (vs. **R$239** in **3Q24**). Besides the factors mentioned, we believe this cycle reversal has been exceptionally accelerated by the El Niño, which brought an atypically dry winter. This likely led ranchers to keep cattle on pasture in the 2H24, removing them from the slaughter pipeline and further constraining supply.

One overhang has been overcome, but the context is still challenging. Initially, we identified two overhangs keeping investors away from Minerva shares. The first was regarding **(i)** the delay and risk of stringent remedies imposed by CADE for the acquisition approval. This issue was overcome on September 25 with a favorable opinion from CADE for the purchase of **11 plants** in **Brazil**, with Chile and Argentina plants also expected to be approved by local authorities. In Brazil, we consider CADE's imposed remedy mild, requiring only the disposal of an inactive plant, which represents ~**6%** of the local asset group's total slaughter capacity.

Notably, this acquisition makes Minerva the second-largest cattle slaughterer in Brazil, with **22,3K heads of cattle per day**, behind JBS. The deal's closing in Brazil also consolidates the company as the primary exporter in South America. However, according to the company, slaughters at these plants began at the end of October, with a ramp-up period expected to last **30-35 days** due to the sensitive command transition. Thus, **(ii)** we expect **4Q24** to show **still weak shipments**, with the company reaching **full capacity** in **1Q25**, in a scenario of rising cattle prices, which may eventually reduce margins. The cycle reversal was the second overhang, which is difficult to resolve at this stage.

Leverage has dropped for now but will rise sharply in 4Q24. Leverage ended 3Q24 at **2.6x Net Debt/EBITDA**, already including the **-R$1.5bn** disbursement for the acquisition (21% of the total excluding Uruguayan plants). However, we project leverage to increase to **4.5x 24E**, with the expected **-R$5.6bn** complementary payment in **4Q24** (including CDI interest correction). Given our assumptions for incremental EBITDA, FCF generation will be constrained by the cattle cycle reversal, likely making the deleveraging process slower than the 12-18 months indicated by the company. We project leverage to decrease to **3.5x 25E**, still well above the **2.7x** level before the company took on debt for the acquisition. We see this level being reached only in **2H26**, taking nearly twice as long as Minerva anticipated, considering the assets enter operation in 4Q24**.**

Slaughtering margins. While we see the substantial slaughter capacity increase from the 13 plants reaching full capacity accelerating **Net Revenue 25E** by **+29% y/y vs. 24E**, we still believe that **cattle acquisition costs** will inevitably rise next year. The cost increase is tied to the steep rise in arroba prices we are witnessing, so the impact should already compress **margins y/y in 1Q25**. We expect the **EBITDA margin** to decelerate by **-0.5 p.p. 25E**. Until CADE's review was complete, we gave the company the benefit of the doubt regarding the deal's viability despite the overhangs mentioned. The **high USD/BRL exchange rate** conditions that are imperative today, encouraging prominent slaughter volumes driven by strong export demand, could not have been anticipated when the deal was announced in 2023. Therefore, the company likely foresaw a scenario that did not materialize in the short term.

While we haven't changed our view on Minerva's ability to arbitrage prices as a core element of the investment thesis, and the capacity increase capacity will bring scale gains and greater flexibility in future cycles, we acknowledge that **commodity investors often focus on the short term**. And the short-term outlook emerging now isn't promising. As a result, we see **almost no catalysts for stock** in the coming months. This motivates our **rating downgrade to NEUTRAL** (vs. Buy previously), with a **12M target price** of **R$6.80** (vs. R$9.00 previously), indicating an **upside** of **+15.25%**.

Appendix: Minerva

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

Income Statement	2024E	2025E	2026E	2027E	2028E
Net Revenue	**31.698**	**40.922**	**43.850**	**44.125**	**45.084**
(-) COGS	(24.953)	(32.651)	(35.634)	(36.553)	(37.782)
Gross Profit	**6.745**	**8.271**	**8.215**	**7.571**	**7.302**
(-) Expenses	(3.686)	(4.393)	(4.032)	(3.901)	(3.566)
Adjusted EBITDA	**3.059**	**3.878**	**4.184**	**3.670**	**3.735**
(-) D&A	(454)	(497)	(512)	(523)	(532)
EBIT	**2.604**	**3.381**	**3.671**	**3.147**	**3.203**
(+/-) Financial Result	(2.080)	(2.844)	(2.930)	(2.466)	(2.308)
(-) Taxes	(196)	(143)	(227)	(205)	(263)
Net income	**328**	**394**	**514**	**476**	**632**
Profitability					
Net margin (%)	1,04%	0,96%	1,17%	1,08%	1,40%

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

Cash Flow (FCFF)	2024E	2025E	2026E	2027E	2028E
Net Revenue	**31.698**	**40.922**	**43.850**	**44.125**	**45.084**
(-) COGS	(24.953)	(32.651)	(35.634)	(36.553)	(37.782)
Adjusted EBITDA	**3.059**	**3.878**	**4.184**	**3.670**	**3.735**
EBIT	**2.604**	**3.381**	**3.671**	**3.147**	**3.203**
(-) Taxes	(196)	(143)	(227)	(205)	(263)
(+) D&A	454	497	512	523	532
(+/-) Δ WK	(230)	(122)	32	(20)	(103)
(-) Capex	(912)	(970)	(922)	(885)	(903)
FCFF	**1.721**	**2.643**	**3.067**	**2.560**	**2.467**

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