

28 Aug 2020 | Affirmation

Fitch Affirms Suzano's IDR at 'BBB-'; Outlook Negative on IDRs

Fitch Ratings-Rio de Janeiro-28 August 2020:

Fitch Ratings has affirmed Suzano S.A.'s (Suzano) Foreign and Local Currency Long-Term Issuer Default Ratings (IDRs) at 'BBB-' and the national scale long-term rating at 'AAA(bra)'. The Rating Outlook for the Foreign and Local Currency IDRs is Negative. The Outlook for the National Scale Long-Term Rating is Stable.

Suzano's investment-grade ratings reflect the company's position as the world's leading producer of market pulp, with 11 million tons of bleached eucalyptus kraft (BEKP) market pulp capacity. The ratings also incorporate the company's strong business position as a low-cost producer of market pulp and its position as the leading producer of printing and writing paper and paperboard in Brazil. The company's strong liquidity position and comfortable debt amortization schedule are also factored into the ratings.

The Negative Outlook reflects the continued difficulty Suzano will face reducing its net debt. Fitch projects Suzano's net debt/EBITDA ratio will be approximately 5.0x by YE 2020 due to a prolonged period of weak pulp prices, before falling to around 3.2x by YE 2021. Fitch expects FCF of about USD1.6 billion during 2020 and 2021, contributing to a net debt reduction to about USD11 billion by YE 2021 and to below USD10 billion during 2022.

Pulp prices have remained below USD500/ton in 2020 after plummeting to USD480/ton during December 2019 from USD715/ton during January 2019. Fitch expects a slight recovery during 2021, as at current pulp price levels, high-cost producers are operating at very low profit margins and need to close plants or extend their maintenance shutdowns.

Key Rating Drivers

Solid Business Position: Suzano's investment-grade ratings reflect the company's position as the world's leading producer of market pulp, with 11 million tons of BEKP market pulp capacity. The company has an estimated market share of about 18% in market pulp and 32% in hardwood pulp as calculated by Fitch. Fitch views Suzano's competitive advantage as sustainable due to its modern pulp mills, high-yielding forestry plantations, low average distance from the forests to the

mill and efficient logistics. Due to its strong market business position in pulp and very competitive production cost structure in the lowest quartile, Suzano is able to generate positive operating cash flow during cyclical pricing downswings.

Strong Paper Business: Suzano is the leading producer of printing and writing paper and the second largest paperboard producer in Brazil with 1.4 million tons of annual production capacity. Suzano supplies about 40% of printing and writing paper demand and about 25% of paperboard in Brazil according to the Brazilian Tree Industry Association (Ibá). The company's strong market shares in uncoated printing and writing paper and its exclusive distribution system of paperboard allow it to be a price leader in Brazil. During 2019, the company's paper operations accounted for slightly more than 10% of its EBITDA.

FCF to Improve in 2021: Fitch projects Suzano to generate about USD2.6 billion of EBITDA in 2020 and USD3.4 billion in 2021. Cash flow from operations (CFFO) is projected to be USD1.9 billion and USD2.4 billion, respectively, during 2020 and 2021. This compares with USD2.6 billion of EBITDA and USD2.0 billion of CFFO in 2019. The company's EBITDA generation during 2020 reflects higher pulp sales volume and local currency depreciation, offset by weaker pulp prices. Suzano's FCF generation capacity will be negatively impacted by derivatives loss estimated at about USD800 million in 2020 and USD230 million in 2021, resulting in FCF of about USD1.6 billion in the period. Fitch's base case projections considered no dividends in 2020 and 2021, and annual investments around USD800 million.

Gradual Leverage Reduction: Leverage reduction has been slower than previously projected due to a prolonged period of weak pulp prices. Fitch expects Suzano's net leverage ratio to be about 5.0x in 2020 with average prices of USD450/ton and to fall to around 3.2x in 2021 with projected prices of USD525/ton. Suzano's net debt reduced to USD12.6 billion as of June 30, 2020, from USD13.6 billion at YE 2019. Fitch projects net debt to continue to gradually reduce during 2021 and 2022; the pace of reduction is highly dependent on pulp price recovery. Initiatives by the company, like the sale of non-core assets, could also help deleveraging process.

Forestry Assets Key to Credit Profile: A key credit consideration that supports the investment-grade credit profile is the significant forestry holdings of Suzano, which assure a competitive production cost structure. As of June 30, 2020, the accounting value of the biological assets on the forest plantations owned by Suzano was about USD1.9 billion. The nearly ideal conditions for growing trees in Brazil make these plantations extremely efficient by global standards and give the company a sustainable advantage in costs of fiber and transportation between forest and mill.

Downturn in Pulp Cycle: The market pulp industry is very cyclical; prices move sharply in response to changes in demand or supply. Weaker demand for paper and packaging in Europe and the U.S.

has stifled a recovery in the sector following the pulp price collapse in 2019; demand recovery will depend on world economic growth during 2021. Tissue demand increased during 1H20; however, it was not sufficient to offset lower printing and writing demand, and this growth is not expected to be sustainable in the medium term. At current pulp price levels, high-cost producers are already operating at very low profit margins and may extend their maintenance or shut down mills, which will be critical to reduce supply and support price recovery. Higher maintenance downtime are expected during 2H20, as some producers postponed scheduled maintenance due to the coronavirus pandemic.

Rating Pierces Country Ceiling: Suzano's 'BBB-' Foreign Currency IDR is two notches higher than Brazil's 'BB' Country Ceiling due to a combination of estimated EBITDA in hard currency of about USD2.3 billion, about USD1.8 billion of cash held outside of Brazil. Fitch projects the ratio of exports, plus cash held abroad to cover hard currency debt service over the next 24 months above 1.5x. In line with Fitch's "Non-Financial Corporates Exceeding the Country Ceiling Rating Criteria." This could lead to a three-notch upgrade above the Brazilian Country Ceiling.

Derivation Summary

Suzano is the world's leading producer of market pulp, with an annual pulp production capacity of 11 million tons in an industry of 62 million tons of market pulp. Suzano has an estimated market share of about 18% in market pulp and 32% in hardwood pulp, as per Fitch's calculations. The second largest producer of market pulp is Celulosa Arauco y Constitucion S.A. (Arauco; BBB/ Negative), followed by International Paper (not rated) and Empresas CMPC S.A. (CMPC; BBB/ Stable). Suzano is also the leading producer of printing and writing paper and the second largest paperboard producer in Brazil. Suzano's business profile is consistent with a rating in the 'BBB' category.

Similar to Latin American pulp producers, Arauco and CMPC, Suzano's pulp production cash costs are among the lowest in the world, ensuring its long-term competitiveness. The company has a significant size advantage in the fragmented pulp market but with lower geographic and product diversification than its Chilean peers Arauco and CMPC, which are leaders in the wood products segment and tissue markets, respectively.

Suzano's Negative Outlook incorporates Fitch's expectation that deleveraging will be slower than initially projected following two years from the acquisition of Fibria. Suzano's leverage is higher than CMPC, while Arauco's leverage will increase during the period of high investments in MAPA project. Klabin's net leverage around 4.5x reflects the investments in the Puma II project and is not expected to decline to lower levels until 2023. Liquidity is historically strong for pulp producers,

and Suzano has strong access to debt and capital markets. Suzano's operating margins are higher than the Chilean companies that operate in lower-margin business segments such as tissue, packaging and boards.

Key Assumptions

Fitch's Key Assumptions Within the Agency's Rating Case for the Issuer

- Pulp sales volume of 10.4 million tons in 2020 and 10.5 million tons in 2021;
- Paper sales volume of 1.0 million tons in 2020 and 1.2 million tons in 2021;
- Average net hardwood pulp prices of USD450 per ton in 2020 and USD525 per ton in 2021;
- No dividends in 2020 and 2021;
- Average FX rate of 5.2 BRL/USD in 2020 and 5.1 BRL/USD in 2021;
- Derivatives loss of BRL4.1 billion in 2020 and BRL1.2 billion in 2021.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to a positive rating action/upgrade:

- A positive rating action is not expected in the medium term. The Outlook Negative could be revised to Stable if Suzano's FCF generation is stronger, allowing a quicker net debt reduction.

Factors that could, individually or collectively, lead to a negative rating action/downgrade:

- An expectation that net debt/EBITDA will remain above 3.5x in 2021, considering no significant improvement in current weak pulp prices;
- An expectation that the company's net debt position will remain well above USD10 billion by YE 2021, with no clear expectation of reduction during 2022.

Best/Worst Case Rating Scenario

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade

scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

Liquidity and Debt Structure

Strong Liquidity: Suzano has historically maintained a strong cash position. In June 30, 2020, Suzano had USD2.3 billion of cash and marketable securities and USD15.8 billion of total debt, including about USD900 million of debt factoring as per Fitch's calculation. About 80% of the company's cash position as of June 2020 was denominated in U.S. dollar. The company's short-term debt maturities total about USD1.0 billion, excluding debt factoring. The company has a manageable debt maturity profile with about USD900 million debt falling due during the 2H2021 and in 2022.

In April 2020, Suzano withdrew its USD500 million revolving committed credit facility (RCF) to strength liquidity due to high uncertainties from the coronavirus pandemic. The company amortized the RCF in August 2020 and the USD500 million RCF is fully available as an additional source of liquidity, along with the BRL1 billion unused RCF.

Suzano enjoys strong access to both the debt and equity markets. Fitch expects the company to preserve an extended debt amortization profile and conservative liquidity. Financial flexibility is enhanced by the potential sale of forestry assets and/or less strategic assets, if necessary.

As of June 30, 2020, total debt comprised of senior notes (43% of total debt), Exports Financing (31%), Debentures (6%), Factoring (6%), BNDES (4%) and others (10%). The majority of the company's debt is denominated in U.S. dollar.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Suzano S.A.: Energy Management: 4

Suzano has an ESG Relevance Score of 4 for EFM Environment - Energy Management as the

company sells excess energy to the grid from cogeneration based upon a renewable resource, which has a positive impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Except for the matters discussed above, the highest level of ESG credit relevance, if present, is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Suzano Austria GmbH

---senior unsecured; Long Term Rating; Affirmed; BBB-

Fibria Overseas Finance Ltd.

---senior unsecured; Long Term Rating; Affirmed; BBB-

Suzano S.A.; Long Term Issuer Default Rating; Affirmed; BBB-; RO:Neg

; Local Currency Long Term Issuer Default Rating; Affirmed; BBB-; RO:Neg

; National Long Term Rating; Affirmed; AAA(bra); RO:Sta

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Additional information is available on www.fitchratings.com

Applicable Criteria

[Corporate Rating Criteria \(pub. 01 May 2020\) \(including rating assumption sensitivity\)](#)

[National Scale Rating Criteria \(pub. 08 Jun 2020\)](#)

[Non-Financial Corporates Exceeding the Country Ceiling Rating Criteria \(pub. 25 Feb 2020\)](#)

Applicable Model

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 ([1](#))

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