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Research Update:

Suzano Papel e Celulose S.A. Outlook Revised To Negative And 'BB' Credit Rating Affirmed On Slower Debt Reduction

Primary Credit Analyst:

Diego H Ocampo, Buenos Aires (54) 114-891-2124; diego_ocampo@standardandpoors.com

Secondary Contact:

Rafaela Vitoria, CFA, Sao Paulo (55) 11-3039-9761; rafaela_vitoria@standardandpoors.com

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Overview

- Brazilian pulp and paper producer Suzano has reduced refinancing risks and issued equity to improve its capital structure, but we believe its debt reduction will be slower than we originally projected.
- We are revising the outlook to negative from stable and affirming the 'BB' ratings on the company.
- We may downgrade Suzano if its leverage metric remain persistently high, despite lower refinancing risks.

Rating Action

On Nov. 29, 2012, Standard & Poor's Rating Services revised its outlook on Suzano Papel e Celulose S.A. to negative from stable. At the same time, we affirmed our 'BB' ratings.

Rationale

The outlook revision follows the revision of our base-case scenario, which now incorporates a slower deleveraging trend in the next few years as uncertainties about the company's initiatives for debt reduction have grown. Suzano did manage to issue new equity through its shares offering and will most likely improve its credit metrics following the opening of its new pulp mill in Maranhão in late 2013. The company has successfully maintained sizable cash reserves relative to short-term debt maturities, and it has reduced refinancing risk by tapping new, long-term bank loans and securing financing to conclude the Maranhão project. However, a one-notch downgrade is possible in the next few quarters if the company can't reduce adjusted debt to EBITDA to below 5x by 2014.

We assumed in our previous base case that its debt to EBITDA would peak at slightly higher than 6.0x in 2013 as the company raised debt to conclude the Maranhão project, but we also expected the ratio to decline to 4.0-5.0x by 2014 due to a combination of noncore asset sales and the incremental cash flows from its Maranhão plant. We now believe that deleveraging may take longer, resulting in debt to EBITDA to remain around 6.0x (about 5.0x if surplus cash is netted when computing the ratio) by 2014.

The ratings also incorporate Suzano's recent initiatives to extend debt

maturities and reduce refinancing risks. The company managed to roll over about R\$2.8 billion in bank loans in 2012, thus reducing short-term maturities and preserving cash reserves. Coupled with the R\$1.46 billion equity issuance in July 2012 and the conversion of convertible debentures into equity, Suzano has enhanced its medium-term financial flexibility. It has also secured financing for its expansion projects and working-capital needs through a R\$2 billion standby credit facility with BTG Pactual, which will remain available through March 2014. We don't foresee any immediate, material change in Suzano's business and financial strategy due to the recent change of its CEO. Our assessment of Suzano's management and governance is "fair."

We assess Suzano's business risk profile as "satisfactory" due to its advantageous cost structure for pulp production that stems from its access to highly productive forest, its solid position in the global pulp market and the Brazilian market for uncoated and coated printing and writing paper and paperboard. Those factors help offset pulp price volatility, which we expect to remain significant in the next few years. Our revised base case assumes list prices for hardwood pulp at around \$750 per ton (CIF China). Under these conditions, coupled with Suzano's initiatives to reduce costs and the positive effects of a weaker local currency throughout 2013, we project EBITDA margins may improve to around 24% in 2013 from 22% in the 12 months ended September 2012. We also assume as our base case that Suzano will successfully start up its Maranhão plant by 2014, which should boost its EBITDA margins further.

Liquidity

Although Suzano's cash reserves are quite strong, we consider its liquidity as "adequate" because we project the company will breach covenants on its third debentures issue by the end of 2013. Still, our expectation is that the company's cash sources should exceed cash uses in the next 24 months, even under harsher market conditions. Our analysis incorporates the following assumptions:

- Cash sources (cash reserves of \$1.9 billion as of September 2012, the committed credit facility of around \$1 billion, and cash flow from operations of \$350 million - \$390 million in 2013 and 2014) will surpass cash uses (investments for \$1 billion in 2013 and probably \$550 million in 2014, scheduled debt payments of about \$240 million in the last quarter of 2012, \$407 million in 2013, and \$584 million in 2014, and some minor working capital variation and minimum required dividend payments) by more than 2.0x in the next two years.
- Cash sources would exceed cash uses even if Suzano's EBITDA were to decline by more than 30%.
- Under the term and conditions of its third debentures issuance of R\$678 million (\$340 million), Suzano is required to comply with maximum net debt to EBITDA of 4x by Dec. 31, 2012, which we anticipate it won't meet. As in previous years, Suzano may either negotiate a waiver fee with debenture holders or prepay the debentures using its robust cash reserves.

Outlook

The negative outlook reflects the possibility of a one-notch downgrade in the coming quarters if Suzano can't reduce its leverage metric below 5x by 2014 that could bring its credit metric to levels in line with the rating category. The ratings already incorporate that the company's financial flexibility will remain robust during the construction of Maranhão due to its successful debt refinancing strategy and the capital increase. Upside rating potential is currently limited due to the company's high debt.

Related Criteria And Research

- Criteria Methodology: Business Risk/Financial Risk Matrix Expanded, Sept. 18, 2012
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Sept. 28, 2011
- Key Credit Factors: Criteria For Rating The Forest Products Industry, Dec. 11, 2009
- 2008 Corporate Ratings Criteria, April 15, 2008

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Suzano Papel e Celulose S.A. Corporate Credit Rating	BB/Negative/--	BB/Stable/--
Suzano Trading Ltd. Senior Unsecured	BB	

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