

Brazil Pulp & Paper Trade

Slower Pulp Exports – Pressure for Price Cuts Continues to Build

■ Industry Overview

- **Key Takeaways** — We are negative on the August data as weak activity in Europe and the US drove another drop in Brazilian pulp exports (-5% M/M, -16% Y/Y), and coated paper imports reached the highest level since May 2011. Two key read-throughs: **1) higher pulp producer inventories**; given normal utilization rates, the weaker shipments suggest another rise in producer inventories in August (negative for price negotiations), and **2) paper import pressure**; we begin to see risk to the recent 8-10% paper price hike given weak global demand and China's overcapacity
- **August 2012 Summary** — Brazilian pulp shipments fell to 661,000 tonnes (-5% M/M) as weaker shipments to Europe and the US completely overshadowed the rebound in China (+28% M/M). Despite the M/M rebound, China activity remains below year ago levels (-3%) and below the YTD monthly average. In paper, imports increased for coated (+5% M/M) and uncoated (+25% M/M), while kraftliner exports rose (+24% M/M). Export prices were mixed; pulp (-3%), paper (+1-4%).
- **A Look Ahead...Better Activity, Yet With Price Risk** — As we enter Sept, we expect volume activity to reflect a slight improvement for both pulp and paper products, yet the risk to pricing remains as global demand has yet to find firm footing. Pulp: seasonal demand should allow for better activity, yet ongoing macro concerns may drive a below-average rebound; as such demand may fail to absorb recent inventory build by producers (a risk to prices). Paper: We expect stable paper demand in Brazil, yet the full implementation of the announced price increases may be restricted by imports.
- **Investment Strategy** — We remain cautious on Brazilian pulp stocks given expected pulp price pressure (-US\$50/mt in Sept-Oct) and rich valuations (Neutral Fibria, Sell Suzano). Within the sector, we prefer Klabin (Neutral) given growth potential, a healthy balance sheet and stable packaging fundamentals.

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Brazilian Pulp & Paper Imports/ Exports - Aug 2012

Brazil Pulp & Paper Trade	Aug-12	Jul-12	MoM %	Aug-11	YoY %	2012	2011	YTD %
PULP - Exports (000 tns)	661	692	-5%	785	-16%	5,546	5,571	0%
to Europe	320	368	-13%	359	-11%	2,650	2,751	-4%
to North America	137	155	-11%	207	-34%	1,029	1,140	-10%
to China	145	113	28%	149	-3%	1,313	1,141	15%
to Asia (ex China)	57	40	45%	57	0%	473	471	0%
to Rest of World	2	17	-86%	13	-81%	82	69	19%
PAPER - Net Exports (000 tns)	25	25	1%	51	-50%	381	393	-3%
Coated - P&W	-38	-35	7%	-25	53%	-234	-221	6%
Uncoated - P&W	55	63	-12%	72	-24%	573	540	6%
Kraftliner	17	13	24%	16	5%	151	183	-17%
Other*	-9	-16	-45%	-13	-32%	-108	-110	-2%

Source: MDIC/SECEX. CIRA *includes newsprint, cartonboard, and other paper products

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Pulp Exports

Aug 2012 Pulp Exports: May pulp exports were down 5% MM and down 16% Y/Y. North America and Europe were the regions that contributed to the decrease in the overall shipments. YTD pulp export activity remains mostly stable, with China activity remaining the key support to the figure (+15% YTD)

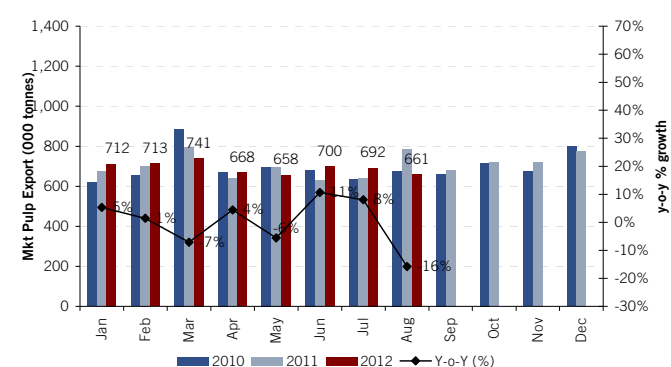
Aug 2012 Prices: Average export prices were down 3% M/M at \$492/ton.

Figure 1. Brazil Pulp Exports (000 tonnes)

BRAZIL PULP EXPORTS	Aug-12	Jul-12	MoM %	Aug-11	YoY %	2012	2011	YTD %
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to Asia (ex China)	57	40	45%	57	0%	473	471	0%
to Rest of World	2	17	-86%	13	-81%	82	69	19%
Export Mix								
to Europe	48%	53%		46%		48%	49%	
to North America	21%	22%		26%		19%	20%	
to China	22%	16%		19%		24%	20%	
to Asia (ex China)	9%	6%		7%		9%	8%	
to Rest of World	0%	2%		2%		1%	1%	
Exports/Capacity	80%	83%		95%		134%	143%	

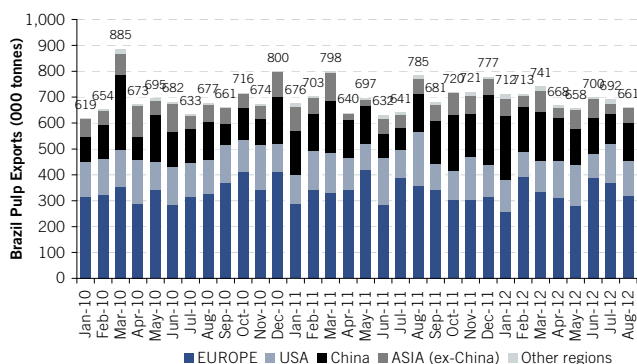
Source: MDIC/SECEX, Citi Research

Figure 2. Pulp Exports – Monthly (2010-12)



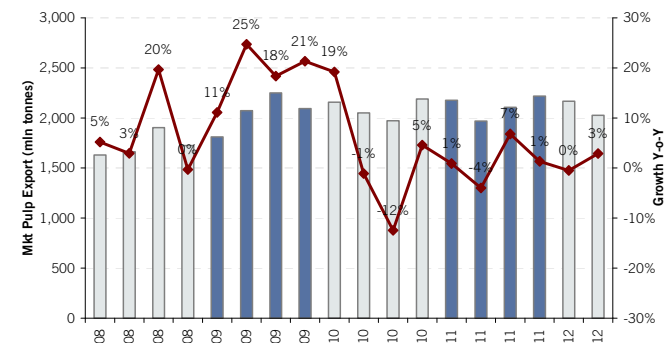
Source: MDIC/SECEX, Citi Research

Figure 3. Brazil Pulp Exports by Region



Source: MDIC/SECEX, Citi Research

Figure 4. Net Pulp Exports – Quarterly (2005-12)



Source: MDIC/SECEX, Citi Research

Figure 5. Brazilian Pulp Export by Region – Monthly

BRAZIL PULP EXPORTS	Aug-11	Sep-11	Oct-11	Nov-11	Dec-11	Jan-12	Feb-12	Mar-12	Apr-12	May-12	Jun-12	Jul-12	Aug-12
Total Exports (000 tonnes)	785	681	720	721	777	712	713	741	668	658	700	692	661
Y-o-Y Growth	15.9%	3.0%	0.6%	7.0%	-2.8%	5.3%	1.5%	-7.1%	4.5%	-5.6%	10.7%	8.0%	-15.8%
Europe	359	342	305	303	318	257	392	332	310	281	389	368	320
US	207	101	114	165	120	124	96	124	144	157	92	155	137
China	149	168	212	166	274	248	172	187	166	140	143	113	145
Asia (ex China)	57	60	86	73	59	66	47	79	41	74	69	40	57
to Other Regions	13	10	2	14	6	17	7	19	8	5	7	17	2
Export Mix													
Europe	46%	50%	42%	42%	41%	36%	55%	45%	46%	43%	56%	53%	48%
US	26%	15%	16%	23%	15%	17%	13%	17%	21%	24%	13%	22%	21%
China	19%	25%	30%	23%	35%	35%	24%	25%	25%	21%	20%	16%	22%
Asia (ex China)	7%	9%	12%	10%	8%	9%	7%	11%	6%	11%	10%	6%	9%
to Other Regions	2%	1%	0%	2%	1%	2%	1%	3%	1%	1%	1%	2%	0%
Exports/Capacity	95%	82%	87%	87%	94%	86%	86%	89%	81%	79%	84%	83%	80%

Source: MDIC/SECEX, Citi Research

Paper Imports/Exports

Aug Paper Activity: Net Paper exports increased to 25k tonnes up 1% M/M, but down 50% Y/Y driven by higher coated paper imports and lower uncoated paper exports.

Pricing Activity (USD): Paper prices showed mixed performance in USD. Imported coated paper were up (+3% M/M), while kraftliner exports vs. imports prices were in opposite +4% M/M vs. -10% M/M, respectively.

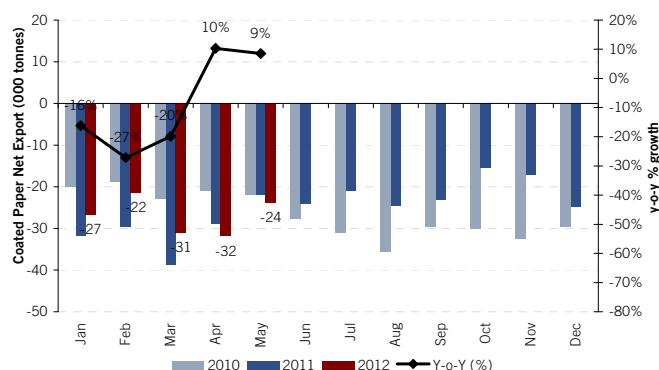
Figure 6. Brazil Paper & Paperboard Import/Exports (000 tonnes)

BRAZIL PAPER TRADE	Aug-12	Jul-12	MoM %	Aug-11	YoY %	2012	2011	YTD %
Total Net Exports	25	25	1%	51	-50%	381	393	-3%
Coated - P&W	-38	-35	7%	-25	53%	-234	-221	6%
Uncoated - P&W	55	63	-12%	72	-24%	573	540	6%
Kraftliner	17	13	24%	16	5%	151	183	-17%
Other*	-9	-16	-45%	-13	-32%	-108	-110	-2%
Exports	155	151	3%	172	-10%	1,332	1,402	-5%
Coated - P&W	2	2	-29%	2	-30%	17	26	-37%
Uncoated - P&W	73	77	-5%	90	-19%	681	684	0%
Kraftliner	17	13	24%	17	-3%	151	186	-19%
Other	64	58	11%	62	2%	483	505	-4%
Imports	130	126	3%	122	7%	950	1,009	-6%
Coated - P&W	39	37	5%	27	45%	251	247	2%
Uncoated - P&W	18	14	25%	18	0%	108	144	-25%
Kraftliner	0	0	-38%	1	-97%	0	3	-88%
Other*	73	74	-1%	75	-4%	591	615	-4%

*includes newsprint, cartonboard, and other paper products

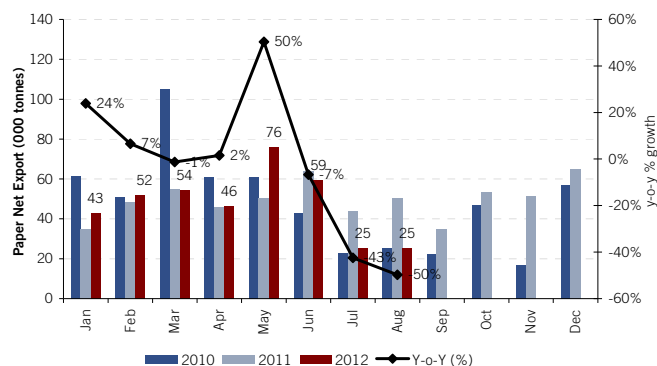
Source: MDIC/SECEX, Citi Research

Figure 8. Coated Paper – Net Exports – Monthly (2010-12)



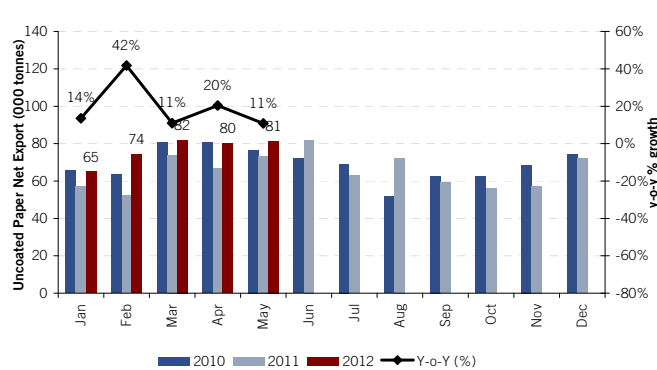
Source: MDIC/SECEX, Citi Research

Figure 7. Brazilian Paper Net Exports – Monthly (2010-12)



Source: MDIC/SECEX, Citi Research

Figure 9. Uncoated Paper – Net Exports – Monthly (2010-12)



Source: MDIC/SECEX, Citi Research

Figure 10. Brazilian Paper Net Export by Grade – Monthly

PAPER/ PAPERBOARD NET EXPORTS	Aug-11	Sep-11	Oct-11	Nov-11	Dec-11	Jan-12	Feb-12	Mar-12	Apr-12	May-12	Jun-12	Jul-12	Aug-12
Total Net Exports (000 tonnes)	51	35	53	51	65	43	52	54	46	76	59	25	25
Y-o-Y Growth	100%	56%	14%	206%	14%	24%	7%	-1%	2%	50%	-7%	-43%	-50%
Coated	-25	-23	-15	-17	-25	-27	-22	-31	-32	-24	-27	-35	-38
Uncoated	72	59	56	57	72	65	74	82	80	81	73	63	55
Kraftliner	16	22	24	20	20	25	16	21	17	26	15	13	17
Other	-13	-23	-12	-9	-2	-21	-17	-18	-19	-7	-1	-16	-9
Imports	122	132	109	103	102	120	106	124	122	118	105	126	130
Coated	27	27	19	20	27	28	24	33	34	25	29	37	39
Uncoated	18	25	18	15	15	12	10	14	13	14	13	14	18
Kraftliner	1	1	0	1	1	0	0	0	0	0	0	0	0
Other	75	79	72	67	59	80	72	77	74	78	63	74	73
Exports	172	167	162	155	167	163	157	178	168	194	165	151	155
Coated	2	4	3	3	2	2	2	2	2	1	2	2	2
Uncoated	90	85	74	72	87	77	84	96	93	95	85	77	73
Kraftliner	17	22	25	21	20	25	16	21	17	26	15	13	17
Other	62	56	60	58	57	59	54	59	55	71	62	58	64

Source: MDIC/SECEX, Citi Research

Export/Import Prices (FOB US\$/tonne)

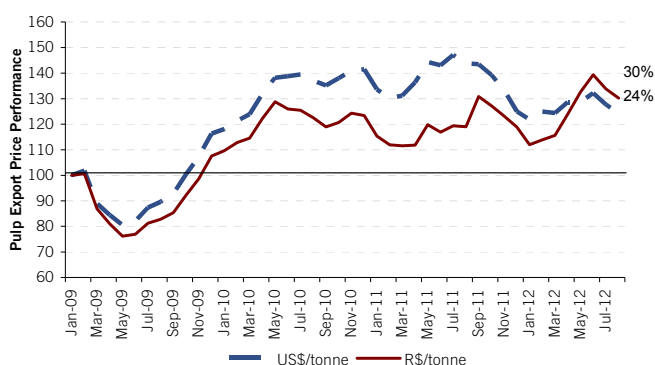
Figure 11. Performance – Brazilian Export/ Import Paper Prices (in US\$ and R\$ terms)

EXPORT/ IMPORT PRICES	Aug-12 US\$/tn	Performance - in USD terms				Performance - in BRL terms			
		1 month	6 months	1 year	YTD	1 month	6 months	1 year	YTD
Pulp Export Prices	492	-3%	-1%	-14%	-1%	-3%	14%	9%	10%
Europe	515	-1%	1%	-11%	3%	-1%	16%	13%	13%
U.S.	461	-3%	-8%	-18%	-10%	-3%	6%	4%	0%
China	476	-4%	0%	-17%	-1%	-4%	15%	5%	9%
Paper Export Prices									
Coated - P&W	1,205	1%	22%	6%	20%	1%	40%	34%	32%
Uncoated - P&W	969	1%	14%	-5%	10%	1%	32%	20%	21%
Kraftliner	565	4%	8%	-5%	0%	4%	25%	20%	10%
Paper Import Prices									
Coated - P&W	993	3%	-12%	-9%	-11%	3%	1%	15%	-2%
Uncoated - P&W	923	1%	-10%	-4%	-6%	1%	3%	21%	4%
Kraftliner	933	-10%	34%	118%	31%	-10%	54%	176%	44%

*Prices in FOB terms

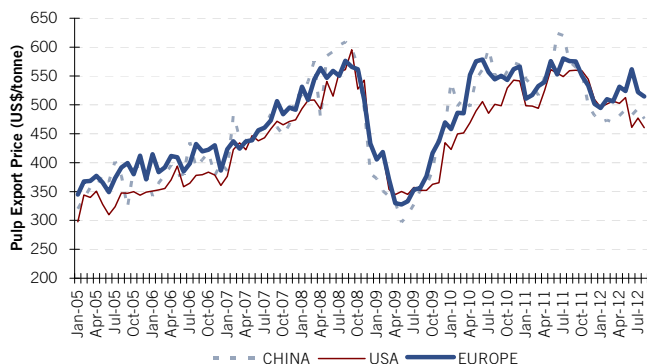
Source: MDIC/SECEX, Citi Research

Figure 12. Performance – Brazil Pulp Export Price (US\$ vs. R\$)



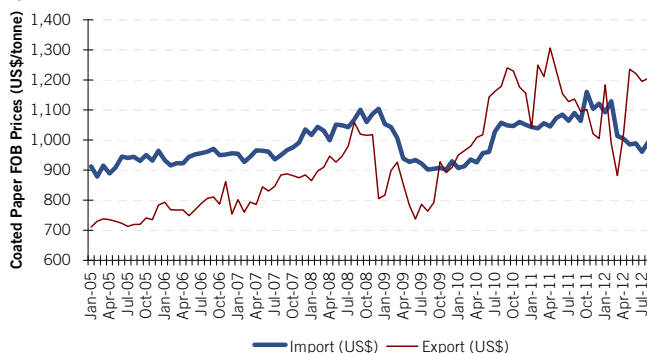
Source: MDIC/SECEX, Citi Research

Figure 14. BR Pulp Export Prices – Europe, US, China (US\$/tonne fob)



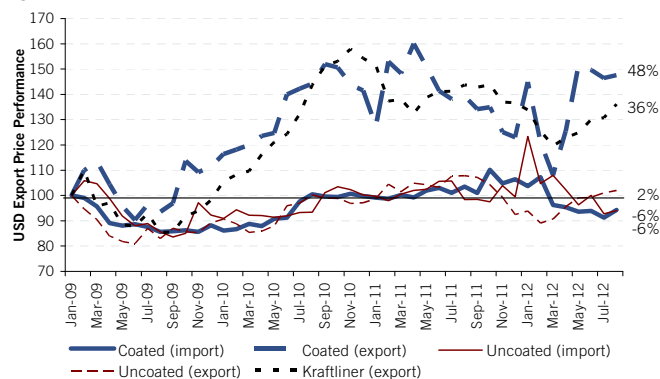
Source: MDIC/SECEX, Citi Research

Figure 16. Coated Paper Prices – Export vs. Import (US\$)



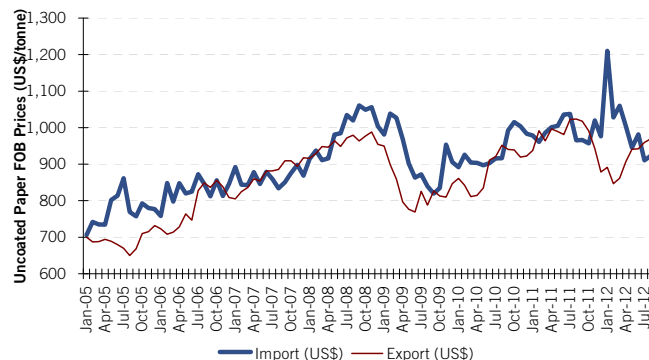
Source: MDIC/SECEX, Citi Research

Figure 13. Performance – Brazil Paper Export/Import Prices (US\$)



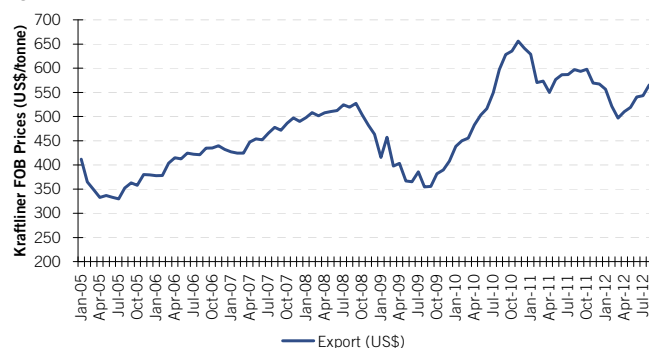
Source: MDIC/SECEX, Citi Research

Figure 15. Uncoated Paper Prices – Export vs. Import (US\$/tonne fob)



Source: MDIC/SECEX, Citi Research

Figure 17. Kraftliner Paper Export Prices



Source: MDIC/SECEX, Citi Research

Fibria Celulose SA

(FBR.N; US\$8.65; 2H)

Valuation

Our target price of US\$7.8/ADR (R\$15.5/share) is based on our multiple valuation (EV/EBITDA). We apply an EV/EBITDA multiple of 8.5x to our 2012E EBITDA forecast and derive a value of US\$7.8/ADR for Fibria. Our 8.5x target multiple is in line with Fibria's historical multiple.

Risks

We rate Fibria shares High Risk due to its highly leveraged balance sheet, which may limit its ability to invest in growth, exposure to volatile pulp markets and FX movements. Below we highlight some risks to our earnings estimates and the achievement of our target price:

1) Pulp Price Outlook: With almost 100% of its revenues generated from market pulp sales, Fibria's earnings are highly sensitive to pulp prices. Higher pulp prices would result in higher earnings and target price, while lower pulp prices would result in lower earnings and target price.

2) Exchange Rate Fluctuations: With 100% of revenues linked to US dollar and only 20% of its costs in US dollar, profitability declines when the Brazilian Real appreciates, but increases when the currency depreciates.

3) Brazilian Risk: Higher/lower Brazilian risk could negatively/positively affect FBR. The performance of Fibria shares is exposed to Brazilian risk in two main ways:

-Through its operations: 100% of Fibria's operations are located in Brazil.

-Through Market Sentiment: High Brazilian risk could negatively affect Fibria's cost of capital and share price performance.

Klabin SA

(KLBN4.SA; R\$9.78; 2)

Valuation

We set our R\$10.0 target price based on our DCF valuation model (R\$11/share) and multiple valuation (R\$9/share) with 50% and 50% weight respectively.

DCF Valuation.

We discount Klabin's free cash flows to the firm (FCFF) at a nominal average cost of capital of 9.5% in R\$ terms to determine the DCF value of the shares. Our base case scenario includes 5% terminal growth (4% long-term inflation + 1% real growth), an unlevered beta of 0.80, and a Brazilian risk-free rate of 6.3% and a Brazilian risk premium of 6.4%, which results in a DCF value of R\$11/share.

EV/EBITDA Valuation.

We apply an EV/EBITDA multiple of 8.0x to our 2013 EBITDA forecast and derive a value of R\$9.0/share. Our 8.0x target multiple follows the Brazilian consumer sector has traded over the past 5-years, and at a 25% premium to Klabin's historical

average, as we believe a re-rating is justified given renewed growth potential and improved earnings clarity.

Risks

We believe the primary risks associated with Klabin shares reaching our target price are:

Execution of cost improvements: Klabin made investments to improve the energy matrix of its plants as well as other projects to reduce its costs. If these investments and projects fail to be accomplished, there would be downside risk to our estimates and target price, while if they are well implemented, there would be upside risk.

Weaker domestic growth: We expect Klabin's sales volume to grow in line with the domestic market growth. However, if demand is lower than expected or Klabin's market share decreases, there would be downside risk to our forecasts. Conversely if domestic growth or Klabin's market share increases ahead of our expectations, there would be upside risk to our forecasts.

Exposure to Global Kraftliner Prices: Klabin is also exposed to the global kraftliner market and is affected by its growth patterns. If kraftliner prices are lower than we expect there would be downside risk to our estimates and target price, while if they are higher there would be upside risk.

Other risks related to an investment in Klabin are: overhang on share prices, if the BNDES decides to divest its stake in Klabin (15% of preferred shares); and BRL appreciation/depreciation could negatively/positively impact our estimates.

Suzano Papel e Celulose SA

(SUZB5.SA; R\$4.91; 3H)

Valuation

We set our R\$4.0 target price for Suzano based on our EV/EBITDA multiple valuation. We apply an EV/EBITDA multiple of 8x to our 2012 EBITDA forecast and derive a value of R\$4.0 per share for Suzano. Our 8x target multiple is above Suzano's 5-year historical multiple of 6.5x, yet in line with periods of pulp price pressure and slower growth; during the most recent pulp price downcycle, Suzano traded between 4.5x and 8x.

Risks

We rate Suzano High Risk due to its exposure to volatile pulp markets, operations in an emerging market country, low share liquidity and no tag along rights for preferred shareholders. Below we highlight the main risks to the shares reaching our target price:

- **Pulp Prices:** We forecast that 45% of 2011 revenues will be derived from pulp sales. Higher-than-expected pulp prices would have a positive impact on our earnings estimates and target price for Suzano, while lower pulp prices would have a negative impact.

- **Currency Appreciation:** As the majority of Suzano revenues are linked to the USD (direct export sales and or domestic sales linked to international prices) and only 30% of its costs are linked to the USD, earnings are likely to increase if the Brazilian currency weakens.

- **No Tag Along Rights:** Suzano has voting (ON) and non-voting (PN) shares outstanding. Most of the free float is of PN shares. While PN shareholders receive a 10% dividend premium, they are not entitled to tag along rights if control of the company changes. If the Suzano were acquired, the treatment of preferred and voting shareholders is likely to be different. If SUZB5 is acquired or there is a change in control, voting shareholders are entitled to receive 80% paid to the controlling shareholders. PN shareholders have no such guarantee at Suzano. While if the company decides to move to Novo Mercado and convert all shares into voting shares, this could be positive for the stock.

- **Relatively small size**, when compared to other Brazilian producers could result in a weaker competitive position.

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

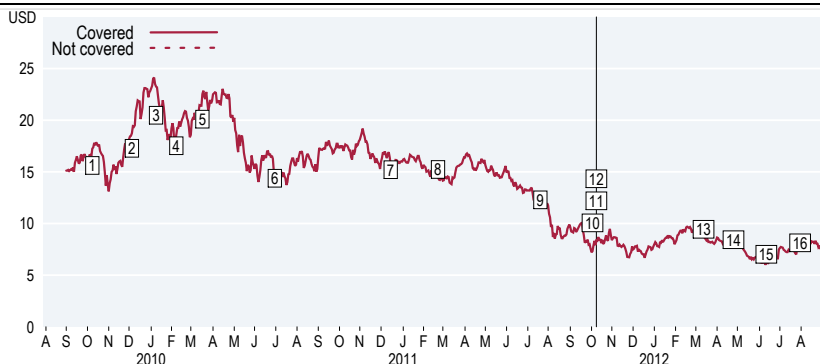
Fibra Celulose SA (FBR.N)

Ratings and Target Price History

Fundamental Research

Analyst: Juan G Tavaréz

Covered since December 5 2009



	Date	Rating	Target Price	Closing Price
1	8-Oct-09	3H	*14.00	17.24
2	4-Dec-09	3H	*18.00	18.74
3	8-Jan-10	*3M	*21.00	23.26
4	8-Feb-10	*1M	*21.50	18.61
5	17-Mar-10	1M	*26.00	22.53
6	30-Jun-10	1M	*21.00	14.80

* Indicates change

	Date	Rating	Target Price	Closing Price
7	15-Dec-10	1M	*20.50	15.72
8	22-Feb-11	1M	*19.00	14.50
9	20-Jul-11	*2M	*13.80	11.55
10	4-Oct-11	2M	*8.90	7.32
11	8-Oct-11	Stock rating system changed		
12	8-Oct-11	*2H	8.90	7.90

	Date	Rating	Target Price	Closing Price
13	13-Mar-12	*3H	*8.20	8.85
14	25-Apr-12	3H	*8.30	7.94
15	12-Jun-12	*2H	*7.10	6.18
16	31-Jul-12	2H	*7.80	7.69

Rating/target price changes above reflect Eastern Standard Time

Fibra Celulose SA (FBR.N)

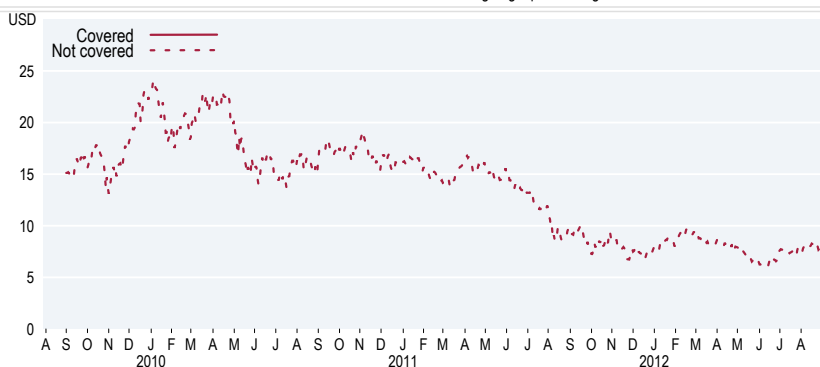
Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Juan G Tavaréz

Covered since December 5 2009



* Indicates change

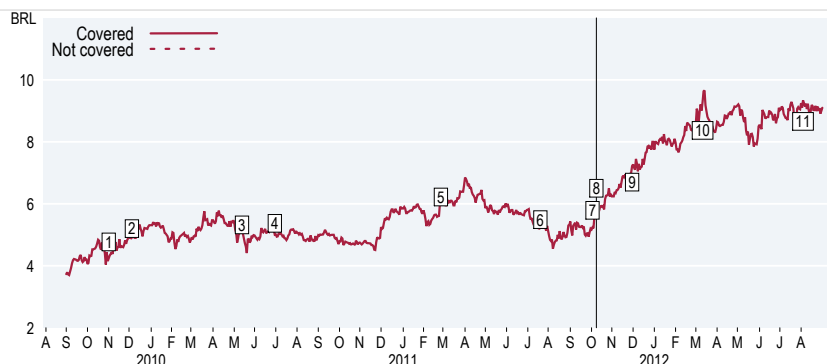
Rating/target price changes above reflect Eastern Standard Time

Klabin SA (KLB4.SA)

Ratings and Target Price History Fundamental Research

Analyst: Juan G. Tavares

Covered since December 5 2009



	Date	Rating	Target Price	Closing Price
1	2-Nov-09	2H	*5.00	4.15
2	4-Dec-09	2H	*5.50	4.91
3	13-May-10	2H	*6.00	5.24
4	30-Jun-10	2H	*6.20	5.00

* Indicates change

	Date	Rating	Target Price	Closing Price
5	25-Feb-11	*1H	*7.80	6.22
6	20-Jul-11	1H	*7.10	5.22
7	4-Oct-11	1H	*6.80	5.24
8	8-Oct-11	Stock rating system changed		

	Date	Rating	Target Price	Closing Price
9	30-Nov-11	*1	*8.00	7.22
10	12-Mar-12	*2	*9.50	9.29
11	3-Aug-12	2	*10.00	9.34

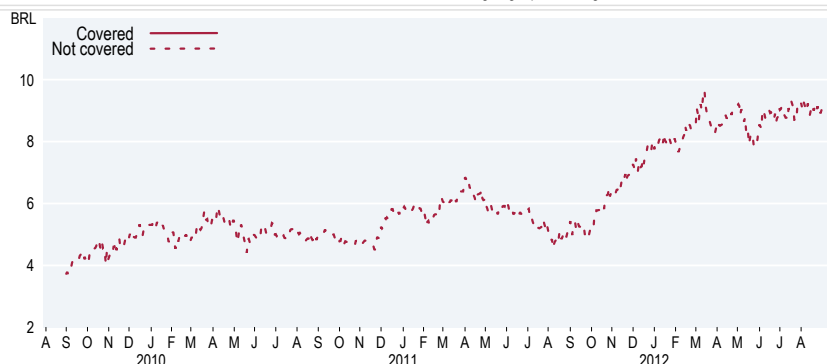
Rating/target price changes above reflect Eastern Standard Time

Klabin SA (KLB4.SA)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Juan G. Tavares

Covered since December 5 2009



* Indicates change

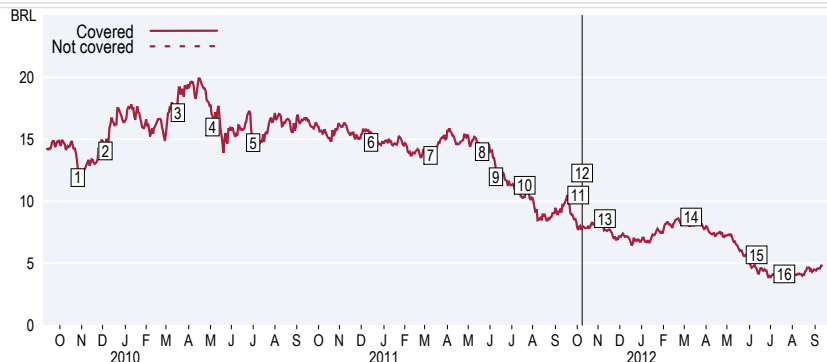
Rating/target price changes above reflect Eastern Standard Time

Suzano Papel e Celulose SA (SUZB5.SA)

Ratings and Target Price History Fundamental Research

Analyst: Juan G. Tavares

Covered since December 5 2009



	Date	Rating	Target Price	Closing Price
1	27-Oct-09	1H	*16.79	12.66
2	4-Dec-09	1H	*18.39	14.67
3	17-Mar-10	1H	*22.39	18.31
4	5-May-10	1H	*22.40	16.91
5	1-Jul-10	1H	*20.50	15.15
6	15-Dec-10	1H	*20.00	15.55

* Indicates change

	Date	Rating	Target Price	Closing Price
7	9-Mar-11	1H	*21.00	14.21
8	20-May-11	1H	*19.00	14.20
9	9-Jun-11	1H	*17.00	12.53
10	20-Jul-11	*2H	*12.00	10.29
11	4-Oct-11	2H	*9.30	7.69
12	8-Oct-11	Stock rating system changed		

	Date	Rating	Target Price	Closing Price
13	10-Nov-11	2H	*9.00	7.71
14	12-Mar-12	*3H	*8.00	8.04
15	12-Jun-12	3H	*4.50	4.55
16	20-Jul-12	3H	*4.00	3.99

Rating/target price changes above reflect Eastern Standard Time

Suzano Papel e Celulose SA (SUZB5.SA)

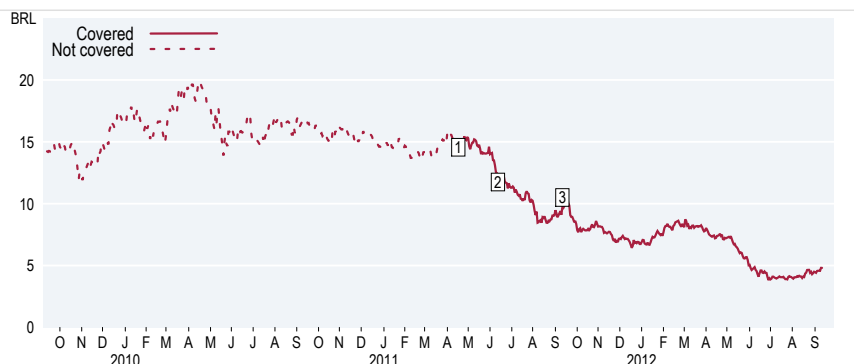
Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Juan G Tavaréz

Covered since December 5 2009



	Date	Rating	Target Price	Closing Price
1	18-Apr-11	*ADD MP	-	14.60

* Indicates change

	Date	Rating	Target Price	Closing Price
2	13-Jun-11	*REM MP	-	11.98

	Date	Rating	Target Price	Closing Price
3	12-Sep-11	*ADD LP	-	9.70

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Data current as of 1 Jul 2012

Citi Research Global Fundamental Coverage

% of companies in each rating category that are investment banking clients

12 Month Rating			Relative Rating		
Buy	Hold	Sell	Buy	Hold	Sell
53%	37%	10%	10%	80%	10%
44%	43%	40%	48%	43%	45%

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