

M. Dias Branco

4Q20 Review – Very weak; lowering ests; remain cautious

Commodity reflation is taking its toll: all-time low gross margin of 28.6%

MDB reported a tricky and volatile quarter that we believe underscores how tough life can still be in 2021. Net sales missed us by 7% to R\$1.7bn on much lower volumes, while better average prices did little to prevent a massive 910bps y/y gross margin drop to 28.6%, the lowest on record on higher raw material costs and operational deleverage. EBITDA was polluted by a one-time tax reversal, without which we estimate the recurring figure would be R\$45mn, 75% below our call and 81% lower y/y. Sales expenses rose on intensifying marketing efforts, more than offsetting G&A cuts, to a recurring EBITDA margin of 2.6%, 1170bps lower y/y and also a historical low. Based on a recurring LTM EBITDA, leverage ratio rose to 0.8x.

Too much pricing? Volumes sank 15% y/y with lower market share

Volumes were down 15% y/y, led by all core categories, with MDB clearly trying to recompose margins via an average price hike of 13% q/q, with market share slumping 40bps in cookies and 140bps in pasta. Most intriguing to us is that MDB is pushing prices so much ahead of the competition despite being vertically integrated and holding several months of raw material inventory. We also believe that MDB's greatest exposure to the northeast region, where the impact of the government's financial aid is arguably higher, could explain greater price elasticity. Market share/volume volatility underscore a still unstable commercial platform.

Headwinds intensifying; mixed views on strategic direction; TP down to R\$29

While we believe that MDB (and the rest of the industry) will be able to force prices higher in the early months of 2021 to offset commodity/FX inflation, it is clear that it not only should take a few quarters before margins can recover as it won't come without a strong dose of volume pressure. We also wonder whether MDB strategy to focus on third party distributors (now 8.2% of sales from 4.4% a year ago) while reducing sales to more profitable channels won't jeopardize mix/margins even more, while making higher marketing investments less effective. We're updating our estimates to a 14% below consensus 2021 EBITDA of R\$783mn. With a controversial commercial strategy playing out, a tougher macro, and low visibility on LT margins, we remain cautious on the stock, our bottom F&B pick (details on pages 2 and 3).

Valuation	12/2019	12/2020	12/2021E	12/2022E	12/2023E
RoIC (EBIT) %	6.3	5.9	6.8	12.2	13.3
EV/EBITDA	20.3	17.4	13.5	8.6	7.9
P/E	23.2	15.1	20.6	12.2	11.1
Net dividend yield %	0.7	1.2	0.2	2.2	2.5

Financials (R\$m)	12/2019	12/2020	12/2021E	12/2022E	12/2023E
Revenues	6,104	7,253	7,641	8,309	8,990
EBITDA	672	696	783	1,225	1,327
Net Income	557	764	504	851	940
EPS (R\$)	1.64	2.25	1.49	2.51	2.77
Net DPS (R\$)	0.25	0.40	0.07	0.68	0.76
Net (debt) / cash	(717)	(555)	(131)	(131)	(131)

Source: Company reports, Bovespa, BTG Pactual S.A. estimates. / Valuations: based on the last share price of the year; (E) based on a share price of R\$30.70, on 31 March 2021.

ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 6

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Rating	Neutral
12m Price Target	R\$29.00/US\$5.15
Price	R\$30.70/US\$5.45
RIC: N.A., BBG: MDIA3 BZ	

Trading Data and Return Forecasts

52-wk range	R\$40.92-27.15/US\$8.24-5.06
Market cap.	R\$10,407m/US\$1,847m
Shares o/s (m)	339.0
Free float	25%
Avg. daily volume('000 Shares)	1,109
Avg. daily value (R\$ m)	34.5
Forecast price appreciation	-5.5%
Forecast dividend yield	0.2%
Forecast stock return	-5.3%

Stock Performance (R\$)



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4Q20 Review – Very weak

Table 1: M.Dias Branco – 4Q20 Review

Income Statement (R\$m)	4Q20	4Q20E	4Q19	3Q20	A/E	y/y	q/q
Net Revenues	1,702	1,828	1,694	2,029	-6.9%	0.4%	-16.1%
COGS	(1,214)	(1,233)	(1,055)	(1,380)	-1.5%	15.1%	-12.0%
Gross Profit	487	594	639	649	-18.0%	-23.8%	-25.0%
Selling Expenses	(369)	(360)	(334)	(400)	2.5%	10.6%	-7.6%
Adm Expenses	(70)	(83)	(82)	(75)	-16.3%	-14.6%	-7.1%
Taxes	(13)	(11)	(10)	(8)	12.3%	21.2%	55.6%
Depreciation on expenses	(22)	(20)	(19)	(23)	9.0%	17.6%	-5.6%
Other Operating	112	0	34	120	n.m.	n.m.	n.m.
EBIT	126	120	228	263	5.2%	-44.9%	-52.2%
Depreciation	68	63	61	67	7.5%	10.7%	1.9%
EBITDA	194	183	290	330	6.0%	-33.1%	-41.2%
Adjusted EBITDA	45	183	243	205	-75.4%	-81.5%	-78.1%
Financial	57	(8)	37	31	n.m.	n.m.	n.m.
EBT	181	112	265	292	62.0%	-31.5%	-37.9%
Income Taxes	31	0	(9)	(56)	n.m.	n.m.	n.m.
IT Benefits	(3)	4	9	30	n.m.	n.m.	n.m.
Net Income	209	116	265	265	80.1%	-21.1%	-21.3%
Adj. Net Income	(35)	116	174	103	n.a.	n.a.	n.a.
Gross Margin	28.6%	32.5%	37.7%	32.0%	-3.9p.p	-9.1p.p	-3.4p.p
Operating Margin	7.4%	6.5%	13.5%	13.0%	0.9p.p	-6.1p.p	-5.6p.p
Adj. EBITDA Margin	2.6%	10.0%	14.4%	10.1%	-7.4p.p	-11.7p.p	-7.5p.p
Net Margin	12.3%	6.4%	15.6%	13.1%	5.9p.p	-3.4p.p	-0.8p.p
Adj. Net Margin	-2.1%	6.4%	10.3%	5.1%	-8.4p.p	-12.3p.p	-7.1p.p
Operating Highlights	4Q20	4Q20E	4Q19	3Q20	A/E	y/y	q/q
Net Revenues (R\$m)	1,702	1,828	1,694	2,029	-6.9%	0.4%	-16.1%
Biscuits	845	920	897	1,018	-8.2%	-5.8%	-17.0%
Pasta	387	409	378	458	-5.3%	2.3%	-15.4%
Flour and Bran	303	343	289	397	-11.8%	4.8%	-23.7%
Margarines and Fats	132	118	94	116	11.7%	40.2%	14.3%
Other	35	37	36	42	-6.9%	-2.3%	-16.4%
Volumes (000 ton)	416	491	492	559	-15.3%	-15.5%	-25.6%
Biscuits	126	143	141	157	-11.4%	-10.0%	-19.4%
Pasta	95	106	105	122	-10.7%	-9.9%	-22.5%
Flour and Bran	164	213	220	250	-23.2%	-25.5%	-34.5%
Margarines and Fats	27	25	23	25	5.0%	14.6%	6.8%
Other	4	4	4	5	20.0%	20.0%	-8.7%
Avg. Price (R\$/kg)	4.09	3.72	3.44	3.63	9.9%	18.9%	12.7%
Biscuits	6.69	6.45	6.39	6.49	3.7%	4.7%	3.1%
Pasta	4.10	3.86	3.61	3.75	6.2%	13.6%	9.2%
Flour and Bran	1.85	1.61	1.31	1.59	14.8%	40.6%	16.5%
Margarines and Fats	4.95	4.65	4.04	4.62	6.4%	22.4%	7.0%
Other	8.26	10.65	10.14	9.02	-22.4%	-18.5%	-8.4%
COGS/kg	(2.92)	(2.51)	(2.14)	(2.47)	16.3%	36.3%	18.3%
Adj. EBITDA/kg	0.11	0.37	0.49	0.37	-71.0%	-78.1%	-70.6%

Source: Company / BTG Pactual

It's time to make adjustments...

We're taking a much-needed opportunity to revise our forecasts in light of an increasingly concerning combination of poorer macro backdrop for Brazil's domestic consumption, rising raw material costs and what we still see as a mixed new commercial strategy, where the focus on "attack" regions seems to be increasingly

jeopardizing MDB's fortress based on shelf space occupation of small retailers and a direct distribution platform. The growing focus on brand building (pull strategy) as opposed to the volume-based (push strategy) approach that defined MDB for many years still presents mixed results with regards to its capacity to create value.

In 4Q20, when the income boost provided by the government's financial support likely started to fade, we saw an unprecedented level of price elasticity, with corresponding market share erosion for MDB. What makes this even more intriguing to us is that this is happening for a company whose vertically integrated production model historically meant that times of rising raw material costs were times when it would wait for the competition to pass on higher prices while gaining some share. This time it was the other way around: MDB apparently rose prices earlier, sacrificing share, while being unable to recompose margins on the back of a strong push to marketing/trade-marketing and an apparent channel/mix erosion. Our longstanding thesis of MDB as a story of declining marginal returns never made so much sense, in our view.

We're lowering our 2021 forecasts considerably to reflect a much weaker exit rate from 2020, which we believe means that it'll take time before margins can recover from all-time lows. MDB's need to push prices higher while hoping not to lose market share and volumes seems an increasingly tough task. We're now some 14% below consensus on 2021 EBITDA, while we also believe our LT EBITDA margin call of 15%, which reflects lower pricing power in regions/channels that are growing the most, is probably much lower than what the consensus (and the company) deem feasible. We remain cautious on the stock with a 12-month forward TP of R\$29/sh. Trading at 20.6x P/E 2021, we also see no reason to hope for a near-term rebound whatsoever.

Table 2: New vs. Old Estimates

(R\$mn)	2020E			2021E		
	New	Old	Δ	New	Old	Δ
Net Revenues	7,641	8,105	-5.7%	8,309	8,517	-2.4%
EBITDA	783	1,190	-34.2%	1,225	1,398	-12.4%
<i>EBITDA Margin</i>	10.3%	14.7%	-4.4p.p	14.7%	16.4%	-1.7p.p
Net Earnings	504	847	-40.5%	851	1,019	-16.5%
<i>Net Margin</i>	6.6%	10.5%	-3.9p.p	10.2%	12.0%	-1.7p.p

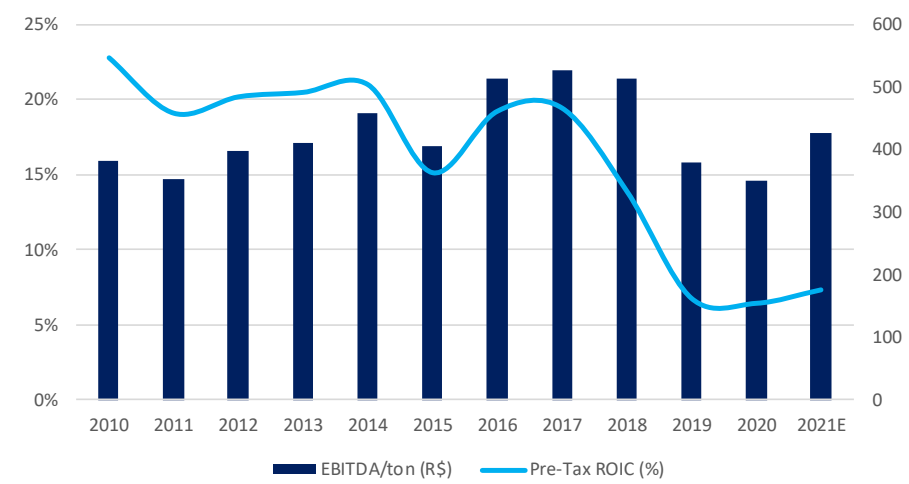
Source: BTG Pactual

Table 3: New Estimates vs. Consensus

(R\$mn)	2020E			2021E		
	BTGP	Cons.	Δ	BTGP	Cons.	Δ
Net Revenues	7,641	7,615	0.3%	8,309	8,207	1.2%
EBITDA	783	909	-13.8%	1,225	1,191	2.8%
<i>EBITDA Margin</i>	10.3%	11.9%	-1.7p.p	14.7%	14.5%	0.2p.p
Net Earnings	504	650	-22.4%	851	822	3.6%
<i>Net Margin</i>	6.6%	8.5%	-1.9p.p	10.2%	10.0%	0.2p.p

Source: Thomson Reuters / BTG Pactual

Chart 1: 2021 ROIC is expected to remain well below the 10-year average of 17%, as margins take longer to recover



Source: Company / BTG Pactual

Income Statement (R\$m)	12/2016	12/2017	12/2018	12/2019	12/2020	12/2021E	12/2022E	12/2023E
Revenue	5,328	5,415	6,024	6,104	7,253	7,641	8,309	8,990
Operating expenses (ex depn)	(4,322)	(4,373)	(5,048)	(5,488)	(6,796)	(6,858)	(7,084)	(7,663)
EBITDA (BTG Pactual)	919	967	936	672	696	783	1,225	1,327
Depreciation	(119)	(128)	(182)	(234)	(260)	(267)	(279)	(281)
Operating income (EBIT, BTG Pactual)	801	839	753	438	436	516	946	1,047
Other income & associates	0	0	(3)	100	278	0	0	0
Net Interest	32	77	46	31	81	(25)	(8)	(8)
Abnormal items (pre-tax)	0	0	0	0	0	0	0	0
Profit before tax	832	916	797	569	796	492	938	1,039
Tax	(48)	(71)	(74)	(12)	(32)	12	(87)	(99)
Profit after tax	784	845	723	557	764	504	851	940
Abnormal items (post-tax)	0	0	0	0	0	0	0	0
Minorities / pref dividends	0	0	0	0	0	0	0	0
Net Income (local GAAP)	784	845	723	557	764	504	851	940
Adjusted Net Income	784	845	723	557	764	504	851	940
Tax rate (%)	6	8	9	2	4	0	9	10
Per Share	12/2016	12/2017	12/2018	12/2019	12/2020	12/2021E	12/2022E	12/2023E
EPS (local GAAP)	2.31	2.49	2.13	1.64	2.25	1.49	2.51	2.77
EPS (BTG Pactual)	2.31	2.49	2.13	1.64	2.25	1.49	2.51	2.77
Net DPS	0.52	0.56	0.41	0.25	0.40	0.07	0.68	0.76
BVPS	12.78	14.73	16.41	17.80	19.60	21.09	21.47	22.02
Cash Flow (R\$m)	12/2016	12/2017	12/2018	12/2019	12/2020	12/2021E	12/2022E	12/2023E
Net Income	784	845	723	557	764	504	851	940
Depreciation	119	128	182	234	260	267	279	281
Net change in working capital	144	(127)	(264)	(12)	(398)	(68)	(113)	(159)
Other (operating)	0	0	0	0	0	0	0	0
Net cash from operations	1,048	845	641	778	626	703	1,017	1,062
Cash from investing activities	(260)	(298)	(905)	(395)	(328)	(280)	(294)	(309)
Cash from financing activities	(112)	(302)	907	(167)	702	(800)	(0)	(0)
Bal sheet chge in cash & equivalents	511	66	(475)	(86)	865	(377)	0	0
Balance Sheet (R\$m)	12/2016	12/2017	12/2018	12/2019	12/2020	12/2021E	12/2022E	12/2023E
Cash and equivalents	860	926	451	365	1,229	853	853	853
Other current assets	1,492	1,626	1,998	1,957	2,641	2,711	2,841	3,035
Total current assets	2,352	2,552	2,449	2,322	3,871	3,564	3,693	3,888
Net tangible fixed assets	2,297	2,468	3,191	3,352	3,419	3,432	3,447	3,476
Net intangible fixed assets	832	857	1,730	1,722	1,719	1,719	1,719	1,719
Investments / other assets	200	213	438	705	721	721	721	721
Total assets	5,681	6,090	7,807	8,101	9,730	9,436	9,581	9,803
Trade payables & other ST liabilities	469	476	584	530	817	819	836	871
Short term debt	348	114	697	623	817	817	817	817
Total current liabilities	817	589	1,281	1,154	1,634	1,636	1,653	1,688
Long term debt	295	228	552	458	967	167	167	167
Other long term liabilities	235	281	413	454	483	483	483	483
Total liabilities	1,347	1,098	2,246	2,066	3,084	2,286	2,303	2,339
Equity & minority interests	4,334	4,992	5,562	6,035	6,646	7,150	7,278	7,464
Total liabilities & equities	5,681	6,090	7,807	8,101	9,730	9,436	9,581	9,803

Company Profile:

M Dias Branco S.A. Indústria e Comércio de Alimentos. The Group's principal activities are to manufacture, distribute and marketing of food products like: cookies, breads, pastas and it also operates in the segments of wheat grinding, oil refining, fats, margarine and vegetable creams. It imports wheat, maize, raw materials and packaging materials.

Financial ratios	12/2019	12/2020	12/2021E	12/2022E	12/2023E
EBITDA margin	11.0%	9.6%	10.3%	14.7%	14.8%
Operating margin	7.2%	6.0%	6.8%	11.4%	11.6%
Net margin	9.1%	10.5%	6.6%	10.2%	10.5%
RoE	9.6%	12.0%	7.3%	11.8%	12.7%
RoIC	6.3%	5.9%	6.8%	12.2%	13.3%
EBITDA / net interest	-22.0x	-8.6x	31.8x	155.3x	168.3x
Net debt / EBITDA	1.1x	0.8x	0.2x	0.1x	0.1x
Total debt / EBITDA	1.6x	2.6x	1.3x	0.8x	0.7x
Net debt / (net debt + equity)	10.6%	7.7%	1.8%	1.8%	1.7%

Source: Company reports and BTG Pactual estimates. Valuations: based on the last share price of that year(E) based on share price as of 31 March 2021

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Buy	Expected total return 10% above the company's sector average.	60%	52%
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Sell	Expected total return 10% below the company's sector average.	1%	0%

1: Percentage of companies under coverage globally within the 12-month rating category.

2: Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

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- b) a Neutral rated stock can not have an expected total return below -5%
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Valuation Methodology

M. Dias Branco S.A. [BRMDIAS] (Primary) - Our TP is DCF-based, using Ke and g of 8.1% and 3.0%, both in USD terms.

Company Disclosures

Company Name	Reuters	12-mo rating	Price	Price date
M. Dias Branco ^{1, 2, 4, 6, 10, 18, 19, 22}	N.A.	Neutral	R\$30.70	31-3-2021

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M. Dias Branco



Source: BTG Pactual and Economática. Prices as of 31 March 2021

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