Q2 2009 Earnings Call

Company Participants

- Andre Gerdau Johannpeter, President, CEO
- Osvaldo B. Schirmer, Vice President, IR Officer
- Unidentified Speaker, Unknown

Other Participants

- Carlos De-Alba, Analyst
- Felipe Hirai, Analyst
- Leonardo Correa, Analyst
- Rodolfo De Angele, Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good afternoon. And thank you for Gerdau's Second Quarter of 2009 Earnings Conference Call. At this moment, all participants are connected in listen-only mode. And later on we will start the question and answer period.

(Operator Instructions).

We would like to stress that statements that might be made during this call; they may seem to be business outlook of Gerdau projections, operating and financial targets or just forecasts, which are based on expectations by the company's management regarding the company's future. Although, Gerdau believes that its remarks are based on reasonable assumptions, there is no guarantee that future events will not affect this evaluation.

Today, we have with us, Mr. Andre Gerdau Johannpeter, President and CEO of the company. And Osvaldo Schirmer, Vice President and IRO. Now, I would like to give the floor to Mr. Andre Gerdau Johannpeter, please you may proceed, Mr. Johannpeter.

Andre Gerdau Johannpeter

Thank you.

Good afternoon. Welcome to our Second Quarter of 2009 Earnings Conference Call.

As we always do, we will start with an analysis of our performance in the period. And of the outlook for the market in which we operate. Osvaldo Schirmer, later on she will talk in detail about our financial performance. And soon after that, we will be available for your questions.

For those who are following us on the Internet, on screen number two, we have the highlights for the period. We continue to see a gradual recovery of demand for steel in the world. In the worldwide level production was 286 million tons of steel in the Second Quarter, an increase of 8% vis-a-vis the First Quarter of 2009, according to the World Steel Association.

Once again, China stands out accounting for 49% of the world's steel production with 139 million tons produced, which means a 9% increase vis-a-vis the First Quarter of 2009.

This trend has already been identified in our earnings conference call for this First Quarter. And with a comparison at the time between the sales volume, between December 2008 and March 2009.

Therefore, the evolution of market has been felt month by month. But with different improvement depending on the geography and the lines of products in the operation.

Therefore, the comparison that we will make is always between the performance of the Second Quarter vis-a-vis the First Quarter of '09 because the periods are in one same economic scenario.

From April to June 2009, we continued to work to adjust our operations with this new market reality in a fast and efficient manner.

With the important commitment of our teams, we were able to increase our cash to BRL6.3 billion. And we have a higher sales volume. And a reduction in our working capital, mainly in terms of inventories and cost as well. Over the first half-year, total production costs of the company were touched by BRL2.4 billion, therefore contributing a lot to the increase in the company's cash position.

Besides, there has been a major reduction in our gross sketch, in mainly our net debts during the half year. Gross debt comes to BRL20 billion, to BRL18.9 billion. And net debt comes BRL17.7 billion to BRL12.7 billion.

Now, I would like to talk about our shipments. For those who are following us on the Internet, this means slide number three.

You can see in the bar chart, consolidated shipments, 3.4 million tons during the Second Quarter, an evolution of over 10% in our operations. And here in the chart, you can see the breakout per operation.

The signs of recovery are shown by comparisons between the consolidated shipments in December 2008. And through 2009, when we had an increase of 26.2% in this period.

Now, I'm going to talk about sales according to each one of the operations. But I would like to ask you to see here on the right, the monthly evolution of shipments, where we show a chart with our monthly shipments starting in January '07 with 100 basis. And we see a growth until half July '08. And then a drop with the world crisis, which strongly affected our shipments. And then a recovery as of January 2009 until July, where we reached 95% in a comparison with January '07.

Our monthly shipments are already going back to our 2007 levels. And which was an important recovery in our market. More specifically about Brazil, sales were 1.2 million tons shipped, which means 11% higher than the First Quarter. It is important to stress that the gradual reaction of the domestic market does not occur at the same pace in exports.

In the domestic market, the evolution was of 13%, mainly 812,000 tons, which means a significant growth. And exports grew by 7%, amounting to 400,000 tons in a slower pace, as you can see. And export revenue was BRL389 million. In North America, we showed 1.2 million tons from April to June, exceeding by 15%, the volume achieved in the First Quarter.

And this performance is a consequence of the change in the inventory of our skilled distributors or service centers and some signs of recovery in the U.S. economy already, in spite of the fact that market conditions are still difficult, there are some signs of improvement. During the quarter, we could see that volumes were stable and prices as well for our whole product line.

And for most of our products, there is an inventory volume, which is in line or slightly below demands in the whole chain that supplies the market. In Latin America, 507,000 tons, 4% higher vis-a-vis the First Quarter of '09.

And part of this volume was caused by the inventories that were funded before with higher costs, because they were manufactured when there was a higher demand for steel.

And in this recovery process, I would like to stress the importance of the Chilean Gerdau mix in specialty steels, 6% higher sales, reaching 420,000 tons. Our units in the United States and Spain were the most deeply affected by the crisis that impacted the automotive sector different from Brazil. In general, the inventory for the automotive chain is very well adjusted, both in Brazil. And the United States. And Spain as well.

Regarding the heavy vehicle segment, there is still a need for re-adaptation of inventories, especially in the United States and Spain. And here, we would like to highlight Brazil, where the production of automotive vehicles in the Second Quarter, increased by 22%, vis-a-vis the three first months of '09 reaching 807,000 units, a performance that was encouraged by the maintenance of the lower industrialized products tax.

In the United States, 3% increase, 1.2 million units. And the production of cars and light commercial vehicles had an even more expansive growth, a growth by 14% in the period, in the United States and Europe, started by government measures taken. The licensing of light vehicles grew by 16% in the Second Quarter, vis-a-vis the first three months of 2009, reaching 3.9 million units produced. And the licensing of commercial vehicles, however dropped by 17% in the same period.

On page number four, about steel production. The consolidated crude steel production, 3.1 million tons is a very major increase, 22%. I would like to stress the performance of Brazil with an evolution of 33%, North America, 17% increase, specialty steel 28%. And Latin America in line with the First Quarter practically.

On slide number five, I would like to talk about the major figures of Gerdau's net revenues, amounting to BRL6.4 billion, with a reduction of 8% vis-a-vis the First Quarter of '09.

Because of the lower prices practiced in the different markets and also due to the negative exchange rate effect on revenues generated in dollars, when they were converted into Real, which was partially offset by the higher volume sales sold in the period. And the EBITDA was BRL595 million.

Also, due to the grow-up in the steel prices, the EBITDA was kept in line with the First Quarter of '09, in spite of the increase in the volume of shipments.

Now, net income for the quarter without the non-recurrent items was BRL467 million. Here, we are not considering the non-recurring items, as I said before, which Schirmer would explain later on. These items are related to the BP/E write-offs and intangibles. And goodwill, which had a negative impact of BRL796 million in our earnings, net of income tax. As a consequence, we had a negative accounting result of BRL329 million.

And the earnings for the quarter are impacted by these non-recurring items and with no significant impact on our cash. And this does not reflect the efforts of operational adjustments that we had, that we carried out in the scenario of a reduced demand. But that has a gradual improvement as you can see.

Investments, though there was a disbursement during the quarter of a $149 million. So that we could continue our project, that we're already underway. Half of that was for investment in Brazil. And half of that operation is about for 2009. Our forecast for disbursements is BRL550 million. And BRL391 million have already been invested over the first half of the year.

I would like to mention also our covenants, when in June we got the approval of our proposal to make our performance clauses or covenants more flexible for some time in the financial contracts that we have with banks. I would like to stress the initiative by Gerdau in terms of being proactive by negotiating the performance clauses, because of a probable adverse scenario in the future in the company was very well received by the financial market.

And it reinforced the credibility acquired over one century of operations with a sound and responsible financial management. And Schirmer will inform you about this covenant operation in detail later on. On slide number six, we talk about the outlook for the future. And the realities, that we see a gradual evolution in the world economic scenario. And that we saw already during the Second Quarter.

And that should continue during the next two periods for 2010. Our outlook for the evolution of the economy is more optimistic, as we believe there will be an expansion of 2.5% of the GDP in the world, or according to data by the IMF.

And then, world steel production, considering the strong historical correlation between economic growth and the evolution of the fuel industry, the gradual improvement of the economic scenario will be translated into an expansion of steel consumption.

And I would like to talk now about Brazil, where the recovery of the economic activity will continue in the next few months. And measures taken by the government in order to increase credit facilities. And also to extend this reduction of the IPI. And to decrease interest rates are helping to this recovery of the industry.

And civil construction infrastructure works will become more pervasive in the second half of 2009, with the PEC project. And we're already supplying steel with many important (inaudible) works in the country, such as the Madera power plant and the (inaudible) in Sao Paulo.

With the construction, very good outlook, already an increase in the demand for (inaudible) re-barge. And we are also receiving many consultations about steel solutions, such as the welded grooves measured for the production of reinforced steel walls. This material is used mainly in more popular housing, which is related to the My House My Life program, which is focused on this segment.

And we understand that we already see some positive signals. And we believe that the demand for steel for this segment will continue.

For North America, we believe that the consequences of the stimulus package. And the increase in demand by (inaudible) users will be felt by Gerdau Ameristeel, as of mainly the Fourth Quarter of '09. And mainly in -- although we already see some recovery in the U.S. economy.

On page number seven, Latin America, we see a gradual recovery as well during the second half towards the end of 2009. And significant improvement in 2010, very much linked to incentive programs by governments and investments in infrastructure, in specialty steels, Brazil, United States and Spain.

We believe that government will continue to encourage consumption and giving support to the local industry, which are the examples of the reduction in this IPI, which is attached on industrialized products and also in Europe and in the United States, which will serve as a basis for a gradual recovery of this sector.

And inventories are already at more adequate levels, matching the pace of demand. And in the United States, the new measure for the exchange of old cars, what we call 'Cash for Clunkers', up to $4.5,000 per unit is released per (inaudible) use. And $1 billion have already been year-marked for the program. And additional $2 billion will be approved very soon.

And as a consequence, the payoff sales, the (inaudible) in 12 months went up to 11.2 million units in the United States, according to what was published in the press. And with the return of General Motors and Chrysler to the market, we see that there is already a higher demand in our order book, because of the whole chain, there are some inventories that are lower than the desired levels. And the demand for TEO for the automotive chain, supply chain in the United States. And (inaudible) in Brazil, in fact passes every cultural implements and construction equipments. In all these areas, we see the effect of government initiatives.

As of July, with a positive impact on the performance for the next quarter, besides the reduction of the IPI, the BNBS started to finance 100%. And interest rates came down, just to give an idea, the volume of steel used by a heavy truck, 1500 kilos is equivalent to 10 light vehicles.

And on the number eight, I would like to conclude my presentation with some remarks. And the first one is that we had a very difficult half-year in spite of the gradual recovery of the market. And in spite of the gradual recovery, we continued to assess the behavior of demands in a careful manner, in order to guarantee that our operations are adapted to the reality of markets.

Currently, we have a very well balanced company, very well adjusted to the market demand, with a major cash generation and major liquidity. We are prepared to, very quickly, meet the gradual evolution of demands. This is a very important point, because 75% of our production is by mini mills based on scrap and electric furnaces. And this is why we are able to react very quickly in this increase and demand.

It's already increased. And will continue to increase. For the second half, we are moderately optimistic. We believe markets will improve. And this can already be seen with the increase of consolidated shipments, that we had since July, which were 15% higher than June. And as you can see, in the sales slide that I showed you, regarding prices and trends in Brazil Steel have stable prices after a period of consecutive drop. However, we expect a gradual recovery in other markets, because of the growing pressure of the cost of industrial input. And also the increase in demand that we already see in many markets in the world.

Now, I would like to give the floor to Osvaldo Schirmer, who will talk about the financial performance of Gerdau during the quarter. And then I will come back during the Q&A session.

Osvaldo B. Schirmer {BIO 1754610 <GO>}

Good afternoon. Perhaps you could take a look at slide number nine, where there is some information. Andrea and I will try and guide you through this screen.

So, with the support of this big screen, I would like to start with our earnings per segment of business. And then, I will show you the most important operating point in the quarter.

As Andrea has already said, the net income consolidated revenue of sales was BRL6.4 billion, a reduction of BRL567 million over the revenue of the previous quarter, in fact a drop of 8%.

As you can see, in the first part of the year start of the EBITDA. And this drop in the net revenue is due to the drop in prices. And the negative exchange effect generated in dollars.

And this is made up for, or offset by the greater (inaudible) sold during the period. The cost of sales was reduced by BRL579 million. And you can see that on the second bar of the chart, which was (inaudible) reductions from production costs, which we have been following since Third Quarter. In fact, this started already at the end of last year, when the crisis broke out.

So, the gross margin has reached 12.5% in the Second Quarter, above the 11.3% compared to the First Quarter. And you can see that in the top part of the slides. And the gross margin for 11.3% to 12.5%. And EBITDA margin from 8.6 to 9.3. So, we have left in EBITDA 5.9. And we're now at the end of June BRL595, the same level for both.

The EBITDA margin at this time went from BRL8.6 and dropped up to BRL9.3. Lowdown on the chart, also under the (inaudible) same concept of the bridge chart, we see the earnings for the first and the Second Quarter, showing the contribution of each different item to make up these earnings.

So, let's just start off, net income was BRL35 million in the First Quarter. We have had a negative effect of BRL4 million from the EBITDA, which we can see about on the left hand, right hand -- left hand corner. The positive effect on depreciation was BRL32 million. And the loss of actually BRL1 billion, because of the write-off assets, which I will tell you more about later on.

The financial earnings in the period were positive $695 million, which we can see in that bar above, showing a positive exchange variation of BRL547 million. Once again, offset the losses which we had, as we converted revenues generated and bought into Real, because of the greater value of the Real. The consolidated earnings were negative in BRL329 million in the Second Quarter of '09.

If we set aside the losses, because of the write-off of assets net (inaudible) BRL1 billion '08, this becomes BRL796 million. So, in this case, the results would have been positive by

BRL467 million. And if we take the opinion of most of the analysts, it's almost a consensus regarding the operating results of the company around BRL450 million, BRL460 million. The market did not know, nor could it know, nor did we know. But this was what would be caused by the impairment, which I would explain.

So, now please go onto page 10, where we will try and explain this number to you, this BRL1.80 billion. IN a consolidated way, the IFRF criteria allows us to recognize the informant of assets, which stem from several causes, such as the, for example, the write-off of assets, little us of the closing down of plants. And we also see impairment on intangibles.

When you buy a company, generally you would sign a lot of the goodwill to the plant's portfolio. And when the plants are in the reduced number. And we must review this. And also impairment on the goodwill. For the analysts, there is nothing new about this. Whenever you buy a company. And you pay above book price, you have to attribute this access, which we called goodwill, to different (inaudible) of assets, DTF from intangibles etc.

So, what has happened here to us? This BRL1.1 billion, 41% have to do with the impairment of fixed assets, 28% impairment on intangibles. And 22%, the impairments of goodwill. And the balance 9% other costs, which have to do with the closing down of (inaudible). And then, 81% of this write-off of BRL1 billion refers to the segment of specialties for used steel. And the balance 19% is spread out throughout the operations of North America and Latin America.

We must mention that impairment on PP&E in view of the low level of users or temporary closing down. And also impairment of intangibles can be reverted. And account for 69% of the total write-off that we recognized in this quarter. As you all know, losses because of the write-off of assets are items which do not substantially effect cash. But unfortunately, they do have an impact on the bottom nine.

And page 11, production costs. And as we have said in our conference call last quarter, we continue with our efforts to adjust cost structure to the new demand levels. We have reduced by BRL2.4 billion, the total production costs throughout the First Quarter. I would like to mention that alongside the effort to reduce fixed cost, which remained around 24% to 25% of total costs, in spite of the higher level of activities reflected in the increase of production in the First Quarter.

We manage to reduce costs of several raw materials. So that variable costs could also be reduced around BRL1.7 billion, almost BRL2 billion, as you can see on the slide. And also, we have mentioned in our previous conference call. But I would like to repeat that the Gerdau productive process model is focused on mini-mills, which account for 75% of total production.

And this has allowed us greater flexibility. And be able to act much more quickly, when we have to adapt to the new levels of the current scenario. It's important to mention also, that the inventories made up in the previous months, has not yet allowed us to capture the totality of this effort of cost reductions. Therefore, these will probably become clear in the next few months.

Slide 12, let's now have a look at operation per operation in Brazil. We continue to have a net revenue in Brazil of BRL2.4 billion in the Second Quarter, a slight increase, vis-a-vis the First Quarter. The recovery and shipments was of 11%, as you can see in the right hand upper corner, particularly for the domestic market. And this was enough to offset the drop in prices, in fact slight increase of revenues.

And the foreign exchange generated by exports were a total of BRL389 million in the quarter, 16% of the net revenue of the Brazil segment. We must also mention that the comparison of the volume of shipments in June of 2009, the December of 2008, the Brazil operations. So a growth of 34%, which means a monthly average growth of 5%.

This trend, we think, will be confirmed in this ongoing quarter, which Andrea has already pointed out in his presentation, because of the orders that we already have. The Brazil segment has come in with 38% of the consolidated net revenue. Gross margin was 29% in the Second Quarter, a little below the First Quarter of '09, basically for the reasons that I have already explained.

The price to the left, they dropped about 8% of the chunks. And also low profitability of exports. The drop that we can find in gross margin also is reflected in the EBITDA margin in the Second Quarter, which was 24%. Even so, EBITDA generated by the Brazil operations was a total of BRL571 million. And this operation, the Brazilian operation, is the one that accounts more for the generation of consolidated cash.

America, North America, slide number 13, net revenue of Latin America, of North America was $2.1 billion, 12% below that of the First Quarter, basically because of the negative exchange effect and the conversion to Real. However, the net revenue in dollars was stable, about $1 billion, where the drop in prices was offset by the increase of shipments during this period. Shipments increased 15% in North America. And as you can see in the upper right hand corner of the chart, 1.213 million ton, $1 million, not $1 million (inaudible).

The North American segment has contributed with 61%. And with a comparison again, in other words, volume of shipments in June 2009, with December 2008, the North American area has a 16% increase, also a monthly average growth of 2.5%. EBITDA in the Second Quarter was BRL125 million, 42% above the First Quarter. And a marginal 6%.

14, Latin America; for the net revenue of the Latin America segment was BRL798 million in the Second Quarter, 13% below the First Quarter. And this was due, particularly, because of a drop in prices during this time, which got 16% in Reals, even though shipments increased 4%.

Quarter compared to corporate (inaudible), the Latin America segment has contributed with 12% of the consolidated net revenue. Comparing the shipments of June 2009 with December 2008, Latin America segment has grown 39% (inaudible). So, that is to say a monthly average growth of 5.6%. Gross margin, although still negative. And by 2.7%, shows the growth during this period, because of the increased volumes sold, which has led to less fixed cost per ton.

This margin could have been even better, had it not been believed to adjust inventories at market prices, worth almost BRL7 million taken out of the earnings. EBITDA in the Second Quarter was still negative BRL95 million. EBITDA margin, which was minus 15 in the Second Quarter, is minus 12 Second Quarter. Slowly. But surely, we are getting there.

Specialty Steels, 15; the Specialty Steel segment, although growth -- there was a growth of sales 6% in the Second Quarter, the net revenue shows a drop of 16%, vis-a-vis First Quarter of 2009, a total of BRL1.1 billion, which can be seen in the upper right hand corner. And this is because of the lower net revenue per ton. So, which has dropped 21% in Reals. And the exchange effect of the conversion to Real of the American and Spanish operational earnings. And you know, that the Specialty Steel has very important operations in Brazil, Spain and the United States.

In Brazil, the growth of car sales has brought about a recovery, important recovery that I am offsetting the lesser level of sales in the United States. The best sales in Brazil, which historically have margined above the others, have contributed to the recovery of the gross margin, which was 0.2% in the Second Quarter. This margin also could have been better, had it not been the lead (inaudible) inventories at market prices, an amount of approximately BRL46 million, particularly the need to adjust inventories in Spain. In spite of recovery that we can see in the gross margin, the EBITDA in the Second Quarter is still negative by BRL6 billion.

16, the renegotiation of covenants. The market has already been formed. But we may remind you that finally in June, this work which started in March and April. Gerdau approved an approval to make covenants more flexible temporarily, the way we do our financing or funding contracts. This agreement has involved more than 40 financial institutions. And we are very proud that we have a unanimous approval from all our bankers, regarding re-adjusting contractual clauses, a total of almost $4 billion.

The renegotiation agreement will be enforced until the 30 September, 2010. And can be revoked at any moment by the company. So, what we have managed to do, was to bring about a greater flexibility of our covenant, which demanded that our debt would not be more than four times the cash generation. We convinced our bankers that this crisis was unprecedented. And was just a question of the current contract. And although we have a comfortable situation, vis-a-vis our covenants, if markets continued to deteriorate, we could in the future have problems.

So, we got ahead of ourselves by nine months to the possible risk of breaking the covenant. And as we literally were seated on a very good amount of liquidity, the bank has became convinced that this was something very contextual. And temporary. And we agreed to make things more flexible for 12 months.

So, for (inaudible) the due reading of the covenant, instead of four times of those debts, it should be five times over the next debt. And another indicator, which is financial expenses or expenses with interest, with the cabinet before required, it was three times. We managed to get it reduced. So, net expenses with interest to be 2.5 times.

There has been a very good understanding with the financial community regarding our needs, as we have already announced that when we exercise this right -- for the time being, we have a lot of leeway, vis-a-vis the old covenants. But we might have need to bring in the three negotiations. So, we have indicated that costs, which will involve the use of this new flexibility, can vary between $20 million and $60 million, because it would then -- well, they will be used. And for how long?

As we feel more confident regarding the horizons above the forests, we can stop using this, or no longer have to use these more flexible terms. On 30 June, gross debts cash generation ratio was 2.9 times, a substantial leeway for us. But we do things with a preventive attitude. We do not want to run after things after they have been done. Therefore, these indicators are at a very comfortable level, particularly our cash -- regarding our cash level, which I will tell you about now.

17, we have the situation of our indebtedness. The gross debts in June was a total of BRL19 billion as Andrea has already mentioned, approximately $9.7 billion. 15% of this amount was the short term debt. And 85% long term debt. They must mention that in the Second Quarter. There was a reduction of gross debt by BRL3.2 billion.

On the 30 June, gross debt was made up by 18% in Reals, 36% in foreign currency contracted by companies in Brazil. And 46% in different currencies contracted by our subsidiaries abroad. And also, besides the amortization schedule for the year of about BRL2.6 billion, the company will amortize more than BRL4.6 billion, because besides previous pay-offs, we have decided to pre-pay. And by the 31 August, $405 million in amorous deal debt, a higher debt with an interest rate of 10.37% a year.

So, besides the (inaudible) dollars saying that $1.5 billion will be scheduled for the year, we will by the end of the year, amortize $2.3 billion. Amortizing future, more expensive debt. And also replacing debts above one year for others of equal value. But longer terms. So, extending some debts, which would come to you next year, the following year, we are already paying.

Throughout 2010, the scheduled amortization is BRL1.9 billion, which gives us a very comfortable situation. As I have said today, we have more than BRL6 billion available. The average debt term on the 30 June was 5.4 years. And in terms of cost, the debt in Reals was costing 8.5%, in dollars, contractors in Brazil, 6.7%. And exchange variation. And 4.4% for debts taken abroad, by our companies abroad. So, the net debt in June, $6.5 billion, or BRL13 billion. And another comment about liquidity.

Slide 18; regarding liquidity, I have two remarks to make. I have already mentioned the cash position in June, 52% held by companies, Gerdau companies in Brazil and invested in local currency. And the balance was invested in different currencies, particularly the dollar. Gerdau has a very stringent political financial policy, regarding its investments. And we select banks that have a high credit rating.

And also, we try to keep our investments in short-term securities with high liquidity. This cash position of $6.3 billion is taken into consideration with the credit line that we already have. It gives Gerdau a liquidity of about BRL7.4 billion. Besides these lines of credit, the NBS has also approved a new credit billet for Gerdau of BRL1.5 billion to -- for investments in Brazil.

These resources may be used, as we will, to revamp modernize plants in different areas, to expand capacity, investments and logistics. And even energy generation. This is a very open line, a spontaneous line even to a private bank.

Working capital, as you can see in the lower right hand corner of the slide, there's a total of BRL7.5 billion in June 2009, reflecting a very strong contribution, both by the reduction of inventories, which were reduced in BRL2 billion, when compared to March of 2009. And you can see on the curve, the company has been reducing its working capital ever since December. And this is freed up resources to add liquidity to the company.

So, to conclude. And before we go onto Q&A, I would like to repeat a message to you, which has already been mentioned by Andrea. And also through our final remarks. I am referring to the effort which the company is carrying out to adapt its capacity to the new market demand. Costs have been reduced, as well as levels of activity seeking a greater equilibrium and profitable operation.

With a gradual recovery in the different segments and geographies, we think that throughout the next quarters, there will be a recovery of demand, better cash generation and hopefully a greater profitability. Thank you, very much. And now let's go onto our Q&A.

Questions And Answers

Operator

(Operator Instructions).

Our first question comes from Mr. Leonardo Correa from Barclays Capital.

Q - Leonardo Correa {BIO 16441222 <GO>}

Good afternoon, my first question has to do with the U.S. market. Maybe you could quantify your expectation regarding the increase in demand. And more specifically volume during the Third Quarter. And if you could say a few words about the spreads in the United States, the trend in the United States?

A - Andre Gerdau Johannpeter

Good afternoon, this is Andrea. We see some signals. But we do not have a specific figure for a volume trend, for North America for the First Quarter. We see some initial signals.

And they point to probably a recovery. But we cannot talk about trends. Your second question has to do with what?

Q - Leonardo Correa {BIO 16441222 <GO>}

Metal spreads, metal spreads.

A - Andre Gerdau Johannpeter

With an increase in scrap. But we also carried out some price adjustments there, in 68:16. And in (inaudible). And that will probably keep the metal spreads stable from the second to the Third Quarter.

Q - Leonardo Correa {BIO 16441222 <GO>}

One other question please, regarding your working capital. You have been very efficient in terms of reducing your working capital since the beginning of this year. Are you going to need more working capital now, because of a recovery in demand for the second half of the year? What about your working capital situation?

A - Osvaldo B. Schirmer {BIO 1754610 <GO>}

Well, I would love to be able to answer your question, because an increase in working capital would surely mean an increase in demand. But as Andrea said about North America, we do not have concrete expectations. But when we reserved or preserved this level of liquidity, of course we are ready to cope with any needs of working capital. We hope, it does come however -- I cannot be more precise. And I cannot say how much of that will go back to working capital.

Q - Leonardo Correa {BIO 16441222 <GO>}

Thank you.

Operator

Our next question comes from Mr. Felipe Hirai from Merrill Lynch.

Q - Felipe Hirai {BIO 15071781 <GO>}

Good afternoon. My question has to do with the Brazilian market. Could you talk about the possibility of a price increase or a reduction in the discounts achieved in the Brazilian market by the end of 2009 maybe? And second, about cost, could you say what is going on regarding cost in Brazil?

A - Unidentified Speaker

Okay. So about prices first. What we see is the price stability for the second half of 2009. We said already that the world steel reduction, during the first and the Second Quarter is something around 9%. But we understand that prices will remain adjustable at the levels that they are now.

About cost, I don't really have a forecast. But we continue to work to achieve more and more cost reduction in order to keep the company competitive. And the work goes on. But I cannot tell you any more specific percentages, or any specific forecast, because it really depends on demand, pressure, on the part of many pit stops that we use. So, I cannot tell you anything more precise than that.

Q - Felipe Hirai {BIO 15071781 <GO>}

Thank you.

Operator

Next question comes from Rodolfo De Angele, JP Morgan.

Q - Rodolfo De Angele {BIO 1541593 <GO>}

Good afternoon, I have two questions. One I'm not sure you'll be able to answer. It's about the United States. Do you have any detail about the commercial property segment? Do you have any feeling about whether it's improving, are expectations improving regarding this segment, the volume terms?

And then Acominas is my second question. Will you recover capacity there? Could you give us some details please about where demand is coming from. And also, give us an idea of the prices for Acominas. Thank you.

A - Unidentified Speaker

The first part of your question, you're quite right. It's very difficult to estimate what is happening for non-residential real estate. And what will happen in the short-term. As Andrea said, we are seeing strong indicators. Well, not so strong. But positive recovery. And orders in (inaudible) have improved. But we don't know how sustainable this is all going to be.

Acominas, well you're probably referring to our decision of maintaining blast furnace number two. And lots of stoppage, as was announced previously to the market. The largest furnace, more than 3 million tons a year, when that came back into operation again, we would stop the furnace number two. But we decided to keep the second one going as well. So, both will be working.

And as we said this morning to some press interviews, the idea is to keep both furnaces going about 70%, 75%, which is recommended for this level of activity. And we are doing this with mixed feelings. We feel improvement of demands, consultation from international markets. And also a stronger demand from the domestic market.

But it's very simple to calculate things. If this demand, increased demand is confirmed for the equation of cost benefits. And it's best to keep those furnaces going. Therefore, this is why we reviewed our decision to (inaudible) furnace two. And decided to keep it going even though the number one came back. I hope the demand is confirmed. And this will show that we were quite right to keep those working.

Regarding prices for Acominas, Acominas -- the products are both due for international markets. So, we'll have to check what's going to happen in international markets first. It's recovering slowly but surely.

Q - Rodolfo De Angele {BIO 1541593 <GO>}

Thank you.

Operator

Our next question from Mr. Carlos De-Alba from Morgan Stanley.

Q - Carlos De-Alba

Yes, thank you very much. Also, on Acominas, you just went to -- so, you expect -- when do you expect to be able to improve the profitability of the experts volumes from that plant? That will be my question number one. My question number two has to do with the profitability of the Latin American and the Specialty Steel business. Obviously, during the last two quarters, we have had very weak numbers on an EBITDA basis. When do you expect to turn the page. And hopefully have a positive EBITDA in these two segments? Thank you.

A - Unidentified Speaker

Well, the question is about profitability of Acominas. And the second part of the question has to do with the Latin American profitability and Specialty Steels in Brazil. So, I am not very sure whether Specialty Steels Brazil or Latin America as a whole. Could you tell me please? Could you confirm the second part? Repeat the second part of your question please.

Q - Carlos De-Alba

Acominas, Schirmer has just mentioned the trend. And the coal, which was an important pit stop, we had to (inaudible) crisis. And because of these stocks that we held in the First Quarter, it was more hit than cost and profitability. But for the Second Quarter. And because of the better production volume, we will have both finances going.

And because of the inventories, which would be more in keeping. And with reality. And better -- more competitive prices with the coal. And the trend of increased export prices. Do we think Acominas' performance will improve in the Second Quarter? In Latin America, we have had some operations which were badly hit with inventory adjustments, high expensive inventories held in their chains of scrap or ore or coal, or intermediary or end stocks.

So, a lot of the earnings in Latin America were a hit, because of these more expensive inventories, which haven't really been adjusted. So, the outlook for Latin America is also to recover profitability for the second half of the year.

Operator

Our next question comes from Mr. Marcus (inaudible) from ITAU Security.

Q - Unidentified Participant

Good afternoon. Just a follow-up regarding Latin America please. How do you see the recovery of volumes in Latin America? We thought that this region has the weakest recovery in volumes. And also price recovery, because this region depends quite a lot on international prices. And import prices as well. So, how do you see volume and prices for Latin America?

A - Osvaldo B. Schirmer {BIO 1754610 <GO>}

I am going to talk about Latin America. And what's occurred in Latin America, as you see the evolution. It grew quite a lot during the First Quarter, vis-a-vis the Fourth Quarter of 2008. And if you take the whole period, you can see that the growth is 5.6% a month, as I mentioned during my presentation.

We believe this level of growth will be kept. And this is the kind of news that we received from our people. And from the market. And from the most recent meeting. So, I would continue to work with this kind of growth, no major (inaudible). Of course, since the countries are not the same. But as we consider the whole of Latin America. So, in terms of projection models, we will continue between 5% and 6% growth for the quarter on a monthly basis. And Andrea is going to talk about the international prices.

A - Andre Gerdau Johannpeter

About prices, Latin America follows the external influence. And there is a market trend, a (inaudible) market trend, they are going up. And of course, this could impact this region as well. Many countries in Latin America are very much influenced by exports of ore, copper and others. And some commodities are heavy price high can -- this usually follows steel. So, we believe that some increase will happen. I couldn't tell you when. But during the second half or maybe 2010.

Q - Unidentified Participant

A second question regarding a bit more flexible covenant. With the three conditions that you mentioned. The three new conditions, as incredible as it may seem, the one that seems to be closer to a limit is the gross debt reaching $11 billion, which is the CAP, as the gross debt already is almost BRL9 billion.

Because of the appreciation of the Real, we will see something around this level in dollars. So, besides redemption of the $400 million that you mentioned. And that will happen in August -- you said that you will probably exchange this for an extension of growth of (inaudible) debts and cheaper debt, with a longer term, longer maturity. So, as you are very close to this CAP, is there any other initiative that you will take just paying back the debt. And no longer taking long-term debts, in order not to get too close to the CAP?

A - Unidentified Speaker

No, I would like to correct something, allow me please. We have around $9 billion. We are going to lower it, as I said, by $2.3 billion over the year. So it will be slightly higher than $6 billion net debt for the year, around $7 million, $7.5 million in terms of gross debt, which puts us very far from the $11 billion.

$11 billion was a way for us to have this equation in order to make the covenants more successful, because one of the concerns that the bankers had, when we were negotiating the covenants, was that if we were too comfortable regarding indebtedness, this could maybe encourage us to make more critical acquisitions. And this is why we have 11.

In fact, we have lots of room for maneuver there. And with the amortization schedule that we have, this debt will further increase during the year, over the year. And what I mentioned was that over the first and the Second Quarter, we also pre-date debt, that would be maturing in 2010, 2011. And we replaced them for longer term investment. And if there are other opportunities for us to do that, we will be paying keen attention to them. Our idea is not to increase our debt, the idea is to exchange our debt for longer-term debt, provided costs are not negatively hit by that. Thank you.

Operator

Our next question comes from (inaudible) from (inaudible) Bank.

Q - Unidentified Participant

Good afternoon, Andrea, Good afternoon, Schirmer. My first question has to do with cable prices in Brazil for the second half of the year. And with -- we do this exercise with an average 5% increase, which is expected for volumes. Where could you see a price recovery for the Third Quarter, vis-a-vis the Second Quarter? And the second question has to do with what you said about consolidated shipments growing by 16% in July, in a comparison for June. So maybe you could break this out by segment? Thank you, very much.

A - Andre Gerdau Johannpeter

Good afternoon, this is Andrea speaking. We do not believe there will be price changes. We believe prices will remain stable in Brazil, even if we see an increase in demand. So, we do not believe prices will change. About these 16% achieved in July, we do not break out our figures per month. And we thought we should mention these 16%, because it shows a trend for the third and the Fourth Quarter.

However, we are not going to break out for each operation -- that wouldn't be prudent. At the end of the quarter, we will have this. But it wouldn't be prudent to talk about this now. The important thing for us is to show you the trend, a very strong trend. June was already good. And July was even better. And what we wanted to communicate to the market was the trend that we see right now. And not specifically talk about each one of the operations.

A - Osvaldo B. Schirmer {BIO 1754610 <GO>}

If you allow me, I would like to say something. Marcus (inaudible) was talking about a fear of us getting close to $11 million. And I believe some -- if Marcus took the total of our debt in Real. And he calculated this into dollars of today. But in fact, most of our debt is really debt in dollars. And which has nothing to do with the Real going up or down in its value. And we do have a major gap here. So, I just wanted to -- this was just calculated by the people who heard your question. And made the exact calculation that you made Marcus, thank you.

(Operator Instructions).

Operator

Our next question is Russell Peterman from Bradesco.

Q - Unidentified Participant

Good afternoon. My first question has to do with prices in Brazil. What I want to try and understand is why is EBITDA in Brazil, why has it dropped quarter-to-quarter? I imagined it was because of prices. But I think that there was more involved, other factors, I know very complex elements in Brazil.

But I also want to know what the cost of coal for Acominas is, whether this was in the EBITDA there? Because in the First Quarter, Gerdau's earnings in Brazil were badly affected by Acominas. So, I want to know if in the Second Quarter, things have got worse? And the (inaudible) in Brazil is worse, because of Acominas, or was it because of the -- was it a drop in prices here in Brazil?

And also, what about the non-recurrent, what do you have which is non-recurrent, possibly lay-off costs? And as I understand, it's probably also effect from higher costs of inventories in Latin America. So, perhaps you could talk a little bit about that. So, how long will there be a negative impact of coals on Acominas, because Acominas is going to have to renegotiate things. And have to put up with more expensive coal, at least until November.

A - Osvaldo B. Schirmer {BIO 1754610 <GO>}

Lots of questions, lots of questions. But we must admit that things have been a little bit of a surprise when we analyzed our own costs. But in fact there was only one guilty party regarding the difference of EBITDA between the first and Second Quarters. But the important part of the production of Acominas goes to the foreign markets, that means exports. Exports means lower margins, also to keep the operations active.

The philosophy of the company is, always when possible, export. Covering variable costs, even if the margin is almost zero or very low. So, basically it was some price reduction as Andrea has mentioned. We have to sacrifice about 10% to make up price, 10%, 8% lower. So, there is a justification obviously. There has been the lay-off costs and indemnities paid. But if I have to mention anything special, it was in the drop in prices and the export volumes.

Q - Unidentified Participant

Prices in Brazil or export prices?

A - Andre Gerdau Johannpeter

Export, we only export from Brazil. So, when we talk about exports, we're talking about exports from Brazil. And prices in Brazil. So the prices in Brazil.

Q - Unidentified Participant

Prices in Brazil, how much is today's cost buy-in in this quarter?

A - Unidentified Speaker

About 10%.

Q - Unidentified Participant

10%.

A - Unidentified Speaker

Yes. But I told you about that to remember as (inaudible).

Q - Unidentified Participant

I'm sorry, I came in late, I'm sorry. And what about the cost of coal? Will there be -- you'll be feeling these effects until well after June, which was the renegotiation date. Or after June, do you think that the expense of coal, prices will drop?

A - Unidentified Speaker

Well, in Acominas, we have already started renegotiating these prices or these costs. We have been successful with some suppliers. But not with all. Some coal is now coming in at a new cost. And we still have a lot of the old coal. I have no dates. I cannot say exactly when we go, especially onto the new coal. But Acominas, with both furnaces in operation, we would have a higher production scale. This will bring costs down. And make it more competitive. And profitability will improve in the Second Quarter.

Q - Unidentified Participant

Well, I understand. But perhaps you cannot this exactly. How long you will have the coal inventories for? That is not exactly what I want to know. But Acominas was obliged back on track in its negotiations. They are obliged to buy expensive coal until November. This was the negotiations which they carried out. So, you are obliged. And what about (inaudible) steel at the old price?

A - Unidentified Speaker

Well, once again we have several contracts with different suppliers. We are renegotiating them all. We have been doing this since the beginning of last -- since the end of last year, when the crisis started -- broke out. So, I cannot give you the exact date or percentage.

I'm not sure about all the details in Acominas, because our case again, all of this is flowing through the inventories. New material has been used, new coal has been used. And we have a new blend. But I cannot give you the details of volumes or date.

Q - Unidentified Participant

One last question. Well, the fiscal incentive (inaudible) fiscal incentive, have you felt the effect of that in the United States, in the sale of -- long sales in the United States?

A - Andre Gerdau Johannpeter

Well, this is obviously the time that elapses between the announcement of this incentive until things actually starts happening. It takes a long time. You have to carry out (inaudible) engineering. And so it takes a long time to (inaudible) through. So, we have not yet felt this very strongly. There have been some signs. The expectation is that the end of the year. And by next year, we will already be feeling the impact of these kind of incentives and on infrastructure.

Q - Unidentified Participant

Thank you, Andrea.

Operator

Thank you. And we would like to close our Q&A session. And I would like to ask Mr. Andrea to get up for his final remarks.

A - Andre Gerdau Johannpeter

I would like to thank you all for your participation, for your interest and we hope to see you again during -- in the Third Quarter conference call to tell you even better news.

Thank you, very much for your participation. And our team is at your disposal. And of course, we are available at all times to clarify any doubts that you might have about the non-recurring events that happened. And we hope to see you again to give you the results of the Third Quarter.

Operator

Thank you, very much, the Gerdau conference call is closed. Thank you, very much for your participation and have a very good afternoon. Thank you.

Statements in English on this transcript were spoken by an interpreter present on the live call. The interpreter was provided by the Company sponsoring this Event.