Q1 2009 Earnings Call

Company Participants

- Charles Putz, CEO
- Eneas Garcia Diniz, Diretor Executivo
- Luis Martinez, Commercial Director
- Paulo Penido, CFO and IR Officer
- Unidentified Speaker, Unknown

Other Participants

- Carlos de Alba, Analyst
- David Martin, Analyst
- Raphael Biderman, Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. At this time, I would like to welcome everyone to the CSN First Quarter 2009 earnings conference call. Today, we have with us the Company's executive officers.

We would like to inform you that this event is being recorded and all participants will be in a listen-only mode during the Company's presentation. After the Company's remarks are over, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions).

We have simultaneous webcast that may be accessed through CSN's Investor Relations website at www.csn.com.br/ir. The slide presentation maybe downloaded from this website. Please feel free to flip through the slides during the conference call. There will be a replay service for this call on the website.

Before proceeding, let me mention that forward-looking statements are being made under the safe harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of the CSN management on information currently available to the Company. They involve risks, uncertainties and assumptions, because they relate to future events and therefore depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of CSN and could cause results to differ materially from those expressed in forward-looking statements.

Now, I'll turn the conference over to Mr. Paulo Penido who will present CSN's operating and financial highlights on this period. Mr. Penido, you may begin your conference.

Paulo Penido {BIO 4384213 <GO>}

Thank you. Good afternoon, everybody. This is my first conference call in CSN. And first of all, I would like to point out that I am very excited to join CSN, Inc. We will work to keep on improving Company's results and to continue to deliver value for all stakeholders.

Let's take a quick presentation about the Company, starting on page three please. In this page, I would like just to stress net revenue made of BRL2.4 billion, our gross margin of 32.8%. And also our net income that reached BRL369 million. These are very strong results, particularly in the current situation of the industry and the world. So, that's very positive this year, just delivering these results at (inaudible) time.

In addition, I would like to show -- to stress the progression of sales of iron ore. Sales reached 5.4 million tons, which is a new Company's record and grew together 26% of total revenues of the Company in this quarter.

Moving to page four please, we can clearly see the reduction in steel volumes in this quarter which is it was expected. It reflects the reality that we are facing here in Brazil. And we can also see that in steel as I have mentioned in the mining activities of the Company, that is delivering volumes (inaudible) into Asia deposits. The size of the (inaudible) each segment is shown in the graphs below. Steel net revenues reached BRL1.5 billion and mining net revenues reached BRL647 million.

Moving to page five please, checking the sales by product chart, we can see -- we clearly see that the Company delivered (inaudible) mix in the First Quarter of 2009 when comparing to the previous quarter and also going down to the graphs in the north portion of the page, we can see that the Company is preserving a good market share in all segments which is very (inaudible) provide more details about this the markets and that evolution and opportunities in this market.

On page six, we present the cost breakdown. There are two major changes when comparing to the Fourth Quarter of 2008 to the First Quarter of 2008. Number one is that we are not using slabs and hot-rolled products acquired from third-parties. So if we do so which is major cost in the Fourth Quarter. But in the First Quarter we have used it making all the coke that was bought when the market price were around the peak levels (inaudible) cause this distortion in the production cost. So, I would like to (inaudible) we are presenting a difficult quarter for the quarter that reflects reality that we are facing.

On page seven, in terms of gross profit, our 32.8% margin really (inaudible) disappointed what according to what is expected for this quarter. But again, reflects how strong and how solid (inaudible) even in this situation that we are living. And also EBITDA, which showed BRL683 million EBITDA, that represented about 28% EBITDA margin. (inaudible) margin variation. But again (inaudible).

Moving to page eight, the debt amortization. The leverage reduction that is presented in this graph reflects the positive cash impact of (inaudible) Thursday of iron ore that was done back in December. The Company has a very comfortable debt maturity schedule and a very (inaudible) leverage to face this challenge that we are living right now.

Now, moving to page nine, we showed the evolution of the bridge between the result of the Fourth Quarter and the result of the First Quarter.

If we exclude NAMISA positive effect from the results of the First Quarter, you clearly see that the First Quarter came about to be better in terms of net results in comparing to the First Quarter loss/profit [ph] of last year.

In terms of the net debt evolution, it increased from BRL2.4 million to BRL2.8 million. If we check this for the 2008 quarter and compare to the loss adjustment rate for us in the past, you see that this addition of increased expense matched the EBITDA level based on (inaudible) that the Company financed these assets (inaudible) in this quarter.

The evolution of our share price was remarkable in the First Quarter. It was 26% in the (inaudible) and SID, 23% in the ADR. So it's remarkable, given the economic crisis. And it shows the recognition of the market for our business model. With this recent reduction that we're planning to do, we are now open for the Q&A session. Thank you.

Questions And Answers

Operator

The floor is now open for questions. (Operator Instructions). Your first question comes from Carlos de Alba from Morgan Stanley.

Q - Carlos de Alba {BIO 15072819 <GO>}

Good afternoon, Paulo. The questions that I have are for the most part in iron ore. I'd appreciate if you can tell us what the production and sales you're expecting for 2009 and how much of that will come from NAMISA and how much of that will come from Casa de Pedra.

A - Paulo Penido {BIO 4384213 <GO>}

Okay. Eneas is going to answer this.

A - Eneas Garcia Diniz {BIO 15087108 <GO>}

Hi, Carlos, this is Eneas. Only we are (inaudible) our guidance in terms of total sales this year in terms of iron ore of 29 million tons split between (inaudible) and NAMISA.

Q - Carlos de Alba {BIO 15072819 <GO>}

And this is -- the 18 in NAMISA is on 100% basis?

A - Eneas Garcia Diniz {BIO 15087108 <GO>}

Carlos, can you repeat?

Q - Carlos de Alba {BIO 15072819 <GO>}

The number that you gave us for NAMISA, is that on a 100% basis or is just CSN proportion?

A - Eneas Garcia Diniz {BIO 15087108 <GO>}

It's 100%.

Q - Carlos de Alba {BIO 15072819 <GO>}

100%? Okay. So, the 29 million includes 100% of NAMISA, correct?

A - Eneas Garcia Diniz {BIO 15087108 <GO>}

Yes.

Q - Carlos de Alba {BIO 15072819 <GO>}

Okay, excellent. And then you can comment on the iron ore inventory that you have? I think it's 11 million tons. You have kept that for quite a while now. What are you planning on doing with them? Can you sell them. And if so, why you have not been able to sell them or to play them in the market? And how long can you keep those inventories before they start to oxidize or to lose quality?

A - Paulo Penido {BIO 4384213 <GO>}

Carlos, we are maintaining these inventories in our sales cados (inaudible). In terms of what we are planning in the next year, it's something that we are in some ways preparing. And the main point then you have -- and you know that the main bottleneck in our project all the time is our report [ph]. And due to -- we are working in a way that you are going to sell these inventories during the next two years.

Q - Carlos de Alba {BIO 15072819 <GO>}

In the next two years? And the -- we think the 29 guidance for '09, are you contemplating a reduction in these inventories or not yet?

A - Paulo Penido {BIO 4384213 <GO>}

(inaudible) starting the reduction of these inventories' levels -- inventory levels. If you compare the size of the inventories from the fourth part to the first part, there is already 500,000 ton reduction. So, it's -- it takes us, as you just said, some time to reduce it. But it's happening, already happening.

Q - Carlos de Alba {BIO 15072819 <GO>}

Okay. Thank you, Paulo. And could you comment on the margin for the iron ore business in the First Quarter?

A - Paulo Penido {BIO 4384213 <GO>}

Yes, it was 51% precisely.

Q - Carlos de Alba {BIO 15072819 <GO>}

51? I think in the Fourth Quarter, it was around 70%. And why there is a sharp reduction?

A - Paulo Penido {BIO 4384213 <GO>}

There are number of operational reasons. But -- and there were supply market reasons. (inaudible) have been called off, (inaudible) there is further information on this.

Q - Carlos de Alba {BIO 15072819 <GO>}

Okay. We'll do it. Thank you, very much. My final question will be on the prices. I think the realized price was around 51%, which was a little bit below of what we were expecting? That means you have already been given out sort of the 10% provision on pricing. Is that correct?

A - Paulo Penido {BIO 4384213 <GO>}

Carlos, that in some ways reflects our strategy in some ways. But you know that we are using this year a benchmark price of 2008. But we are not receiving that now. In summary, (inaudible) which depend on how it's going to be the negotiation and I believe that this is a fact that we will be (inaudible) linear figures.

Q - Carlos de Alba {BIO 15072819 <GO>}

Thank you, Paulo. Thank you. very much.

A - Paulo Penido {BIO 4384213 <GO>}

Thank you.

Operator

Thank you. your next question comes from David Martin with Deutsche Bank.

Q - David Martin {BIO 5583151 <GO>}

Yes. Thank you. I wanted to ask first just about steel prices, domestic prices in Brazil. I believe you've reported an average hot-rolled coil price of just under BRL2000 per ton in the First Quarter.

Where are price levels today and can you give us some guidance about price changes expected in the Second Quarter? And I guess I would add to that they were some trade reports out this morning about some lower prices on some galvanized products. I just wanted to gauge the potential impact of that on the Second Quarter?

A - Luis Martinez {BIO 7187744 <GO>}

David. Good afternoon. This is Luis Martinez speaking. Talking about prices, we have to take into account that in the First Quarter, we have just 6% lower than Fourth Quarter. The second year quarter we are gaining -- there is no way out for us, we have to follow the competition. But we have to offer to the market something like 10% lower comparing these prices in March.

In hot-dip galvanizing, we are not interested in lowering so much the price. In fact, we are working customer-by-customer trying to get as much as possible and another very important point that we have to emphasize we are much more focused in now doing this right now. So, in market galvanize, we are trying to get better margins. But in general 10% more.

Just to give you some nutshell [ph] about those hot-rolled coils, we are working in the range of considering US dollars and real exchange rate in the range of 2.1, we are now in the range of 880 or something like this in hot -- hot-rolled coils.

It means the premium over imported plant [ph] in Brazil something like 40%. That's one of the reasons we have to keep a better distance between imported materials. And now a very important point to be considered. The last year in Brazil, we basically bought material represented in something like 70% to 80% of total market.

So, we are completely interested in getting back these volumes and also obviously recovering our market share in the local market. In the First Quarter, I think it has been successful so far. We are in a range of 80% to local markets and we are planning to have to the end of this year's minimal 85%.

Q - David Martin {BIO 5583151 <GO>}

Okay. And then also can you comment on business activity in volumes in the first month and a half of the Second Quarter? Is it safe for us to assume that volumes will be pretty consistent versus the First Quarter?

A - Paulo Penido {BIO 4384213 <GO>}

Yes, okay. In the First Quarter, we closed in the range of 600,000 metric tons. We are planning to have at least 40% to 50% higher in the Second Quarter. And in the first -- in the third and Fourth Quarters since all the value chains are completely free of the inventories and all the government incentives will be in place, we are planning to almost to recover in the range of 30% in the third and fourth part. Our guidance in terms of volumes for this year will be something like 4 million tons a year. That's nearly 85% of local market.

Q - David Martin {BIO 5583151 <GO>}

Okay, that's helpful. Thank you.

A - Paulo Penido {BIO 4384213 <GO>}

Okay, thank you.

Operator

(Operator Instructions). Your next question comes from (inaudible).

Q - Unidentified Participant

Hello. Good afternoon, everybody. Just a follow-up question with Marceles [ph] from the Portuguese conference call. I would like to know the average discount that you're giving in the domestic market on the steel prices versus the March price. You've mentioned in the previous call that, prices should be 10% lower than the First Quarter average. But what would be prices like in June when you compare to March prices?

A - Paulo Penido {BIO 4384213 <GO>}

Hello?

Operator

Yes, Mr. Paulo.

A - Paulo Penido {BIO 4384213 <GO>}

Yes, speaking.

Operator

Were you able to hear the question, sir.

A - Luis Martinez {BIO 7187744 <GO>}

Yes, can you please ask him to repeat the question?

Q - Unidentified Participant

Okay. I'm here, yes.

(multiple speakers)

A - Luis Martinez {BIO 7187744 <GO>}

Marceles [ph], sorry we are in the mute mode, sorry.

Q - Unidentified Participant

No problem.

A - Luis Martinez {BIO 7187744 <GO>}

Marceles [ph], I already (inaudible). Just comparing the First Quarter this year, we have been on average priced 6% lower than last quarter last year due to basically we keep zinc plate prices stable comparing with last quarter. But in the First Quarter, in hot-rolled price, cold rolled and partly galvanized, we discounted something like 13 to 16% in this product.

In the second product, just to follow the competition, we are going to have on top of our discount in the first product 10% more, including tin plate. So basically you are going to have 20% in hot rolled, cold rolled and partly galvanized.

But I would like to emphasize, as I mentioned in the morning conference, that we are going to do this price analysis. That's something like tailor-made, because we have to take it for granted that some customers at this moment, they are not only interested in prices. Most of the customers now are interested to have daily shipments. So, they are going to have no inventories.

So, we -- if I were to charge a premium for this, I believe that it's reasonable to charge premium of 25 to 28 or maybe 30% over imported lands [ph] in Brazil at this moment. But as you know, CSN is really prepared to fight in the market. We are not interested in that market share in the market. And our total focus would be in the local market.

Q - Unidentified Participant

Okay, Martinez. And the discounts will be effective from which month onwards?

A - Luis Martinez {BIO 7187744 <GO>}

April.

Q - Unidentified Participant

April, okay, great. Second question is regarding the mining business. We saw recently that CSN signed an agreement with Vale regarding all the pending issues that they had between themselves in the Justice. And one of the outcomes of the deal was that CSN will be buying or acquire pellets -- 3 million tons of pellets from 2009 to 2014.

So, I just would like to understand the rationale behind this deal on the pallet business and also if this means that the CapEx on NAMISA for the palletizing plant will not happen until 2014.

A - Charles Putz {BIO 7407612 <GO>}

Hi, Mark. This is Charles Putz, CEO of NAMISA, answering second part of your question. No, we cannot confirm at this moment that the investment for the palletizing plant will not occur this year. For sure, not the entire investment will occur. But at this moment, currently we do not have any (inaudible) in our investments being forecasted. So we have some investments in the palletizing process forecast for this year and they remain so far.

Q - Unidentified Participant

Okay. Last question to Paulo on the CapEx. We saw this quarter a quite sizeable investment on the long steel plants, about BRL100 million. And I would say a smaller number on the standard [ph] business, would just like to have an overview on this on how this business are evolving maybe on (inaudible) as well, as you have an expectation of producing money in 1 million pounds this year already. Do you guys still confirm your guidance? Is this still achievable and how the long steel expansion is going? Thank you.

A - Paulo Penido {BIO 4384213 <GO>}

Okay. Those -- from that business and the long steel business, construction is under schedule. We are -- there is evolution in this area. Just today, we have started (inaudible) from our plant. This is first (inaudible) and we are just starting off. We may change a little bit the schedule for the long business that is CSN's target.

But I would like to stress that our investment probably from this year is likely to be around $1 billion. This is not the final number. There can be a change depending on the market situation at the end of the year. But we have been asked to finalize the adjustments that we already talked about and that are under construction (inaudible).

Operator

Thank you. (Operator Instructions). Your next question comes from Raphael Biderman with Bradesco.

Q - Raphael Biderman {BIO 1529743 <GO>}

Hello. My question is regarding if you can talk a little bit about how are you seeing the iron ore market, how are you seeing with this crisis now (inaudible) if you have felt reduction in orders and if you are already selling to the Japanese partners in NAMISA and how is that evolving?

Also, if you could comment in addition of how your exports (inaudible) are they improving, how much they are improving. (inaudible) to 40 to 50% increase in sales into Q? Do these exports improve a lot or this is mostly the improvements in domestic sales?

A - Charles Putz {BIO 7407612 <GO>}

Hi, Raphael, this is Charles Putz from NAMISA answering the first part of your question. You were asking if we're already to NAMISA's partners. And the answer is yes. We have last date [ph] agreements with them. And they are being normally fulfilled. So we are exporting to our shareholders. And in addition to that, we are exporting to some other long-term partners we have and we are starting to play a normal role in the market and that is to both for NAMISA and for CSN for Casa de Pedra (inaudible).

Q - Raphael Biderman {BIO 1529743 <GO>}

I am sorry, the line was blurred. So, you are exporting [ph] to your existing shareholders already.

A - Charles Putz {BIO 7407612 <GO>}

Correct, we are.

Q - Raphael Biderman {BIO 1529743 <GO>}

Okay.

A - Unidentified Speaker

(inaudible). We during the First Quarter, we have just a small amount of support mainly in tin plate that is the best product, that it remains to give another very nice good margin and we are not exporting another product because its margin is not good for us.

We are waiting for market improvement to start again. We had (inaudible). There is some improvement in Asia. There some emerging markets are again buying. Other markets that future (inaudible) of these evaluation in these currency that they may export very, very low prices of generating international market and we think this decision [ph] are appearing and market is getting again, good price.

This week, this recent week's prices improvement of around, you see, 10%, equal to 10% around $40 per ton hot-rolled coils. Hot-rolled coils is again with a price of having another 150 to forming (inaudible) good news. We are stretch the market maybe very strongly again disputed market. But only when the business is profitable for us.

Q - Raphael Biderman {BIO 1529743 <GO>}

So, you are exporting only tin plates, the other products you are not carrying margins?

A - Unidentified Speaker

So far the process, that we had a notes are not presenting good margin for us. So, we make -- we make some export. But not while our export (inaudible) but we expand material raw material for our affiliate in Europe (inaudible). But yes, like raw materials for that.

Q - Raphael Biderman {BIO 1529743 <GO>}

(inaudible) amazing for me because your cost use to be extremely lower than everyone else in the world. And I wonder why you are not having margin basically because of cold and coil cost I suppose?

A - Paulo Penido {BIO 4384213 <GO>}

Let me say secondly considering our cost, we will be able to make some small margins. But we are not looking for small margins. So, the margins (inaudible) but not where we are looking for. (inaudible) we have a trend that the market will improve and we had enough time to (inaudible).

Q - Raphael Biderman {BIO 1529743 <GO>}

And on coal, you guys have mine coal in the spot market or you continue to buy in the normal way which is your coal price will only change once a year when there is a (inaudible) decisions in June?

Are you guys are -- the situation is so different and that you guys are not doing like that anymore and are buying in the market -- in the spot market coal, how is it happening.

A - Paulo Penido {BIO 4384213 <GO>}

So, at the same that we are negotiating with our contract suppliers, we are making some acquisitions in the spot market.

Q - Raphael Biderman {BIO 1529743 <GO>}

Okay. And one last question, just one follow-up on that question in the other conference call in Portuguese. Was there any maybe recurring costs in your (inaudible) base, because the control I mean already made the calculation and effect of the high coke costs that looking at therefore cost of goods sold throughout depreciation of the controlling Company and the consolidated looking at valuation quarter-over-quarter, there was something (inaudible) the cash cost of goods sold of the controlling Company Q-on-Q and of the consolidated Company do not fail at all while revenues in the revenue scale.

So, I mean I know there is effect of the coke cost but is in fact the controlling Company cost of goods sold which actually (inaudible) last in the audit [ph] could have fallen considering that on sales and that on the consolidated Company even fell at all, it has been flat. (inaudible) any initial regarding cost of the (inaudible).

A - Paulo Penido {BIO 4384213 <GO>}

We are going down to a level that (inaudible) please scroll our Investor Relations team (inaudible) and you can clarify for you the details on the different variances that we have on all these issues, please.

Q - Raphael Biderman {BIO 1529743 <GO>}

Got you. Okay, Paulo. Thank you, very much. And I'll go to (inaudible) your new house, okay.

A - Paulo Penido {BIO 4384213 <GO>}

Thank you, very much. Thanks.

Operator

Thank you. (Operator Instructions). There are no further questions. I will now turn the conference over to Mr. Paulo Penido for closing remarks. Please go ahead, sir.

A - Paulo Penido {BIO 4384213 <GO>}

Thank you. Just to disclose that our Investor Relations team is available for any further questions that you may have. And see you next time. Thanks.

Operator

Thank you. This concludes today's CSN's First Quarter 2009 earnings conference call. You may now disconnect your line and have a great day.