

## Q2 2017 Earnings Call

### Company Participants

- Guilherme Machado, Executive Investor Relations Manager

### Other Participants

- Alexandre Falcao, Analyst
- Stephen Trent, Analyst
- Victor Mizusaki, Analyst

## MANAGEMENT DISCUSSION SECTION

### Operator

Good afternoon, ladies and gentlemen. At this time, we would like to welcome everyone to Rumo's Second Quarter of 2017 Results Conference Call. Today with us, we have Mr. Júlio Fontana, CEO and Investor Relations Officer; and Mr. Guilherme Machado, Investor Relations Manager. We would like to inform you that this event is recorded, and all participants will be in a listen-only mode during the company's presentation. After Rumo's remarks, there will be a question-and-answer session for industry analysts. At that time, further instructions will be given. The audio and slideshow of this presentation are available through the live webcast at [ir.rumolog.com](http://ir.rumolog.com). The slides can also be downloaded from the webcast platform.

Before proceeding, let me mention that forward-looking statements will be made under the Safe Harbor of the Securities Litigation Reform Act of 1996 (sic) [Private Securities Litigation Reform Act of 1995]. Forward-looking statements are based on the beliefs and assumptions of Rumo's management and 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 Rumo and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I'll turn the conference over to Mr. Guilherme Machado. Sir, you may begin your conference.

### Guilherme Machado {BIO 17920567 <GO>}

Good afternoon, everyone, and thank you all for joining the second quarter 2017 conference call for Rumo SA. I'd like to start by reminding you that at the end of 2016 we concluded the reverse merger process of Rumo Logística by Rumo SA, which is the

current denomination of América Latina Logística SA. So we're now presenting here Rumo SA pro forma results considering the accumulated results of Rumo Logística prior to the merging for a better comparison purpose.

Well, in a broader view, this quarter we recorded a significant growth for EBITDA, mainly reflecting higher transportation capacity as a function of our investment program leading to a transported volume growth and higher operational efficiency. So let's start with chart number 3 with Rumo's consolidated results. Rumo presented a good operational performance in this quarter. We reached volume transported of approximately 12 billion RTK, 14% higher, leveraged by increasing capacity related to our investment plan.

The second quarter is historically dedicated to soybean transportation. However, this year we saw a worse commercialization scenario for the grain due to price reduction in the international market. Soybean exports were strong until May when producers decided to store part of the production and await for a better pricing scenario. The trading companies that we serve in the North Operation, our main corridor, decided to anticipate the corn second crop exports to June. As you know, corn transportation usually takes place in the third quarter. These unusual movements generated a complexity to our operations, demanding an additional effort from countryside and port terminals until the full conclusion of replacement of products. However, we were able to adapt our operation, executing the change between soybean and corn, maximizing our volumes transported of both cargoes. Regarding the port loading volume at our terminals in Santos Port, they went down by 6% in the second Q 2017, reflecting the slower start of sugar transportation in this year.

So now let's move on to chart number 4 where we can see the company's consolidated financial performance. The financial performance was benefited from higher volumes transported. Consolidated net revenue in the quarter was up 9.4% to BRL 1.5 billion due to higher port loading and transportation yields. EBITDA climbed 24% from second Q 2016, reflecting efficiency gains achieved through our investment and record soybean and corn crops. Variable costs had a smaller growth when compared to the transportation volume expansion. And fixed costs, excluding depreciation and amortization, had a reduction of 4.4% year-over-year. EBITDA margin also expanded, reaching 49% in this quarter. Our broad net debt came to BRL 9.4 billion in the second Q 2017 while our leverage was reduced it to 4.3 times broad net debt to EBITDA.

Moving onto chart number 5, we can see the breakdown of our business units starting with the North Operation performance. Total volumes transported by North Operation in the second Q 2017 was 17% higher than second Q 2016, reaching 8.3 billion RTK, reflecting higher demand for grain transportation and our increased transportation capacity. Net revenue grew 12% to BRL 1.1 billion in second Q 2017 mainly due to higher volumes transported of agriculture products. The increase in volume transported of industrial products, mainly few, also contributed to the result since strong corn and soybean crops boosted agriculture machinery demand in producing areas, especially in the Mato Grosso state. On top of this, we had higher average yields that also helped achieve the results. Thus, North Operation EBITDA was up 17%, reaching BRL 644 million in the second Q 2017. Higher operational efficiency as a result of the execution of our CapEx plan make it

possible for our operations to receive a larger grain volume and contributed to lower unit cost leading to EBITDA margin expansion.

On the next chart, we can see the increase in the share of transported cargoes by our railway in the Port of Santos. As we can see in the first graph, during the second quarter the average price of soybean in Mato Grosso had a strong reduction impacted by a worse commercialization condition in the international market. This scenario led producers to store part of their cargo in mid-May, waiting better pricing condition. Therefore, the trading company anticipated exports of the second corn of crop to June, which usually happens in the third quarter. Even with the unusual scenario, we were able to adapt our operations to receive larger volumes of both grains. As a result, our market share in grain transportation to the Port of Santos has increased from 40% in the second Q 2016 to 47% in the second Q 2017. This growth in share happened even with the 11% growth in the total grain transportation to the port which demonstrates our gains in capacity due to the execution of our investment plan and consolidation of our commercial strategy.

Moving on to chart number 7, we now present our South Operation performance. Total volumes transport by the South Operation in the second Q 2017 reached 3.5 billion RTK. The 9.4% increase year-over-year was mainly driven by higher soybean and sugar volumes transported and a significant increase in the transportation of industrial products. Similar to the North Operation, the larger capacity generated by an investment in an asset (09:21), combined with a record soybean profit, allowed us to increase our share in the ports of Paranaguá in the Paraná state; and São Francisco do Sul, Santa Catarina state, leading to a significant expansion in our volumes transported in the period. Industrial volume growth resulted mainly from the startup of Klabin's plant in Ortigueira region in the Paraná state in May 2016 as well as from the increased transportation in the construction segment. Net revenue was up by 10% to BRL 333 million in the second Q 2017, driven by both higher average yields and higher volumes transported. As a consequence, the South Operation EBITDA almost doubled in comparison to the second Q 2016, reaching BRL 95 million in the second Q 2017.

Moving on to the next chart, we present our Container Operation performance. Total volume of containers transported in the second Q 2017 decreased nearly 9% year-on-year due to the decision that we have been communicating to the market of not operating non-profitable routes especially in the Mercosur and the Rio Grande do Sul corridors as well as lower demand for refrigerated products transportation. As a consequence of lower volumes, EBITDA of Container Operation was negative BRL 6 million in this quarter.

Moving on, let's talk about the consolidated results of the company, again starting with the indebtedness position. The broad net debt increased almost 4% from BRL 9.1 billion at the end of the first Q 2017 to BRL 9.4 billion as of June 31, 2017 mainly due to the cash consumption related to the implementation of our investment plan, partially offset by the decrease of gross debt as a result of net amortizations in the period. Leverage measured by the broad net debt to EBITDA ratio was reduced to 4.3 times this quarter. This downward trend in leverage may further increase in the next quarter as a result that we're going to have the replacement of quarters with lower EBITDA performance in 2016, especially the third and fourth quarter, for the respective periods in 2017 where as we forecast the higher transportation volumes.

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Moving on to slide number 10, we can see the consolidated financial results and cash flow. The financial result in the second Q 2017 was net expense of BRL 433 million, 7% higher from the same period last year, mainly due to the process of debt restructuring and the internalization of Senior Notes 2024 issued in February 2017. These effects were partially offset by lower expenditures with leasing and real estate receivables certificates as a result of the amortization of these instruments during period without new funding being raised combined with the drop in interest rates in the period. In addition, we had an increasing yield of financial investment due to a higher average cash position in the period.

Moving on to the next chart, we're going to present operational and financial performance indicators. On chart number 11, we can see the historical evolution of Rumo's operating and financial performance indicators. The unitary variable cost is the variable rail operation cost per RTK produced. This ratio decreased 2%, reflecting higher efficiency of company's assets, especially lower fuel consumption of locomotives. Likewise, we present the fixed cost added to SG&A expenses less depreciation per RTK produced. Such indicator improved significantly by 14% as a consequence of the reductions in cost and expenses achieved during last year, partially offset by inflation in the period.

The operating ratio in this quarter show an improvement of 7% compared to second quarter of 2016, reaching 71% as a result of the improvement of variable and fixed cost as mentioned above. Our diesel consumption measured in liters per GTK, which is the gross tonne including load and weight, improved 8% mainly due to lower consumption of the new locomotives. This indicator was also benefited by the higher volume of grains transported in North Operation where there is a lower average fuel consumption when compared to the sugar flows from São Paulo.

Now specifically referring to the North Operation, the grain transportation from Rondonópolis to Santos route, when we analyzed average car load per day, we can observe the improvement from higher volumes of grains originated in the Mato Grosso and also due to operations more efficient in our terminals. Important to mention that the renewal of our fleet, replacing railcars with lower capacity per railcars with 90 tonnes capacity, allowed to transport the same volume with few railcars loaded. Transit time in the second Q 2017 remained in line with the second Q 2016 since scheduled works related to our investment plans were carried out in several sections of the operation. The cycle time of railcars in the Rondonópolis/Santos route in second Q 2017 dropped 6% compared to the second Q 2016, reflecting an increase in the efficiency of the operations of terminals in Santos and also in the countryside.

Looking to the indicators of the South Operation, from routes of the North Paraná to the Port of Paranaguá, we can see that, as we mentioned in the North Operation, the renewal of the fleet with the inclusion of railcars with larger capacity benefited the cycle time, reflecting better operational results at terminals, offsetting the increase in transit time resulting from scheduled work in (16:31).

Moving on, let's discuss the most recent market projections on chart number 12. Here we present the most recent Agroconsult projections for soybean and corn production in Brazil and in the state of Mato Grosso. As you know, 70% of our total volume is represented by

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grain transportation. We can see that the projections for the second half are positive, with the expectation of increasing grains exported over the period. The corn harvest is advancing and indicate a record volume for the this year's crop which maintains our confidence in the implementation of the program for this year.

In addition to that, with price of soybean improving since July, there is expectation that the grain stored by producers will be exported at the end of the year when corn exports are finishing, opening spacing for terminals for exchange of products. Therefore, it's estimated a 20% increase in the soybean production in Brazil; with the crops of Mato Grosso, our main market growing 17%. For corn, a 45% increase in the Brazilian grain production is projected; while Mato Grosso, the increase is even more significant, reaching almost 30 million tonnes, 70% higher than the previous growth.

Moving on the presentation. Let's talk about our guidance for 2017 on chart number 13. As we presented, the market figures indicate that we have a very strong crop for the year. And on top of that, the investment which resulted in a higher capacity and operational efficiency maintain our confidence in increasing results in line with our long-term plan. And therefore, we reinforced our guidance for 2017. We said that in the range of BRL 2.6 billion to BRL 2.8 billion, and CapEx expenditures in total between BRL 2 billion to BRL 2.2 billion.

With this, I finish the presentation. I'm here with Júlio Fontana, Rumo's CEO and IRO; and with our financial team to help in the Q&A section. And I would like to thank you all for joining us in this conference call.

## Q&A

### Operator

Thank you. We will now begin the question-and-answer session for investors and analysts. Our first question comes from Stephen Trent with Citigroup.

### Q - Stephen Trent {BIO 5581382 <GO>}

Yes. Good afternoon, gentlemen. Thanks very much for taking my questions and for the presentation. Just two from me for now. The first is I generally appreciate the color on merging Rumo Logística with Rumo company earlier this few months ago. Do you see any possibility that you guys could consolidate the operational structure between Rumo and Cosan Logística?

### A - Guilherme Machado {BIO 17920567 <GO>}

Hi, Stephen. It's Guilherme. In practical terms, and being very direct to your point, this is much more a shareholder discussion than a management discussion, okay? It's something that do not take part of the executives' time on a daily basis. So I think that in this matter, Cosan Limited has an agenda to simplify their structure. But it's something that, in our level here, we have a low visibility so far.

## **Q - Stephen Trent** {BIO 5581382 <GO>}

Okay. That's fair enough and appreciate the color. And actually just two more, if I may. One, if there's any chance I could ask you for an update regarding expectations around BNDES funding. And two, I was also curious in terms of the management level if you guys have any plans to replace José Cezário or if you're comfortable with the way that the structure is currently operating. Thank you.

## **A - Guilherme Machado** {BIO 17920567 <GO>}

All right. So regarding BNDES, we are discussing with these guys and we have been updating you through our conference calls and the earnings calls. We have provided all the detailed information necessary to move on with our request. They have already pre-approved data as you have followed. And with this provided information, it's now an internal process from BNDES to have their credit analysis, and there is nothing I would say pending from our side to have the completion of their analysis. So it's a total internal process that we're supporting them and we hope to have a positive feedback sooner than later.

Regarding the replacement of Cezário as CFO, we have in our structure and together with me in this call, (23:04) which is the Director for Treasury and Planning; and (23:09) who is the Controlling and also Internal Reports Director. Now we report to Júlio. It's a structure that do not provide any disruption to all the subjects that were being taken in place with Cezário and it's something that is designed and working well at this point in time.

## **Q - Stephen Trent** {BIO 5581382 <GO>}

Okay. Very helpful and thanks for the color.

## **Operator**

The next question comes from (23:45).

Hi. Thanks for the opportunity. Congratulations on the results. My first question, just following-up on the BNDES financing update. First question is if there's any credit committee dates that has been established. Just trying to get, in terms of the timing, a more precise expectation. Second question is just regarding the - when I look at the South Operation's margin improvement, that's been significant. What is the achievable margin you think in the business plan period? Can we expect it to approach the North Operation's margins or if there's a structural issue that prevents it from getting to that level of margins? And the last question is just really on the Container Operations. What is kind of the expectation, what is the outlook, and when can we see that turning positive in terms of EBITDA contribution? Thanks.

Okay. This is (24:55) speaking. Thanks for the question. And regarding BNDES, as Guilherme just mentioned we kind of provided all sort of information that have new (25:06) for us as of now. There may be some new follow-up questions that may be coming in the upcoming days, but we don't believe in that. But in case it comes we'll be

able to reply. But taking that in consideration, we have not received from BNDES firm forecast in terms of approval from the credit committee from them. But what we have from them is that in few months we will be able to sign the agreement. So this is what we are going for.

#### **A - Guilherme Machado** {BIO 17920567 <GO>}

And addressing the South and Container question. So in the South we saw a very important improvement in this quarter mainly - it's totally connected with the investment that we're performing and improving the efficiency of this business line. So we are somehow avoiding accidents in these specific segments which helps to improve the process in the terminals that we operate, and certainly the availability of our assets for transportation. And it's an improvement that we see that'll take place throughout the investment plan if the margins will arrive, but we have a target to move on to a level between 20% to 30% with what we have been designing in our long-term plan.

And lastly, about the container operation. This is almost a turnaround processing size, the turnaround of Rumo. They have finished some contracts that provided no profitable margins to the business. So we're starting to create the client bases in the Container, and that is something that we see with good potential over time and a point that we see additional capacity being created in the business. So it's the status that we see today with good prospects for the future.

#### **Q - Operator**

Thank you very much.

#### **A - Guilherme Machado** {BIO 17920567 <GO>}

Welcome.

#### **Operator**

Our next question comes from Alexandre Falcao with HSBC.

#### **Q - Alexandre Falcao** {BIO 5515455 <GO>}

Thanks for the question. My question is regarding the whole season or the whole harvesting season for this year. I have two questions. First, what do you expect as a consolidated basis to be your market share versus trucks by the end of this harvesting season? And second, taking a look on the dynamics of second crop of corn and the storage that we see and sort of reports that we're going to see people leaning to sell their crops, is there any chance that we're going to see a third quarter that could be at least slower than we expected or you guys are full in capacity and that's it? Thank you.

#### **A - Guilherme Machado** {BIO 17920567 <GO>}

Well Falcao, we're seeing a very positive second half of 2017, taking to consideration the performance of the company in July and the prospects for the harvest of corn and soybean until the end of the year. As Júlio mentioned in the Portuguese conference call,

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we expect to haul corn until December. And then we believe that the soybean that is stored by the producers will sooner or later come to export as well, so then operate at some point both projects and the increasing capacity will be possible for us to move these two cargoes. We have expectations that approximately 16 million tonnes of soybeans in our storage as of now, and at some point this volume should be hauled to the ports for export, due to the cargo dedicated for exports as we see.

So in terms of market share, we have been improving as a function of the investment. It's tough to give a precise number. We believe that is going to be the railroad. And, I mean, on top of that Rumo is taking the total grain exported through Santos which is our main port that we operate. We estimate it'll be more than half of the total, I mean, between 50% to 50-plus percent. So it's tough to give away a specific number, but as a function of an increasing capacity we believe that we can expand that figure.

**Q - Alexandre Falcao** {BIO 5515455 <GO>}

That's very helpful. Thank you.

## Operator

The next question comes from Victor Mizusaki with Bradesco BBI.

**Q - Victor Mizusaki** {BIO 4087162 <GO>}

Hi. I have a quick question here. When we take a look on your KPIs, we can see consistent improvement over time. Is there anything that you can share with us related to, for example, target operational ratio that you can achieve in the coming years or maybe something related to fuel consumption?

**A - Guilherme Machado** {BIO 17920567 <GO>}

Hi, Victor. Sure. As a function of the investment plan, that's what we're performing, acquisition of new locomotives, acquisition of new railcars, and also the improvements in the permanent weight, we're already achieving these results as you have highlighted, the sustainable performance. So operating ratio in our strategic business plan will reduce over time from the level of 70% that we're seeing today to something around 60% as a function of cost reductions and cost dilution that we have. And also fuel consumption, we have internal targets to reduce that over time. We have faced fuel reductions from 2015 to 2016 and 2016 to 2017 of approximately 5%. So the idea is to keep this trend as we have the conclusion of the investment.

**Q - Victor Mizusaki** {BIO 4087162 <GO>}

Okay. So basically, Guilherme, you were saying that, for example, if you think about operating ratio, 60% is something that you can achieve like in five years, three to five years?

**A - Guilherme Machado** {BIO 17920567 <GO>}

Yes.



**Q - Victor Mizusaki** {BIO 4087162 <GO>}

Okay. Thank you.

**A - Guilherme Machado** {BIO 17920567 <GO>}

You're welcome.

**Operator**

This concludes today's question-and-answer session. I'd like to invite Mr. Guilherme Machado to proceed with his closing statements. Please go ahead, sir.

**A - Guilherme Machado** {BIO 17920567 <GO>}

Well I'd like to thank you all for joining us for this earnings call. And we're available and hope certainly we can talk in the next conference call. Bye-bye.

**Operator**

This concludes Rumo's audio conference for today. Thank you very much for your participation. Have a good day and thank you for using Chorus Call.

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