

Y 2016 Earnings Call

Company Participants

- Andre Gerdau Johannpeter, President & Chief Executive Officer
- Harley Lorentz Scardoelli, Executive Finance Vice President and Chief Financial Officer

Other Participants

- Bruno Giardino, Analyst
- Carlos de Alba, Analyst
- Gabrielle Curtis, Analyst
- Ivano Westin, Analyst
- Karel Luketic, Analyst
- Leonardo Correa, Analyst
- Marcos Assumpcao, Analyst
- Milton Sullyvan, Analyst
- Thiago Lofiego, Analyst
- Thiago Ojea, Analyst

Presentation

Operator

Good afternoon, and welcome to Gerdau's Conference Call to discuss the Results of the Fourth Quarter and Full Year of 2016. At this time, all participants will be on listen-only mode during the company's presentation. And after the company's remarks, we will initiate the question-and-answer session. (Operator Instructions)

We would like to emphasize that any forward-looking statements that might be made during this conference call related to Gerdau's business outlook, projections, and financial and operating goals are mere assumptions based on management's expectations related to the future of the company. Even though Gerdau believes that its comments are based on reasonable assumptions, there is no guarantee that future events will not affect this evaluation.

Here today are Mr. Andre Gerdau Johannpeter, Director, President and CEO; and Harley Scardoelli, Executive Finance Vice President. With no further ado, I would like to give the floor to Mr. Andre Gerdau Johannpeter. You may proceed, sir.

Andre Gerdau Johannpeter

Thank you. Good afternoon, everyone, and welcome to this earnings conference call to discuss Gerdau's results. We will begin our analysis with an overview of the world steel industry, followed by comments on Gerdau's performance in 2016. Further on, we will elaborate on the investments during the period.

It is important to mention that we will analyze the performance of the consolidated results for 2016 and the fourth quarter of 2016. After those comments, Harley Scardoelli will elaborate on Gerdau's financial performance, and at the end we will be available to take your questions.

For those of you who follow us on the web, I'm on slide two that refers to the world steel landscape. According to the World Steel Association, the world steel production totaled 1.6 billion tons in 2016, up by 0.8% vis-a-vis 2015. This growth was mainly driven by an increase in steel production coming from the Middle East and Asia. The highest growth came from India which posted an increase of 1.2% in the period, and China had an evolution of 1.2% [ph] in the period, and the country accounted with 49.6% of the entire production 808 million tons. However, there was a downturn in steel production in Europe, the Americas and Africa. The most significant decrease was in Brazil that posted 9.2 reduction in steel production in 2016.

Now if we look at world installed capacity utilization, it stood at 69.3%, very similar to the figures of last year which was 69.7%. World installed overcapacity is around 800 million tons, and it still remains a matter of concern for the industry.

Now looking at 2017, it is expected that the world steel consumption should grow 0.5% mainly in emerging and developing economies, where consumption should grow 4%, excluding China. In China, consumption of steel should drop 2% in 2017.

In Brazil, we expect a 3.5% increase in steel consumption in 2017, according to Instituto Aço Brasil. The outlook indicates that a recovery in steel demand should start in the second half of the year. The first six months of 2017 should perform at the same levels of 2016.

In North America, steel consumption should grow 3% in 2017. The industry should benefit from the growth in demand coming from non-residential construction and the recovery of demand from the industrial sector. There is high expectation around the development of infrastructure projects announced by the Trump administration during his presidential campaign.

Other factors that could impact Gerdau's performance in the US is the current analysis being conducted by the US Department of Commerce and the application of anti-dumping tariff levied on rebar imports coming from Turkey, Japan and Taiwan, and also countervailing measures on rebar imports from Turkey. The anti-dumping investigation should be concluded during 2017.

In South America, the highlights are GDP growth in countries like Peru, Colombia and Argentina which should grow between 3% and 4% in 2017.

Now referring to Specialty Steel, there should be improvements in the automotive industry in Brazil and in India and the US should experience more stability. The oil and gas market that posted a strong decline in 2016, and an increase this year should experience more stability in 2017.

Going to page three now, I will talk about the main performance figures for Gerdau in 2016. Consolidated shipments reached 16 million tons, where shipments were down by 8% during 2015 mainly due to lower volumes showed in all business operations in our total sale of the specialty steel unit in Spain.

Now, net sales totaled BRL37.7 billion, down by 13% vis-a-vis the year before. Gerdau's net income in 2016 was negatively impacted by non-recurring items related to accounting write-offs, mainly property, plant and equipment and goodwill amounting to BRL2.9 billion non-cash. Thus, the company's EBITDA and adjusted net income are presented in a way that best reflects Gerdau's performance and the internal effort of the management in all the operations.

Adjusted profit before interest, taxes, depreciation and amortization, known as EBITDA, adjusted EBITDA totaled BRL4 billion, a 10% reduction vis-a-vis 2015 due to lower gross profit, partially offset by a reduction of BRL343 million in SG&A. Now, adjusted net income was BRL91 million, down 87% over 2015, due to lower generation of adjusted EBITDA in the period. Including the non-recurring items accounting income in the period was negative by BRL2.9 million.

I would also like to mention, free cash flow, one of the priorities of Gerdau's financial efforts totaled BRL2.3 billion in 2016, mainly due to the generation of BRL1.2 billion in the fourth quarter of the year.

Now I will talk about our divestments on page four. We continue to pursue our strategy to focus in our most profitable assets. And in 2016, divestments totaled BRL1.3 billion, considering its economic value. That refers to the sale of the specialty steel units in Spain; the sale of long steel mill in Colombia; the Cleary Holdings company, a coke producer and holder of a coking coal reserve in Colombia; also 30% stake in the company Corporacion Centroamericana del Acero; and also the sale of downstream units and land in the US. Since 2014, total divestments had up to BRL2.4 billion, along three years just to give you an idea, we've sold 13 assets in the United States, Europe and Latin America.

Now let's talk about investments. In 2016, a total BRL1.3 billion, that was a reduction of 43% vis-a-vis the year before, and this reflects how selective we were in choosing new investments. The main highlights were the conclusion of investments, I mean, centered in the heavy plate rolling mill at the Ouro Branco mill in Minas Gerais, and also the conclusion of the plant in Argentina which should start up next March.

In 2017, Gerdau will continue to be very selective in terms of CapEx with a disbursement of 1.3 billion focusing on productivity improvement and the maintenance of its plants.

Now I will give the floor to Harley, and then I'll come back to you after his presentation. Thank you.

Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Thank you, Andre, and good afternoon. Now let's take a look at slide seven, and I'll talk about the results and performance of each business operation in the fourth quarter of 2016. Further on, I'll give you more details about our consolidated results.

Starting with Brazil, shipments in the fourth quarter of 2016 in relation to the same period of the year before was higher due to increase in exports and a slight recovery in the domestic market. Looking at EBITDA and the margin in the fourth quarter of last year, there was an increase due to lower SG&A, even though the gross profit remained stable. Specifically related to the third quarter of 2016, reductions in EBITDA and EBITDA margin were caused by the market mix, a drop in the domestic market, and an increase in export with lower cost of remedy coming from exports and scheduled maintenance costs amounting to BRL100 million.

Now referring to North America, sales were stable when we compare the fourth quarter of 2016 with the fourth quarter of 2015. EBITDA in the fourth quarter of 2016 was down vis-a-vis the fourth quarter of the year before due to lower net sales per ton denominated in dollars by competition and also by competition from imported goods. This reduction was partially offset by lower SG&A. Thus the EBITDA margin went from 8.7% in the fourth quarter of 2015, to 3.8% in the fourth quarter of 2016.

Now referring to South America, shipments in the fourth quarter of 2016 were slightly down when compared to the fourth quarter of the year before, in keeping with the economic performance of each country where Gerdau operates. EBITDA and EBITDA margin in the fourth quarter of 2016 posted a reduction when compared to the fourth quarter of 2015 due to lower net sales that were -- that were higher than the reduction in cost of sales.

In terms of specialty steel, shipments in the fourth quarter of 2016 were down by 27.8% when compared to the fourth quarter of 2015, mainly due to the sale of the units in Spain. And improvements in EBITDA and EBITDA margins in the fourth quarter of 2016 vis-a-vis the same period of the year before occurred due to the sale of the units in Spain that have lower margins

when compared to the other units of specialty steel in addition to higher earnings on the United States units.

Now going to the slide eight, we talk about consolidated figures. In consolidated terms, adjusted EBITDA totaled BRL716 million in the fourth quarter of 2016, down 21.4% in relation to the same period of the year before. Now if we look at the bridge chart in the upper part of the slide, we see that the decrease in the adjusted EBITDA is a result of lower shipments and lower net sales per ton, partially offset by the optimization of operating costs and expenses, mainly SG&A expenses.

It is important to highlight that the consolidated results for the quarter was impacted by the fact that the two largest operations Brazil and North America posted results continuously lower than those posted in the third quarter of 2016 as mentioned in previous slide.

On the bridge chart in the lower part of the slide, we can see that we went from an adjusted net loss of 41 million in the fourth quarter of 2015 to an adjusted net loss of BRL205 million in the fourth quarter of 2016 as a result of lower EBITDA in the period.

Now, speaking about dividends in 2016, Gerdau paid out BRL85.4 million equivalent to BRL0.5 per share to payout dividend as a result of our earnings obtained in the first nine months of 2016 and also due to pre-existing earning reserves.

Looking now at slide nine, I will talk about our investment and liquidity of the company. This limit our positive figures related to the closing of the year. Gross debt as of December 31st, 2016 was BRL20.6 billion, down by 2.4% when compared to September of 2016 and 22.3% vis-a-vis December of 2015, basically due to working capital financing amortization. So weighted average costs of the debt was 7.2% a year with the average amortization tenure of 5.7 years.

On December, the 31st, 2016, almost 22% of the gross debt was short-term, mostly represented by working capital lines. From the BRL4.5 billion of short-term debt, as illustrated on the right part of the slide, BRL2.6 billion refer to a 2017 bonds that matures in October of this year and the rest refers to working capital lines that are constantly renewed.

Cash and cash equivalents and the credit lines of the company are more than enough to cover the investments or to cover this bond in October 2017. In addition, the company could also refinance the debt in total or partially. The significant reduction of net debt over EBITDA ratio of 4.2 times in December 2015 to 3.5 times in December 2016 is in despite of lower EBITDA in the periods mentioned. The consequence of debt amortization that was made possible through cash generation in the period in addition to the positive effect of the foreign exchange variation.

One of the positive aspects that I would like to highlight is the company's strategy related to the capital structure of the Metalurgica Gerdau SA Holding. In November 2015, the company entered a public offering amounting to BRL900 million, aiming at reducing its debt position at that time. In addition, in August 2016, the company issued convertible, exchangeable and redeemable debentures in the amount of BRL430 [ph] million, and as a second step also to optimize its capital structure.

To that end, in the fourth quarter of 2016, we sold 15 million of preferred shares of Gerdau SA that were owned by Metalurgica Gerdau, amounting to BRL641.3 million, with the strategy that Metalurgica Gerdau was able to reduce its net debt from BRL2.1 billion in September 2015 to BRL574 million in December 2016, which will significantly improve its balance sheet in the coming years and also its capital structure.

Now moving to the next slide, the slide 10, we will refer to working capital. In December 2016, the cash conversion cycle of the company was lower when compared to September 2016, due to a 15.1% reduction in working capital when compared to a reduction of 0.9% in net sales. The working

capital reduction was a result of inventory adjustment and lower trade accounts receivable in almost all business operations. It's worth mentioning that in 2016, there was a BRL2.6 billion reduction in working capital and the company remained focused on the management of this indication. The cash financial cycle currently find itself at a much higher level, which shows that we promoted a very significant structural change in the way the company operates.

Now moving to slide 11, we talked about cash generation, and this is a very relevant and very significant event this quarter. As we can see in the chart, the generation of BRL1.2 billion of free cash flow in the fourth quarter of 2016 and BRL2.3 billion in the year of 2016 with the consequence of the release of working capital in addition to EBITDA that was more than enough to honor the company's commitment. CapEx discipline and the efforts to manage working capital will continue to play an important role in the generation of free cash flow in 2017, which will allow the company to continue deleveraging the company.

I would also like to highlight some important aspects that must be taken into consideration, when we look at the performance of the year. The drop in gross profit due to lower shipments during the year was offset by 48% due to all pricing efforts promoted by our management and resulted in about 13%, or BRL340 million in reduction in SG&A. Thus the EBITDA margin in the year went from 10.3% in 2015, to 10.8% in 2016. And this will make possible and cause the reduction in the gross margin. In addition to this reduction in working capital, and a 40% reduction in CapEx allowed us to maintain strong cash generation in 2016 and also the consequence reduction of the other indicators.

Now going to slide 12, and well, I would also like to talk about accounting losses non-cash in the fourth quarter of 2016. Gerdau presents its financial statements in compliance with IFRS that determines that we should conduct impairment test for goodwill and other long lived assets of the company. To determine the impairment value of each business segment, the company uses the discounted cash flow method based on the economic and financial projections for each segment. These projections are updated taking into account changes to the economic landscape in the market where the company operates, as well as the assumptions related to the results expected for each segment.

And in 2016, particularly in the fourth quarter, the total impairment of the asset reached BRL2.9 billion, being BRL2.7 million posted as goodwill and BRL100 million as property, plant and equipment in the North America BD, and BRL139 million as PP&E in the South America BD. I would like to mention once again that these extraordinary events affected Gerdau's accounting results, but it was a non-cash impact.

Now, I'd like to give the floor back to Andre for his final remarks.

Andre Gerdau Johannpeter

Thank you, Harley. To conclude, I would just like to say a few things about this current nominal structural challenges that we still face in the global steel market, the economic downturn that has been faced Brazil, which is almost coming to an end and the drop in shipments in our main market. We were able to close 2016 despite of that with a positive performance.

And I would like to start by mentioning the BRL2.3 billion of cash flow generation, a reduction of 43% in CapEx vis-a-vis the year before, we also improved our leverage ratio with a 26% reduction of our net debt, and promoted a 13% reduction in SG&A when compared to the previous year.

Moreover, we continue pursuing our strategies and focus our efforts in assets of higher profitable margin. And in 2016, divestments totaled BRL1.3 billion, and in the last three years, BRL2.4 billion. In view of all of these initiatives, our management efforts were acknowledged by the capital markets,

which resulted in a very strong stock price appreciation of Gerdau SA and also Metalurgica Gerdau SA in 2016.

Now, the outlook for 2017, we remain challenging in the steel industry, but we hope to see a gradual recovery of steel demand throughout the year. On a positive note, I would like to tell why we believe that that will be the case and that's because international steel prices are higher this year than the year before, much due to increases in raw materials, especially coal. Price of coal has escalated, and more recently, we've seen a strong price recovery of iron ore, which helped to keep international prices at a higher level.

Also in 2017, we can mention the accelerated growth in the US, probably boosted by the new administration and what has been announced during Trump's campaign like infrastructure investments, mainly in energy and environment, a possible tax reduction, which is currently being analyzed, and also they want to fight unfair trade in the US.

Well, with these initiatives, we should expect to see a recovery in the landscape. And as for Brazil, we expect to see recovery of growth in the second half of the year and comparing today with the year before, now we see inflation approaching the target, and today we may expect another announcement and experts are pointing out to interest rates at around 10%.

The government is working on several reforms like pension funds, welfare and labor laws, and if we look at GDP a year ago, we expect a drop to 3.45% and 4%. But we should expect a growth of 0.5% or even 1%, looking at all of these factors combined, we believe that in the second half of the year, Brazil -- Brazil's economy should recover and that will be very positive in terms of steel demand. We've made many adjustments at Gerdau as part of our management efforts, and today we operate in a simple way, and we are ready to operate in our most important markets like Brazil and the US.

Now for 2017, we will continue to work diligently to increase the value of the company, focusing on several initiatives. We will start to carefully manage with our financial indicators and reduce leverage, and we will work towards our culture modernization at Gerdau to initiatives such as digital innovation, which is part of our important productivity gains and cost reductions. We will also continue as I said before to focus on our most profitable assets.

And this concludes our presentation, and now, we are available to take your questions.

Questions And Answers

Operator

Ladies and gentlemen, we will now initiate the Q&A session. (Operator Instructions) Our first question comes from Thiago Lofiego from Bradesco BBI.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Good afternoon, everyone. I have two questions. Andre, first, I would like you to comment a bit on the competitive landscape in Brazil. Talking a little bit about demand, but also supply, the market seems to be more fragmented with new small players in the market that may be bothering or steering up this competitive landscape. Do you believe that we should expect a decent consolidation in the industry and how aggressive are these smaller players?

My second question refers to the US, whether you see any evolution of the metal spread in the first quarter, maybe, I don't know whether you can give me any expectation about this first quarter, and whether you can comment on the steel demand still referring again to the first quarter, if you can?

A - Andre Gerdau Johannpeter

Good afternoon, Thiago, this is Andre. I'll start by answering your first question, and then Harley will take the second question. About new entrants, these entrants are mainly focused on rebars. Well, we should also recall that we have other product lines that do not experience a market with so many players, like bars or iron ore, wire, they do not experience the same dynamics.

But when it comes to rebars and we experience the entry of new players that happened when the market was down and this is what we've been experiencing in the last two, three years. However, we've also noted that these new players were gradually finding their niche markets, and the market adjusted itself to the new demand.

And with a rebound in the second half of the year that effect will be minimized, because we face a 16% drop and last year 14% drop in consumptions, so with a drop in consumption of 3%. This year the trend for the new players that have been in the market for quite some time, they are already revisiting their clients and the market will adjust itself in terms of supply and demand.

So I think the worst is already behind us, but again the market is very competitive, that's why it's very difficult to make any predictions about how the market will behave from now on.

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Good afternoon, Thiago. This is Harley. To answer your second question about the metal spread in the US, and at year-end and this was one of the factors that negatively impacted our margins is that the metal spread were under pressure and the numbers were in both (inaudible), and this was one of the lowest levels. And metal spreads in the fourth quarter was even lower than that, and certainly this affected our figures.

We expect from now on to see some improvement in some areas. I mean the market begins to recover, and we already saw some stability in spread prices, and that's why the trend is for metal spreads to improve. Of course, it takes some time until that is materialized, and I don't know how long it will take, whether it will be all entirely in the first half of the year or the second half. But we expect to see some improvements, and certainly this was hand in hand with our plans or with the overall landscape and investments in infrastructure in the US as mentioned by the current administration. But the market in a way is already showing signs of recovery.

Now, I am referring to our operation, but the market as a whole. These are aspects that involve potential improvements throughout the year.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Thank you, Harley, and thank you, Andre very much.

Operator

Next question from Felipe Hirai, Bank of America Merrill Lynch.

Q - Karel Luketic {BIO 16467278 <GO>}

Good afternoon. In fact, this is Karel. I have two questions, the first reference to cash generation whether you could give me in more details about working capital, or whether there is still room for further reductions. I know that in 2016 you promoted great reductions, but whether you can give me also some outlook for CapEx not only in 2017, but also 2018? Thank you.

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Good afternoon. This is Harley. In terms of working capital, there are few things that should be considered. We work diligently in the last three years. And if you look at our history since 2010, we

went from more than \$5 million to numbers around 2.1 million, and of course, this affects our earnings generation. But when you look at the cycle, I mean, at the cash conversion cycle, we moved today to numbers close to 70 to 80 days.

We already demonstrated our efforts in terms of working capital in the last two years. From now on, we are better adjusted meaning that we shouldn't promote any further major working capital reductions unless the market deteriorates. So that's not in the horizon, because we foresee some recoveries, and we already show you the decrease in our shipments, and we already experienced some increases that should probably impact working capital, but not significantly.

In terms of cash generation, I may mention EBITDA that in a way should repeat or should mirror this landscape of slight recovery both in Brazil and North America. And we are diligently pursuing a very strong discipline in terms of CapEx.

When you look at what we spent in 2016 is BRL1.3 billion. This could be maintained in the following years, if we continue to experience a recovery. And this is more than enough to keep our operations going with this maintenance levels and also good enough to maintain our equipment fully operational and in good shape. So we will continue to generate a positive free cash flow in the next few years. And this combined with a more stable exchange rate, we will be able to improve our leverage.

Q - Karel Luketic {BIO 16467278 <GO>}

Thank you.

Operator

Next question from Ivano Westin from Credit Suisse.

Q - Ivano Westin {BIO 17552393 <GO>}

Good afternoon, Andre; good afternoon, Harley, and thank you for the questions. Well, the first one refers to the South America BD, you have a significant margin in the second quarter, and now in this quarter a decline. Could you elaborate on the outlook for that unit, and whether you will be reasonable to consider that there is a one-off situation and that we should expect a 15% figure again, you know that we should resume the 15% figure that we had in the past?

You have a ramp up of flat steel coming soon, and even considering this current scenario with recovery in the second half of the year, due to that positive scenario and your plans coming for next year, what would be the volume delta consolidated for the domestic market you can -- can you anticipate? Thank you.

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

This is Harley. As for the first part of the question related to margins in South America, we do believe that the fourth quarter was heavily impacted by the seasonal aspect, which is normal. But South America operation should have margins -- I mean have good margins, and we expect to maintain the same margins posted in 2016. We see a positive growth of GDP and some countries like in Peru, Argentina also will post positive figures, and we were impacted by seasonality in the fourth quarter that we should resume our regular levels in the next coming months.

About our plan, we have the hot coil rolling mills that has been in operation for about three years, and the performance has been very good also in terms of sales. We are very pleased because it's being well accepted by our customers, but it's (inaudible) a mature process and at high utilization levels in terms of its capacity. Utilization capacity is over 80%.

Now the heavy plate rolling mills started up more recently, and we still have to go through a learning curve which takes about six months to one year until we can see improvement. And the utilization volume is lower. We cannot disclose the volumes for the future, but I can just give you an idea about the coil hot rolled -- rolling mills that we hope to see some market recovery in terms of the heavy plate rolling mills, but we are introducing very lot of products of high quality and very differentiated. We have had positive feedback from our customers. Customers are pleased, and therefore, we are very excited with the performance that we will certainly achieve was the heavy plate rolling mills reached full maturity.

Operator

Next question from Thiago Ojea from Citibank.

Q - Thiago Ojea {BIO 17363756 <GO>}

Good afternoon, and thank you for this opportunity. My first question is about scrap prices in Brazil. We've seen a drop on the average steel or long steel prices, and -- but we've seen an increase in the price of scrap in Brazil. How do you see that movement, and what could be the short and mid-term outlook?

And the second question refers to demand in the United States. Andre mentioned the new Trump administration and the measures that should be implemented, but in view of all of these measures, can you anticipate any rebound of the economic activity or you think that the US will depend on these new measures to be able to grow more?

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Good afternoon, Thiago. This is Harley. Referring to the scrap, I think what you mentioned is more a one-off structurally. Our scrap in Brazil reflects our advantage, because we have a very diversified spread around collection of scrap throughout Brazil, even though, there are some one-off effects here and there. Structurally speaking, we haven't seen any changes. And in this landscape, the structure is very strong, especially considering the way we collect scrap.

Now about the United States, I commented on Trump's administration initiatives, things that were announced during his campaign, and we are just waiting to see whether these things will be implemented. Infrastructure is not something that will happen overnight, we do not have a lead time yet. So we are just waiting to see what will happen.

Tax reduction is something that will produce a more immediate effect, and this would have tripled on the industrial side. We also have an anti-dumping case on rebars. And I think this week we will hear something about that from the US Department of Commerce.

But in the shorter term, we can say that non-residential construction continues to develop, and at this level, the industry itself also have some recovery. And that starts with the increase in commodity prices. This affects some industries in the US. Oil and gas, and energy, we start to see some reaction. And we see some signs in the industries, but our market focuses more on the non-residential market that continues to develop well. Infrastructure will produce a losing consumption, not for now, but probably for 2018, it should be a bit stronger.

Q - Thiago Ojea {BIO 17363756 <GO>}

Thank you. Do you think that this non-residential improvement is something that could be seen in the first quarter because then we also have to take into account the seasonality effect?

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Hard to say probably it could be more noticeable in the second half of the year because the winter will be over and spring, summer and autumn are betterment [ph] mainly because of the climate condition.

Q - Thiago Ojea {BIO 17363756 <GO>}

Thank you.

Operator

Next question from Marcos Assumpcao from Itau BBA.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Good afternoon. You just talked about countervailing duties and anti-dumping cases in the US. Could you please give me an idea of what should be expected in the short-term and what could possibly be the margin in the US. If these cases are proven, and in part of rebar from Turkey would go down? Can you also talk about reductions in leverage in Metalurgica Gerdau since 2015. And how do you see leverage ratios in Metalurgica now. Do you believe that the ideal situation would be still to have some debt or no debt at all. So how do you see the situation going forward?

A - Andre Gerdau Johannpeter

Thank you, Marcos. I will talk about trading and probably we'll talk about Metalurgica. Our expectation is that it should -- the results should be positive for the industry. Three years ago, between 2013 and 2014, there was a previous study and the evaluation showed a very small percentage of anti-dumping. But the period of that is under analysis now is 2015/2016 and there was a big leap in volumes.

We also believe that it will be possible to prove that anti-dumping impact occur and some countervailing measures will be adopted that's what we expect to see. But, you never know, you have to wait for the results. It's very difficult for us to expect any opinion, but we are hopeful because looking at the industry data here is a possibility that the anti-dumping case will be successful. There might be any effect in the market depending on the percentage, and then we will have to see what the market dynamics will be. Mostly here we are talking about imports of rebars into the US, that's why this case is so important. And so we have to wait and see what the final outcome will be.

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Good afternoon. Marcos, this is Harley. Now, about Metalurgica as a holding company are objective is reaching zero debt. We only want to hold stake in operating asset. So this is our objective. So all of the efforts there has started back in 2015 produced good results. And we have to find a solution to the debt without putting pressure on Gerdau and this something that we do successfully.

Part of the debt has to do with the debenture that we issued that are in high demand, and once that is converted into equity, and there is a great possibility of that happening that will -- brought [ph] our debt down until we will be in a more comfortable position. And we believe that once we were in the net debt over EBITDA ratio, Gerdau results will emerge that will produce more dividends to Metalurgica and this equation with cash generation will be well evolved.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Thank you very much. Thank you, Andre. Thank you, Harley.

Operator

Next question from Leonardo Correa from BTG Pactual.

Q - Leonardo Correa {BIO 16441222 <GO>}

Good afternoon, everyone. I do apologize for the quality of my landline, but I hope you can hear my question. My first question is addressed to Andre. About the US, my question has to do with some possible listing of the operation in the US. Whether this has been contemplated or whether this could be studied in the future? I know that G&A (inaudible) who have been listed and you engaged in a daily scenario, the scenario changed and we see some Gerdau peers in the US where Commercial Metals and Nucor is trading, nine or 11 times EBITDA that is a relevant multiple differential which generates great value potential. I would just like to hear your views about this movement and what you see coming forward in terms of listing abroad, listings abroad, especially considering a more promising scenario in -- with this Trump administration.

My second question is about operating adjustments. Our -- the quarter had some stoppages, and this harmed some of the analysis. Do you think that, would you see some more streamlining of assets, or this is a project that will continue further or not, and what should be expected? Also, given this benign scenario of metals -- metal spreads, I want to know whether you expect to export in that market?

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Good afternoon, Leonardo, this is Harley. Let me first answer the first part of your question about listings in the US. When you look at the comments of the market -- on the market, you see that rebars market today, is using very good multiples in this industry. And this also impact us indirectly, therefore, indirectly we benefit from such move. And even though, we are not considering anything at the current moment, this is always an option that is brought over to us. I would say therefore that this is an option that always marries our attention and further analysis.

I will -- I think you also asked about operating adjustments. In fact, the last quarter of 2016 was heavily impacted by schedule maintenances and adjustments that at the end, pollutes [ph] the entire result, and it's difficult to outline all of the impact. But in fact, we have to consider drop, the drop in Brazil and also the drop in shipments in the US, because the main adjustment stoppages occurred in Brazil, but now we resume operations in our new -- in January, so things should be back to normal.

We don't have anything in the pipeline for the year or we do not anticipate any adjustments or shutting downs or stoppages that would cause great impact. We closed (inaudible). And in the second half of the year, we were much lower than that, due to the normal seasonality. But I think that the impact was stronger this year.

But as of iron ore, our priority is to start the Ouro Branco Mill, but our production, it's higher than Ouro Branco's consumption, not only in terms of volume, but we also buy from other local producers in order to do the necessary plan. And so from what we produced, we end up now consuming everything, so we try to sell it both domestically and abroad. And we are constantly monitoring that. We have some sort of rush here, but now iron ore hits 95 almost. But we want to look at the reality of the moment itself. And at given moment, we may export and then we should resume to regular moment. It's just a one-off situation, because our focus at the moment is to supply to our Ouro Branco Mill.

Q - Leonardo Correa {BIO 16441222 <GO>}

Thank you, Andre. If you allow me to add something to my question, do you have any significant inventory that you could tell probably faster, I don't know whether you can tell us anything about your iron ore inventory levels?

A - Andre Gerdau Johannpeter

Honestly, I can't tell you, because we would have to analyze the operation. Usually, all of the output is already sold. We don't carry much inventory. We produce as, you know, in the same pace of our

deliveries, that maybe we can try new. We can answer you in more detail later on. Okay?

Q - Leonardo Correa {BIO 16441222 <GO>}

Yes. Thank you.

Operator

Next question from Bruno Giardino from Santander.

Q - Bruno Giardino {BIO 15974970 <GO>}

Good afternoon. My first question is about price increases. If you try to increase prices in February, and I just want to know how that's moving forward? And the second question has to do with the impact of this price vis-a-vis coal prices and volatility?

A - Andre Gerdau Johannpeter

Bruno, good afternoon. This is Andre. On pricing, I'm not going to be specific for market. But as I said, there is an environment that is simply sustaining prices, influenced by the spike in coal prices. It's still very high, even though we had dropped a bit, and also iron ore prices were up. And this impact international prices and corporate prices. To largely, we've heard of global prices in China, and also from other exporters like Turkey, and reasonably the prices are going up. And this has an impact on domestic market, which caused a further adjustment, but this should be looked on a market-by-market approach.

If this continues, this should lead to further adjustments due to higher international prices and raw material prices. And I think your other question was on coal. It's difficult to say, because there was a spike in coal prices and then prices came down a bit. Therefore, it's difficult for me to give you any figures at the moment.

Q - Bruno Giardino {BIO 15974970 <GO>}

Thank you.

Operator

Next question from Gabrielle Curtis from Banco Do Brasil.

Q - Gabrielle Curtis

Good afternoon and thank you for the opportunity. I would like, you to elaborate more on what happens to that non-recurring depreciation at the Brazilian real? And also a question regarding divestments. I don't know whether you can comment on the assets that you have in mind to sell. And where they are located in what unit, and how much you will expect to gain from the sales?

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Could you please repeat the first part of your question, because it was very low. The second part of the question was okay.

Q - Gabrielle Curtis

Can you hear me better now?

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Yes.

FINAL

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Q - Gabrielle Curtis

The first question refers to depreciation at the Brazil BD, looking at the amount reported for the fourth quarter.

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Okay. While we look at the depreciation, let me say that we continue pursuing our strategy of focusing on the most profitable assets than last year, we already referred to important divestments in this sales, and keeping with what we've been saying in the past, two, two-and-a-half years. And now, we are just showing some of the results and we will continue pursuing that strategy.

We don't have anything to announce at the moment because we do not disclose anything specific per region. We continue looking at possibilities of full sales or partial sales or even joint venture, so we would continue to focus on this program, and as things happen, we will let you know.

Q - Gabrielle Curtis

Thank you.

A - Andre Gerdau Johannpeter

Now about depreciation in Brazil, in fact in the last quarter, we may experience some adjustments. Comfortably [ph] most representative figure when compared to -- I mean an average between the third and fourth quarter. The startup of our heavy plate rolling mills in Ouro Branco impacted depreciation in the fourth quarter.

Q - Gabrielle Curtis

So you think we could see some, some payroll still remaining in this coming quarter?

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Well, what happened in the third and fourth quarter is more significant than anything else. I would also like to say something about our investments, just to give you an idea of how this is important to us. Other divestments that we already did and what we presented to you during this presentation amounting to 1.3 billion in 2016. For instance, a multiple in relation to EBITDA it was around 8 times to 10 times.

That's why this is so important and it really emphasizes the fact that we are focusing on the most profitable assets. This brings about higher economic value to the company, reducing SG&A and reducing other lines of our balance sheet, and EBITDA will be much -- I mean is much lower. When we sold Sidenor, you remember what the multiple was. The average is very close to what we had in Spain between 8% to 10%.

Q - Gabrielle Curtis

Thank you very much.

Operator

Next question from Milton Sullyvan, XP Management.

Q - Milton Sullyvan {BIO 19085202 <GO>}

Good afternoon. I would like to apologize for the poor quality of the call. But I have two questions, and thank you for this opportunity. The first question refers to scrap prices or scrap costs. So, given the operating leverage of the company, when you take a look at the metallic cost of the company

in the Brazil BD, the metallic costs should be at a better quality. I think that improved significantly. So I would like to revisit the issue of scrap from earlier on. I just want to know whether we are looking at further stability or improvements in the cost of scrap, once we look forward to the second half of 2017?

Then the second question relates to the growth in shipment and the impact in working capital and CapEx. We saw that the company had a good performance in working capital and CapEx. Sir, I want to understand, what are we looking at in terms of shipment growth with that having to look at relevant impacts in investment, working capital and maintenance CapEx? Thank you.

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Good afternoon, Milton. This is Harley. On scrap, well, I would say again that this was one-off situation. So we shouldn't expect any more significant changes. We anticipate a good spread in terms of our scrap, because we collect scrap all over Brazil and this benefits our average cost of scrap, because we collect in bulk. Therefore, what you saw in the quarter is like a one-off situation, but in particular, we don't see any major changes going forward.

Now, in terms of working capital and CapEx, we are well-positioned in working capital. We are more particularly referring to CapEx. Even with a quick recovery in the markets both in Brazil and in the US, our largest markets, we figured in around 60%. We do not anticipate any substantial divestment or changes in CapEx to face this recovery. Once recovery comes, we will be at a great advantage, and there will be no need for further investments.

Now referring to working capital, we are better adjusted, and we also introduced practices to manage working capital, that we're very positive. So once the market recovers, we will tend to recover as well, and operate at a more optimized condition. When you have a 60% capacity, it still have a lot of rooms to use or a lot of rooms to maneuver through our capacity. And then for instance, we can change from one product to the other because we have capacity to do that. So if there is a rebound, we will not need as much working capital. From this year, we believe that even though there will be a recovery in volumes, the efforts in working capital will not be very significant. We always see the seasonal effect at the end of the year and some working capital recovery in the beginning of the following year. So I think we will find results at very optimized levels this year. Thank you.

Operator

Next question in English from Mr. Carlos de Alba from Morgan Stanley.

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

Thank you very much. So I just wanted to know if there are any specific initiatives to further -- or to increase EBITDA, and further improve cash generation. And the working -- the accomplishments on working capital have been great, and CapEx is certainly in the low. So going forward, the cash flow generation has to come from better EBITDA. Could you share any of the specific initiatives that the company may still be pursuing to increase EBITDA? Is it possible to further reduce cost and reduce SG&A expenses without seeing a recovery in volumes or without seeing a strong recovery in volumes?

And the second question has to do with the expectations for higher dividends in 2017. The company paid very low dividends last year, understandably, given the difficult situation as they face, but is it possible that the company would try to increase the level of dividends that it pays in 2017? Thank you.

A - Harley Lorentz Scardoelli {BIO 7283603 <GO>}

Both of those question refer to free cash flow generation for 2017 considering that an important part of our cash generation in 2016 has to deal with working capital adjustment and whether we reach the limit and whether there is a possibility of EBITDA improvement or any entrants reductions in order to maintain that situation, and also whether this will have a positive impact in our dividend payout in 2017.

Well, in that way, we anticipate some vulnerable increases in our operations. We also talked about better margins. And SG&A was significantly reduced in 2016, also taking into account that if we look at the end of the year, at year-end our SG&A level was much lower, therefore towards 2017, we may capture additional reduction.

Well, we are comparing it with the beginning of 2016, where that number was higher, there is a possibility of EBITDA increase, and if we continue to optimize CapEx, like we mentioned BRL1.3 billion, this should also tend to improve and generate good cash.

Another point I want to mention is that as I said we have cash and cash equivalents, and goodwill, good enough to honor all of our commitment. This is the most expensive bonds that we have. Most part of our cash is denominated in US dollars, so there is a difference between the interest that we pay and the interest that we receive in dollar term, and that should also be captured throughout the year once we paid for that bond. And in a way this should improve our interest rate position in 2017.

Having said all that, we could say that cash generation, we will continue to be very good in 2017.

Operator

We will now conclude the Q&A session, I will give the floor to Mr. Andre Gerdau Johannpeter for his final remarks.

A - Andre Gerdau Johannpeter

Thank you all very much for joining us today. Thank you for your questions. And if you have any further questions, please contact our Investor Relations team. And on my behalf, and on behalf of Harley, I would like to thank you and invite you to also join us again on May 4th for the earnings conference call for the first quarter of 2017. Have a good day.

Operator

Gerdau's earnings conference call is now concluded. I would like to thank you for participating, and have a good afternoon.

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