

Q4 2015 Earnings Call

Company Participants

- Andre Gerdau Johannpeter, President & CEO
- Harley Scardoelli, EVP

Other Participants

- Alan Glezer, Analyst
- Gabriela Cortez, Analyst
- Ivano Westin, Analyst
- Leonardo Correa, Analyst
- Marcos Assumpcao, Analyst
- Osmar Camilo, Analyst
- Tatyana Wolff Katalan, Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good afternoon. Welcome to Gerdau's conference call about the results of the Fourth Quarter and year of 2015.

At this time, all participants will be in listen-only mode during the Company's presentation and after that, we will initiate the Q&A 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 of the Company; 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.

Andre Gerdau Johannpeter

Thank you. Good afternoon, everyone and welcome to Gerdau's conference call.

Firstly, I would like to say that we postponed our earnings release conference call of March 1 to today in order to analyze the case records involving Gerdau and the Zelotes operation. To reinstate our position on this topic, we reached the official communicate that many of you already received.

First of all, Gerdau has pending proceedings filed with the Administrative Council of Tax Appeals CARF [ph] and has always used the services of external firms strictly to obtain the best possible technical advice. Contrary to media reports, this is not a matter of tax evasion, false tax statement or omission to skirt eventual taxes due. But it is a question of legitimate use of the right of Gerdau companies, expressed by laws and precedents. The financial information related to ongoing proceedings at CARF have been disclosed in the explanatory notes of the Company's Financial Statements.

All agreements with these external firms and also other contract and agreements with service vendors that Gerdau has entered into with service providers, included a clause that determines absolute compliance with laws, breach of which calls for immediate termination thereof. No money was paid or passed on to external firms in the specific case and agreements were rescinded when the names of service providers investigated were reported in the press for suspected illegal activities. The Company never gave any authorization for its name to be used in alleged unlawful negotiations and strongly repudiates any action taken for this purpose. Thus, Gerdau, as a company that has been in the market for 115 years, reiterates that it has set strict ethical standards for its dealings with public agencies and reaffirms that it is, as it has always been, at the disposal of competent authorities to provide any clarifications that may be requested.

Now, I will proceed with the analysis of the performance of the consolidated results of the Company in the last 12 months of 2015. And I will also speak about the global landscape of the steel industry followed by comments on Gerdau's performance and investment. Right after my presentation, Harley Scardoelli will elaborate on Gerdau's financial performance in the Fourth Quarter. Then at the end, we'll be available to take your questions.

Slide two of the presentation for those of you who follow us, I would like to talk about the world steel industry that in 2016 face another challenging year. According -- as we said before, throughout the year according to the World Steel Association in 2015, production was down by 2.8%, reaching 1.6 billion tonnes, reflecting a reduction in manufactured volumes in all regions of the world except for Oceania. The utilization of installed capacity worldwide was around 69.7% in 2015, when compared to 73.4% in 2014, according to the World Steel Association. Now for 2016, the outlook on the demand side points to a slight growth of 0.7% according to the Association. However demand in China, where most part of this surplus installed capacity is, should be down by 2% in 2016. So the surplus Chinese production puts pressure on prices in the international market.

In addition to China, the world steel market has been significantly impacted by the low level of investments, turbulences in the financial market and geopolitical conflicts in several regions of the world. As I said before, we also have structural factors such as excess installed capacity of over 700 million tonnes in the world which we will continue to impact the global steel industry. Considering only emerging and developing economies, including China, demand should grow 1.2% in 2016. Now in the developed economies, the demand for steel should grow 1.8%.

One factor that impacts the market where Gerdau operates is the entry of imported steel in North America and also Latin America. According to (inaudible), Latin America continues to be one of the main destinations of steel coming from China. The region alone received 9.4 million tonnes of Chinese steel in 2015. To minimize the effect of the unfair competition throughout 2015, there have been some coalitions of two associations both in North and Latin America who are working together to mobilize their governments to adopt antidumping measures to avoid a slowdown of the industrial activity and reductions in headcount in these regions.

In Brazil, the economic downturn had a significant impact in the demand of the main steel consuming sectors; industry, civil construction and the automotive segments. As you've noticed, they posted negative performance -- negative numbers in 2015. Just to give you an idea, according to IBG, the GDP for the industry was down by 6.3% in 2015, whereas the GDP for civil construction was down even further 7.6% and this had a direct effect on the domestic market. Sales in Brazil declined 16.1% in 2015 and these figures are from Instituto Aco Brasil.

Now on the positive side, in North America, they had a good performance, particularly in non-residential construction. In addition, the infrastructure market begins to show signs of recovery. For specialty steels in North America, the situation was different. The automotive industry posted growth, even a record growth, whereas there was a significant reduction in demand in the oil and gas sector, which is impacting the performance of the operation.

In Europe and India, there was an increase in sales of light and heavy vehicles throughout the year. In Brazil, production and sales of vehicles experience dramatic drop. According to ANFAVEA, licensing of new vehicles in Brazil dropped 25% in 2015 vis-a-vis the year before.

Continuing on to page 3, I will talk about the numbers for 2015. The fact that in 2015 the result was influenced by non-recurring items mainly related to the write-off of assets and goodwill amounting to BRL5.3 billion, non-cash. The strong presence of Gerdau in the North American market and the impressive management effort of our teams allowed us to mitigate the impact from the lower demand for steel in our balance sheet in Brazil and abroad. Therefore, we focus on the financial sustainability of the Company, significantly reducing working capital with a cash impact of BRL2.4 billion. And also growing free cash generation by 58% totaling BRL3 billion.

We also reduced expenses with SG&A by 5%. In addition, in the Brazil BO and specialty steel, we adjusted the production in our mills in the country to the levels of market demand. Next, we will present EBITDA and adjusted net income. So as to reflect the performance of the Company and the internal work of management from our team. Consolidated shipments totaled 17 million tonnes. And there was a 5% reduction when compared to 2014. And this came from lower shipments in almost all the operations, particularly in the domestic market in the Brazil BO. In the First Quarter, the Gerdau Brazil performance was impacted with the reduction of 40% in sales to domestic market, particularly in the month of December when compared to the same period of the year before. In view of this landscape, the Company adjusted its operations towards the current demand and future demand of the market, conducting scheduled maintenances in the mills, which impacted EBITDA.

Net sales in 2015 was BRL43.6 billion, 2% higher than the amount posted the year before. This growth is associated to the positive exchange rate effect when sales from abroad were converted into Brazilian reais. The highlight was the performance of the North America BO responsible for generating 39% of the consolidated net sales. The result partially offsets the lower performance of the Brazil BO, as we said before, strongly impacted by the downturn of the local economy.

Adjusted EBITDA was BRL4.5 billion, 8% reduction when compared to 2014, especially due to the lower performance coming from Brazil and specialty steel BOs and partially offset by a better performance coming from the North America BO. Adjusted consolidated net income was BRL684 million and then considering non-recurring items, there was a negative accounting profit of BRL4.6 billion.

Now moving on to slide 4, now talking about our investments, year-to-date [ph] investments in fixed assets totaled BRL2.3 billion, led by the depreciation of the Brazilian real, as part of the investments are tied to the US dollar. The highlights of the year are the startup of the structural profiles mill in Mexico, which took place in June of 2015 and the construction of the melt shop in Argentina with an estimated startup for the end of 2016 together with the installation of the heavy plate rolling mill in Ouro Branco which was then anticipated to July of this year. In 2015, we worked with installed capacity utilization between 65% and 70%, hence because of that, we will continue to restrict CapEx in 2016, prioritizing the maintenance of the existing equipment. The outlook calls for further reductions in investment levels considering that the large carrying investments are about to be concluded.

Thus, this year's investment plan foresees outlays of BRL1.5 billion, which is a reduction of 35% when compared to 2016. The amount of CapEx to be spent in 2016 should be maintained in the following years as the current landscape remains unchanged.

With that, I conclude my part of the presentation. I'll give the floor to Harley Scardoelli, who will talk about the financial numbers.

Harley Scardoelli {BIO 7283603 <GO>}

Thank you, Andre and good afternoon to you all. Now, I will like to refer to the slide number 6 of the presentation. There we will talk about the results and performance of each business operation in the Fourth Quarter of 2015. And next, I will give you more details on the consolidated figures. We conclude, talking about the extra-ordinary event of the quarter.

Concerning Brazil and starting with Brazil, the environment of uncertainties in the economic landscape has caused us to have lower demand and this has affected our business. This has also caused a drop in shipments of steel in the Fourth Quarter of 2015, when compared to the same period of the year before. On the other hand, exports presented an increase in relation to the Fourth Quarter of 2014, due to opportunities in the international market, coupled with a favorable exchange rate.

Looking at EBITDA in the Fourth Quarter of 2015, the absolute value was down by 74% when compared to the Fourth Quarter of 2014, due to lower dilution of fixed cost and a worse market mix. In addition, all the costs related to production started, also impacted EBITDA in BRL110 million in the Fourth Quarter of 2015. This will also affect the EBITDA margin that went from 19.1% in the Fourth Quarter of 2014 to 6.9% in the Fourth Quarter of 2015. Not considering the effects of production stoppages, EBITDA margin in the Fourth Quarter of 2015 will be above 10%.

Now, speaking about North America, the economic environment remains positive. However, there is growing pressure from imported products resulted in a sales reduction of 3.4% when we compare to the Fourth Quarter of this year to -- to 2014 to the Fourth Quarter of 2014. EBITDA in the Fourth Quarter of 2015 was BRL395 million [ph] when compared to BRL202 million in the Fourth Quarter of 2014. There was an increase of 96%. This improvement is mainly due to exchange variation in the period coupled with a better EBITDA margin that went from 5.5% in the Fourth Quarter of 2014 to 9.2% in the Fourth Quarter of 2015, due to lower scrap costs and additional efforts towards cost reduction. I would like to highlight, this is the highest EBITDA margins presented in a Fourth Quarter since 2007.

In South America BO, shipments in the Fourth Quarter of 2015 were down when compared to the Fourth Quarter of 2014, due to high levels of imports into the region. The optimization of operating cost mainly in Argentina, Colombia and Peru BOs in addition to lower scrap costs led to an increase in the EBITDA margin going from 8.4% in the Fourth Quarter of 2014 to 13.9% in Q4 2015.

Speaking now about the specialty steel BO, sales in the Fourth Quarter of 2015 were down by 10% when compared to the Fourth Quarter of 2014 due to strong drop in demand coming from the automotive sector in Brazil and to a lesser degree from the oil and gas industry in the US. The EBITDA reduction in the Fourth Quarter vis-a-vis the same period of the year before was due to lower reduction in fixed cost and also things related to US. Even though these countries continue to present a positive demand from the automotive industry, the challenges coming from the oil and gas sector affected the profitability of these units. On the other hand, in India, they had a better performance, especially when compared to the Fourth Quarter of 2014. As a result, the EBITDA margin was down from 12.1% in the Q4 in 2014 to 6.9% in the Fourth Quarter of 2015. If we compare year-on-year, the margin went from 10.6% to 4.6% in 2015.

Now moving to slide 7, we will talk about the consolidated. Adjusted EBITDA was BRL911 million in the Fourth Quarter of 2015, down by 27% when compared to the Fourth Quarter of 2014. If we look at the bridge chart on the upper part of the slide of page 7, we will see that the reduction of adjusted EBITDA was caused by the drop in shipments, partially offset by higher net sales per tonne. And the bridge chart on the lower part of the slide, we notice that we went from an adjusted net income of BRL95 million in the Fourth Quarter of 2014 to a negative adjusted income

of BRL41 million in the Fourth Quarter of 2015 due to lower EBITDA and higher depreciation, partially offset by positive amount in income taxes and others when we compare and also the scheduled stoppages in the Fourth Quarter.

In terms of dividends in 2015 and even with a very challenging landscape and the steel industry, Gerdau still paid out BRL253 million with the equivalent to BRL0.15 per share in payments and interest on equity for profits obtained in the first half of 2015 and also reserves from pre-existing profit. These dividends that were paid out in the first nine months of 2015 were above the 30% established in the Company's bylaw.

Now going to page 8, I will talk about debt level and liquidity of the Company. Gross debt on December 31, 2015 was BRL26.5 billion, lower when compared to September 2015 due to amortizations carried out in the Fourth Quarter of 2015 in addition to exchange rate variations in the period. The weighted average cost of the debt was 6.8% a year with an average amortization tenure of 6.5 years. On December 31, 2015, only 9% of the gross debt was short-term, mostly represented by working capital lines that were renewed.

I would also like to highlight that the most part of the EBITDA in the last 12 months was generated by BOs abroad, particularly denominated in US dollars and more than 80% of the consolidated net debt by December 31, 2015 was also denominated in US dollars and the net debt over EBITDA ratio was 3.6 times. I would also like to say that some recent evaluations by rating agencies for companies in our industry have reflected the steel crisis in the world and the impact from global surplus installed capacity, the slowing down of the economy in China, the decline in demand from emerging countries and the deterioration of the economic situation in Brazil that also saw the re-evaluation of the security.

Despite all that, it's also important to highlight that the reaffirmation of Gerdau's investment grade by some rating agencies about the Company just demonstrated that the Company has sound liquidity by means of the strong cash position, access to consolidated credit lines from banks in Brazil and in the US with no covenants and it has generated positive free cash flow in the last few years. In addition, the Company's debt structure has long-term amortization. And therefore reiterate that its cost of debt should remain unchanged.

Now moving to page 9, we will talk about working capital. In December 2015, the cash conversion cycle was down by two days when compared to September of the same year due to a reduction of 14.8% of working capital compared to a reduction of 12.4% in net sales. It's also good to mention that this working capital reduction of BRL1.7 billion from September to December 2015 contemplates the exchange rate variation over working capital of companies abroad. Not considering this variation, the cash effect was a reduction of BRL1.4 billion from September to December of 2015, which demonstrate all the efforts of the Company to optimize working capital. From December 2014 to December 2015, the effect of cash in the reduction of working capital was BRL2.4 billion.

Now moving on to page 10, I would like to highlight the strong cash generation of the Company, both in the Fourth Quarter and year-to-date. As we can see in the higher part of the chart, in the Fourth Quarter of 2015, we had BRL1.2 billion with a strong contribution coming from the release of working capital in the period. In the lower chart, we notice that in 2015, the Company generated BRL3 billion of free cash flow. This is due to EBITDA generation of BRL4.5 billion, which was up by BRL593 million in relation to what the Company had to pay, CapEx, income tax. And interest. In addition to the benefit of working capital release of BRL2.4 billion, this free cash flow positive now is -- in keeping with the strategy of the Company of maintaining financial sustainability as it has happened in 2013 and 2014 as part of a very challenging landscape for the steel market. For 2016, we will still continue to release working capital and one of the main drivers will be a restriction of outlay of CapEx. And this will impact an important reduction of 33% as Andre already mentioned in 2015.

On page 11, we report the extraordinary events during the period. Gerdau presented financial statements in compliance with IFRS. And this standard requires the goodwill and other long-term assets recoverability tests be conducted to determine the recoverable amount of each business segment. To that end, the Company uses the method of discounted cash flow using economic financial projections for each segment as a base. The Company carried out the goodwill and long-term assets recoverability test in 2015 due to the following events.

Number one, higher deterioration of the market, coupled with the excess capacity in the sector. Two, drop in demand from steel consuming countries, especially automotive and construction. Three, lower activity in certain industrial plants. And finally, or the fourth point, changes in the composition of Gerdau's business segment, which has already been mentioned in the Third Quarter of 2015. The tests were able to identify the impairment of assets and the write-off of deferred tax assets because of low possibility of change in the short-term. The total amount of these extraordinary items was BRL5.3 billion in 2015 non-cash. In the Fourth Quarter of 2015, the total impairment of assets of BRL3.1 billion due to non-recoverability of assets, I mean BRL1.2 billion was posted as goodwill at North America and BRL1.1 billion as goodwill at the specialty steels BO and BRL835 million posted at Brazil BO as property, plant and equipment. This was due to lower demand and production stoppages in some units of the Company throughout 2015, which aimed at readjusting production to the current demand level and productivity of our operation. I would like to highlight again that these extraordinary events affected the overall results of Gerdau, however, they did not produce any cash effect.

Slide 12, just to conclude my presentation, we would like to say that Metalurgica Gerdau SA did a public offering in November of 2015. The transaction involved 500 million shares with capitalization of BRL900 million used to amortize debt and also to improve the Company's liquidity position. With this transaction, the net debt of Gerdau went from BRL2.1 billion to BRL1.2 billion on December 31, 2015. The management used the proceed to settle the debts with higher cost in short maturity and as a consequence, the cost of the debt went from 110% of CDI to 105% of CDI. In addition, the liquidity of the shares of the Company had a significant increase, more than doubling its share outstanding. And increase in the number of securities traded daily from 5.3 million shares to 13.5 million on average. According to what was mentioned by management during the offering, the existing debt and low liquidity were the factors responsible for a holding discount much higher than historical figures, close to 40% [ph]. After the offering, the holding company discounts began to decline gradually being now close or below 20%.

Now, I give the floor again for Andre for his final remarks.

Andre Gerdau Johannpeter

Thank you, Scardoelli.

To conclude, I would like to reinstate the Gerdau's result in 2015 was heavily influenced by non-recurring items, though non-cash. However, our strong presence in the North America market and management efforts of our teams were crucial to reduce the impact from the difficult moment faced by the steel sector both in Brazil and in the world. One highlight of 2015 was the successful public offering at Metalurgica Gerdau SA which represented a capitalization of BRL900 million to amortized debt and also improved liquidity.

For 2016, our priorities will continue to be free cash flow generation, cost reduction, CapEx restriction and financial leverage reduction in view of the current challenging global landscape. Moreover, we will continue to work to grow market value and also to identify opportunities in markets with high added value products as demonstrated by the startup of the heavy plate rolling mill in Brazil amongst other initiatives. By the same token, we are also working with a long-term strategic view to transform Gerdau in order to face future market challenges. This involves extensive work ranging from streamlining operations and internal structures to the modernization of the corporate culture and reassessment of the potential profitability of assets.

With that, we will conclude the presentation and we are available to take your questions. Thank you very much.

Questions And Answers

Operator

Ladies and gentlemen, we will now initiate our Q&A session. (Operator Instructions)

(inaudible).

Q - Unidentified Participant

My first question about your capital structure more particularly related to the debt is that, considering the maturity for 2017 for almost BRL4 million, do you have any renegotiation strategy to renegotiate the debt or this is not yet a priority. And along the same lines, do you have any other strategy in terms of the potential sale of assets and what would be the expected amount of spending from this strategy?

A - Harley Scardoelli {BIO 7283603 <GO>}

This is Harley speaking.

In terms of leverage and I must say something important about 2017, the depreciation of real of 2015 had a very strong impact in our debt. And the productive impact coming from (inaudible). So if the dollar goes back a bit, the trend is that our leverage position will improve. A second point has to do with our free cash management and this is still a priority for 2017. During our presentation, we said that we are working very hard to reduce investments about 35% in reais in terms of reductions for 2016. There is something had to be done in terms of working capital, all of these efforts, together with a dollar position or maybe with a lower depreciation, we may see the deleveraging of the Company in 2016.

Now, referring to our debt that matures in 2017, about half of that will mature in October of 2017. And there are several alternatives to deal with that maturity. We may refinance and I think that today the market is a bit more restricted. But by 2017, until then, I mean we have enough time to deal with that matter. The other part of the debt, our short-term ranging from working capital (inaudible) debt. And all of those should be refinanced. So this is not a problem in terms of rolling over the debt.

A - Andre Gerdau Johannpeter

And now this is Andre.

Referring to the sale of assets, as of last year, we already announced that we are reevaluating the profitability of the assets. We don't have anything to announce that we are looking into several alternatives and they could be a joint venture partial or total sale or partial sale or shutting down of probably some lines that are not profitable. But there are several alternatives and we are looking into all of them. So maybe throughout the year, there may be an announcement. But currently we have nothing to say. But once again, I'd say that we are working very hard, looking at all of the different possibilities and checking the best possible scenario.

Operator

Ivano Westin, Credit Suisse.

Q - Ivano Westin {BIO 17552393 <GO>}

First of all, I would like to elaborate on the Brazil BO, especially related to shipments in 2016. And what kind of mix you expect to have into domestic and foreign markets and price parity? And if you allow me, I would like you to comment on North America and what is the outlook of price in that region. There was an article saying that you should increase prices in the US by \$30 per rebar by the end of April. Could you please tell me something about this price variation?

A - Harley Scardoelli {BIO 7283603 <GO>}

This is Harley.

First of all, in terms of Brazil BO, it's important to say that in the Fourth Quarter of 2015 our cost was impacted due to the stoppages, we talked about that before. But the bulk of that impact was felt in the Fourth Quarter. There is still very little effects to be felt further on. We see a very challenging situation in the domestic market. So this might effect that. We stopped because we did not want to draw [ph] the production and the inventory, I mean, Brazil has a very volatile market. And I think this is one thing to be said about the Brazil BO. About the North America BO, it's almost the opposite, the basics in the US are still good, we see some good signs. Without speaking specifically about some one-off things here and there, rest assure, then when we see the market is gaining momentum, all players in the market try to recover metal spreads. But North America is a market that always starts the year with a big seasonality.

Q - Ivano Westin {BIO 17552393 <GO>}

Perfect, thank you. I would just like to revisit one point. In the Brazil BO, could you speak about exports number, then indicate an estimated export volume throughout the year?

A - Harley Scardoelli {BIO 7283603 <GO>}

It's complicated to make any predictions, because there is a lot of volatility, issues related to the exchange rate and so we make decisions as opportunities come along. Our Ouro Branco is very competitive, because of our own iron ore production. But there is still a lot of volatility in the exchange rate and we have been monitor price evolution in the market very closely. The outlook is good. But we have to monitor on a case-by-case basis.

Operator

Leonardo Correa, BTG Pactual.

Q - Leonardo Correa {BIO 16441222 <GO>}

My first question refers to working capital and it's addressed to Harley. You had a strong result in working capital. And this has been a constant notice in other quarters of 2015. I have a question about sustainability, I've heard some comments in the press that you still have some room in terms of working capital. So you mean that we will continue to see a drop of inventories in that same magnitude or what kind of expectation in terms of working capital we could have for 2016 in terms of results?

My second question is on CapEx. I think a lot of people worked with BRL8 billion for the year but all of a sudden you come with BRL1.5 billion [ph] CapEx. Your maintenance CapEx, particularly abroad. So how do you profit by this number? Is this close to maintenance CapEx or is way below maintenance? Is it sustainable, can you sustain a similar level into the future or this is just a one-off situation in view of the very challenging landscape?

A - Harley Scardoelli {BIO 7283603 <GO>}

This is Harley.

I would speak about working capital which is your first question. We've been working, first of all, working capital is in that operation. This year, we worked very strongly. And this is something very important in terms of cash generation, I mean, the reduction of working capital and we were very disciplined in that regard. We still believe that there is still some room for further improvement. And this is probably related to efficiencies. So we are putting together a many initiative that will probably allow us to gain a few more day. Possibly, we will not be in that same amount from 2015 but there is still some room for further improvement. We have to be very careful. But there is still some room. If we take BOs like Brazil and North America as we have several mills scattered in the country, we have to be -- to have working capital in a more optimized fashion and we may have further benefits in terms of more reduction. There are still some gains to be captured, maybe not as much as what we had in 2015. But some.

A - Andre Gerdau Johannpeter

This is Andre, Leonardo.

On CapEx, I know that the number was below expectation, BRL1.5 billion. And this is due to three to four things. Number one, all of the large investments that we had are now getting close to the end. There was a heavy plate rolling mill in Ouro Branco, the melt shop in Argentina. And the mill in Mexico that already started up. So with that, we will -- we have room for reduction. And the second point is, the exchange rate factor. Maybe the third factor that I should mention is that probably we are reaching a new CapEx level in view of the current challenging landscape. If we look at utilization is around 65% to 70%. So there is almost no CapEx to increase production. And we have excess production to supply to the market. So there is nothing news that will be large enough to cause any impact. In dollar terms, \$300 million and \$400 million is that what we have for this year and the following years. In reais, we posted BRL1.5 billion.

Operator

Marcos Assumpcao, Itau BBA.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

First question, it's on South America. I would like to understand the sustainability of the margin from this business, it was very strong in the Fourth Quarter. The second question refers to the possible sale of assets and liquidity increase, what would be the main destination of these proceeds, bonus payments, payment of debt or increase in dividend payout or something like that. And as a follow-up, Harley said that, first the First Quarter, the domestic market in Brazil, it's a very challenging market. So the quarter is approaching an end and could you please indicate how much the sales are coming down year-on-year?

A - Harley Scardoelli {BIO 7283603 <GO>}

This is Harley.

In terms of South America, there are a few things to be considered. This region has had been feeling the pressure of prices for quite some time. So this is nothing new. And they are trying to optimize their costs and they've been doing that for some time. There is also the fact that all of operations, not only in South America. But certainly South America margins have also played a role in SG&A. There is a reduction, if we exclude the exchange rate effect, year-on-year was 5%. But if we look BO per BO, it would be closer to 14%. So all of these factors have produced those results, especially if you consider Argentina, Colombia. And Peru. This is something to be said about South America.

Now referring to the second part of your question and in terms of liquidity or investments or cash position, we are focusing on reducing our net debt. Everybody looks at net debt and this will give us more flexibility to pay debt whenever we think it's more convenient and according to the market

situation or we can either improve our cash position. But our intent is to reduce net debt with the proceeds coming from that liquidity event.

So last point related to Brazil and the First Quarter of this year is very challenging. In the First Quarter of last year 2015, our mix was much better. We had stronger deliveries from Brazil and this is not the case in this First Quarter, this is one thing to be said about Brazil and I would just like to add one more thing. In terms of liquidity, we talked about working capital. I would just like to add something to my previous answer, saying that we do see some space for further reductions in working capital. With seasonality, working capital tends to increase in the beginning of the year and then this trend is reversed as the year ends. Operations will consume a bit more working capital and then from the second half of the year onwards there will be a reduction in working capital.

Operator

Osmar Camilo, HSBC.

Q - Osmar Camilo {BIO 17227387 <GO>}

In terms of all of the impairments of BRL6.3 billion, even though I agree with you that this had no cash effect. What called my attention is that most of these write-offs occurred in North American specialty steel BO and most or more than half of these impairments were goodwill and this may impact the future profitability of these businesses. So could you probably tell us what is your expectation for these two BOs particularly North America, which is a BO that is very significant and it has helped mitigate the performance of Brazil. What assumptions were used in the impairment test related to margins, demands, for instance the EBITDA margin of the North America BO which is close to 10%. In the impairment tests, I believe that this margin was not around 10% considering that we had this amount of write-off of goodwill, which is not reversible. Even if the economy improves, you will not see the reversion of that. Could you please clarify that?

A - Harley Scardoelli {BIO 7283603 <GO>}

This is Harley speaking.

One important aspect -- I have a few comments related to the specialty steels for Brazil and North America and specialty steels that separate in the factory impact in North America. Both operations, specialty steels in North America, the goodwill position, especially in (inaudible) in the US in specialty steels. This goodwill which is generated in dollars had a strong impact in terms of growth because of the depreciation of the real. According to our position on September 5, we had more than 40% increase in goodwill mainly due to the exchange rate factor. In terms of the discount of cash flows, we also utilize more conceptual interest rates because we know that at year end, interest rates will be impacted by higher volatility everywhere. So if there is an increase in interest rates, this also impact our numbers. And at the end, this is what the Company to be more cautious, when carried out its accounting write-offs. You have no cash impact. So this write-off was very cautious, because of a higher interest rate and also because of the exchange rate impact on goodwill.

Now about the EBITDA margin in North America, 10% is a goal that you think can be sustainable or you think in terms of working with a lower level. We don't usually give any guidance on that. But we have to utilize a longer-term number. And this calculation is very complex. So that's why I don't want to give you any guidance.

Operator

Alan Glezer, Bradesco Bank.

Q - Alan Glezer {BIO 17508681 <GO>}

I have two questions. The first is about the North America BO. We notice an interesting recovery coming from non-residential construction in the US. And sometimes in areas where Gerdau has a very good presence, very strong presence. What is your expectation for 2016 to take advantage of this non-residential growth considering the increase of steel employed in 2016. So how do you see this opportunity vis-a-vis imports? This is my question number one.

My second question relates to specialty steels. We also notice a significant decrease of 300 basis points in the margin in the Fourth Quarter, how much of this margin compression comes from worsening of the regional situation, we see an increasing participation from Europe and India. Therefore, I want to know whether you can quantify how much of that comes from the regional deterioration from specialty steels? So these are my two questions.

A - Harley Scardoelli {BIO 7283603 <GO>}

(technical difficulty) Alan, I was in the midst of my answer. So I do apologize to those of you who are listening. Let me just answer again. The first part of your question refers to opportunities to take advantage of this growth in the US. In fact, we do believe that our geographic position in the West Coast and in the Midwest gives us a very good position and this gives us also the opportunity to take advantage of this growth coming from the non-residential construction market. So I confirm that we see opportunities and also considering an increase in imports in this market.

Another point to highlight is that, in the infrastructure market, we already see some signs of recovery. And even without saying anything about how long it will take for this market to fully recover, this is a market that benefits from local production as we have in that market. And I think on North America these are the most relevant points.

The second part of your question about specialty steels and the mix, this has nothing to do with India. India is growing and it has posted good growth. But this is more related to our North America BO than where we noticed certain deterioration of margins due to the oil and gas industry in the US.

Operator

(inaudible), Bank of America Merrill Lynch.

Q - Unidentified Participant

Can you tell me how much the iron ore EBITDA was and what would the Brazil EBITDA margin be excluding iron ore?

A - Harley Scardoelli {BIO 7283603 <GO>}

Roy's [ph] question was about the EBITDA margin in our iron ore operation and what would be the margin in Brazil excluding this iron ore business. Our mining operation, I mean, in Brazil, the other results are presented in a consolidated fashion so we do not disclose just the mining business separately, because the business is already contemplated in the consolidated numbers.

Q - Unidentified Participant

So would you tell me how much iron ore EBITDA was for that part of Brazil or not?

A - Harley Scardoelli {BIO 7283603 <GO>}

So you're referring to the EBITDA numbers in absolute terms of that operation, we do not disclose that figures separately.

Q - Unidentified Participant

Okay. You used to, it was helpful. Thank you.

A - Harley Scardoelli {BIO 7283603 <GO>}

It's is true, we used to. But since last year, it's been consolidated in the Brazil BO.

Operator

Tatyana, HSBC.

Q - Tatyana Wolff Katalan {BIO 19222986 <GO>}

I have a few questions. My first question is it would be very helpful if you could provide your current availability on the revolving credit facility. And my second question is that I understood that -- if I understood you correctly, you mentioned that without production stoppages in Brazil, your consolidated EBITDA margins would have been more than 10%. So please confirm that if I understood that correctly. And my follow-up question to that is whether you had any production stoppages in Brazil so far this year. And also whether you expect them to take place in 2016 overall?

A - Harley Scardoelli {BIO 7283603 <GO>}

Your first question was about the availability of our credit line for working capital and how much that we still have available. The second question was about the effect of the production stoppages of Brazil BO. And whether I can confirm the numbers without the stoppages. And the last question was whether the effect of the stoppages will still be felt throughout 2016.

Our working capital line has very dynamic changes, fundamentally basis, the total line is \$1 billion. And we already used about \$300 million meaning that we still have about \$700 million available to that credit line. We can withdraw the money any time we want. Now, answering your second question, yes, I would like to confirm that once we exclude the effects of the Brazilian margin, the margin would be above 10% in the Fourth Quarter of 2015. Now, the third part of your question, if I understood correctly, is that most of the costs incurred by production stoppages we're already posted last year. So we start the year without this effect. So we began the year with a very challenging landscape.

Operator

Gabriela Cortez, Banco do Brasil.

Q - Gabriela Cortez {BIO 18801371 <GO>}

One of our priorities for 2016 is cost reduction. So in what operations we will be able to notice further cost reductions, this year or throughout the year?

A - Andre Gerdau Johannpeter

In terms of cost reductions, we are constantly making efforts to reduce costs. And at the same time, this also depends on production levels and volumes produced throughout the year. And this certainly also depends on the market in Brazil. We have lower visibility due to the volatility of the market and the current macroeconomic landscape. But -- and at last, we have a strong focus on cost reductions. We were able to promote a very strong reduction in costs and SG&A. But this also depends on volumes, which is very difficult to predict today.

Operator

We now conclude the question-and-answer session. I would like to give the floor back to Mr. Andre Gerdau Johannpeter for his final remarks.

FINAL

Bloomberg Transcript

A - Andre Gerdau Johannpeter

On my behalf and on behalf of Harley, I would like to thank you for your interest and your participation. If you still have any pending questions, please go to our IR people. I would like to invite you all to our next conference call on May 4 when we will talk about the First Quarter of 2016. Thank you very much and have a good day.

Operator

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

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