

## Q2 2012 Earnings Call

### Company Participants

- Andre Gerdau Johannpeter, CEO
- Osvaldo Schirmer, EVP
- Unidentified Speaker, Interpreter

### Other Participants

- Carlos De-Alba, Analyst
- Hernato Jusadido Antoni, Analyst
- Humberto Morales, Analyst
- Ivano Westin, Analyst
- Jonathan Brandt, Analyst
- Leonardo Correa, Analyst
- Marcos Assumpcao, Analyst
- Raphael Biderman, Analyst
- Rodolfo de Angele, Analyst
- Thiago Lofiego, Analyst

### Presentation

#### Operator

(Via interpreter) Good afternoon. Welcome to Gerdau's Earnings Call about the results for the Second Quarter of 2012. Currently all participants are connected in listen-only mode and later on we will start the Company's Q&A session. (Operator Instructions)

We would like to emphasize that any forward-looking statement 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 those evaluations.

Here today are Mr. Andre Gerdau Johannpeter, Director, President and CEO and Osvaldo Schirmer, Vice President and IR Director. With no further ado, I would like to give the floor to Mr. Andre Gerdau Johannpeter, please you may proceed.

### Andre Gerdau Johannpeter

(Via interpreter) Thank you. Good afternoon. Welcome to our conference call, Gerdau's results for the Second Quarter of 2012. We will begin our analysis by conducting an evaluation of the world landscape of the steel market and after that we will talk about Gerdau's performance during the Second Quarter and the outlook for the regions where we operate.

After my presentation, Osvaldo Schirmer will give you more details about the financial performance of Gerdau and after that we will be available to take your questions.

It is also important to highlight that in our presentation we will evaluate the performance during the Second Quarter of 2012 and comparing it with the same period of the year before. In addition, we will present some comparative data, comparing to the First Quarter of 2012.

For those of you who follow us on the web, on page two we refer to the world steel production, it the total 390 million tons in the Second Quarter of 2012, in line with the volume of the same quarter last year, excluding China as the world production was 207 million tons, which is the equivalent of same Q2 of 2011 according to the World Steel Association.

In Brazil, steel production total 8.6 million tons, down 7% vis-a-vis the same period of 2011 according to (inaudible) Brazil. Steel production in the other countries of Latin America, not including Brazil totaled 8.4 million tons, which was similar to what was posted in the same period of 2011.

Now referring to steel production in the United States it was up by 8% vis-a-vis the Second Quarter of last year, totaling 23 million tons.

On page three, I would like to refer to Gerdau's highlights pointing out to the Second Quarter of 2012. Gerdau's performance was mainly influenced by higher demand of long skills in the Brazilian market. However we are still experiencing the strong impact coming from higher costs of raw materials used in our operations such as iron ore, coal and scrap.

Consolidated shipments totaled 4.8 million tons, tons which is approximately in line with sales of Q2 2011 and Q1 2012. In terms of steel production we totaled 5 million tons, which was a very stable figure when compared to both periods of this analysis.

Net sales of those in growth of 11%, vis-a-vis the Second Quarter of 2011 totaling BRL10 billion, when comparing that with figures from the First Quarter of the year net sales was up by 8%.

Operating cash generation or EBITDA, there was an increase in the raw material costs as I reported before and that had an impact in our operating cash generation and it was down by 5%, reaching BRL1.2 billion. However, when we compared that with the First Quarter of the year EBITDA grew by 23%.

Net income was BRL549 million in the Second Quarter which was up 9%, when compared to the same period of the year before, mainly influenced by the non recurring financing impact in the Second Quarter of last year due to -- due to early debt payment. When comparing it to the First Quarter the consolidated net income was up by 38%.

Dividends that will be payout to Gerdau SA shareholders will be BRL153.2 million, BRL0.09 per share in payout to the shareholders from Metalurgica Gerdau SA is BRL52.8 million or BRL0.13 per share. Investments in the Second Quarter totaled BRL850 million and year to date it totaled BRL1.5 billion.

On page four, we have the outlook for 2012. I would like to start by giving you a general overview according to estimates from the IRM IMX for the global GDP, which point out to the growth of 3.5% in 2012. There was fuel consumption according to the World Steel should grow by 3.6% in 2012 reaching 1.4 billion tons, which is a lower volume considering what was forecasted earlier. This reduction in the expectation is mainly associated to the slowdown of the economies of the emerging nations, particularly China and also the crisis in Europe.

In Brazil, the Brazilian economy should grow by 1.9% in 2012 according to the focus report and steel consumption according to estimates by Aco Brasil should reach 26.4 million tons, which is 5% more than the volumes posted in 2011.

Civil construction industry in Brazil, the civil construction GDP should experience growth of 5.2%, mainly influenced by investments in infrastructure related to the World Cup and also more stability in the deliveries to the real estate market. It's also important to mention that during the First Quarter of 2012 our sales to the civil construction industry were higher than in the First Quarter of 2011.

In terms of the industry, the industrial production should not experience any growth in 2012, mainly impacted by the deindustrialization process that the country is experiencing.

On page five we have the outlook for North America and Latin America. In North America -- and this does not include Mexico and specialty steel mills. In the United States, we are forecasting good demand for the energy and industrial segment, also agriculture and a gradual recovery of the non residential construction industry. For example, according to the purchasing manager index from the institute for supplied management, the main KPI industrial production in the US was 52.7% everything that is over 50% represents growth.

Another important aspect is the non residential construction investment which represented a growth of 16% in the Second Quarter of this year vis-a-vis the same period of 2011, reaching \$35 billion mainly boosted by more construction of industrial warehouses and commercial buildings. As a result, the IMF estimates that the US GDP should grow 2% in 2012. Steel consumption should be 94.2 million tons or 6% increase when compared to figures from 2011.

In terms of Canada, the GDP growth is supposed to grow 2.1% and steel consumption will also grow 2% reaching 14.5 million tons.

In Latin America, preliminary market studies indicate that we will have positive outlook. Colombia, 4.6% positive and Mexico 3.8% positive growth. For 2012, the Latin American countries except for Brazil should reach steel consumption of 41.5 million tons, which is 6% growth vis-a-vis 2011.

On page six, specialty steels, Brazil, United States, Europe and India. In North America during the Second Quarter 3.8 million light vehicles were produced considering the markets of Canada, the US and Mexico which accounts for 25% growth over 2011. In the segment of high vehicles production was 66,000 units. That means a 7% growth over the Second Quarter of 2011.

For 2012, market estimates indicate there should be a growth of 14% in the production of light vehicles and 8% growth for midsize and heavy vehicles. Brazil, specialty steels and vehicle production we produce 813,000 in the Second Quarter, which was down by 8% vis-a-vis the same period of 2011.

Now comparing to the First Quarter of 2012, this volume accounts for an increase of 10% and this is already an impact of the government incentives to boost the acquisition of automobiles starting with a reduction in interest rates and IPIs according to ANFAVEA the production of light commercial vehicles in the country should grow by 4% in 2012, reaching 3.2 million units. However, when it comes to heavy vehicles, the estimate is that it should be down by 16% in terms of production volumes.

In Europe, in the Second Quarter of 2011 vehicle registration experienced a decline of 6% vis-a-vis the same period of the year before, reaching 3.3 million units. In the other segment of light commercial vehicles, the production of 453.7 thousand tons which is a 12% reduction vis-a-vis the last quarter of 2011 and this is already a reflection of the European crisis.

Now, we will talk about investment on page seven, our investment plan and despite all the uncertainties in the world economic market, we are still maintaining our investment plan of BRL10.3 billion for the period between 2012 and 2016. However we are being more selective when it comes to evaluating projects and more flexible in our disbursement schedule taking advantage of the opportunities in the market where we operate.

In Brazil, we will still work in the operation of the coiled hot roll switch rolling mill at Aco Minas Gerais that should start operations at the end of 2012 with installed capacity of 770,000 tons a year and this equipment is suitable to serve the oil -- the demands coming from oil, naval and civil construction industries.

Heavy machinery as well like machinery and inputs. And this mill will also serve the plant for heavy plates rolling mills that should be in operation by 2014. We are still proceeding with the investments that have been announced to reach self-sufficiency in iron ore, we want to reach 11.5 million tons of annual installed capacity by 2014 and we are also moving on with the project to -- for commercial exploration of -- the surplus output of iron ore.

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Today we are also announcing the reinstatement of a project for BRL1.1 billion for the construction of a new mill in Mexico by means of our joint venture. We will have annual installed capacity of 1 million tons of steel and 700,000 tons of iron ore. This will help us replace imports and operation should initiate in the Second Quarter of 2014.

In India, our joint venture, Gerdau/Kalyani will start in August, the operation of the blast furnace where the reproduction capacity is 350,000 tons. In the same period, we will also initiate the operation of the energy generation plant for 6 megawatts and in the second phase of the investment we will also initiate our new rolling mill for specialty steels.

We've installed annual capacity of 300,000 tons. In addition, we will continue with deployment of a coke plant with an annual capacity of 300,000 tons and integrated to this plant we will also have an energy generation plant for 15 megawatts.

Now, my final comments and I would like by saying that this growth that we experience in terms of net sales, EBITDA and net income in the Second Quarter when compared to the First Quarter clearly demonstrates the recovery of our financial and operating performance in this half year and this really reflects an improved demand and improvement in our operation management.

As we said before, we also experience a challenge in increasing prices of raw materials. Adding to that, we also must consider the deindustrialization in the steel chain in Latin America and in Brazil we have other things that affects that so called business costs with high interest rates in as such synergistic systems, high cost of energy and a very high tax burden on payers. So, still have a lot of challenges ahead.

In view of a global landscape of volatility with the slowdown in the economies of emerging countries, Brazil, China and India and also the European crisis, our challenge is to continue to search for improvements of our operating margins, beginning with the continuous improvement of our cost management and in strategic projects. The introduction of the mining product and the trading of flat products in Brazil and also the development of our joint venture in India.

To conclude, I would like to inform as was recently announced, that Schirmer is retiring from his functions as August on the 31st of this year. So therefore I would like to thank Schirmer for his excellent performance during his 26 years at Gerdau, for the position of Senior Vice President of Finance and Controllershship currently taken by Schirmer. The Company appointed Andre Pires de Oliveira Dias, the current CFO for long steel operation in North America. He will also join Gerdau's executive committee.

Now, I will conclude -- I conclude my presentation, I'll give the floor to Schirmer who will then proceed with the financial outlook and after that we will proceed with Q&A. Thank you.

**Osvaldo Schirmer** {BIO 1754610 <GO>}

(Via interpreter) Thank you, Andre, very much for your kind words and good afternoon to you all. I would like to start by our consolidated results and then I will talk about our business operations and finally about our capital structure.

So, please take slide number nine, which shows our accounts in a comparative of the Second Quarter of 2012 for the first column and the second of '11 in the second column and then the half yearly numbers as you can see.

The consolidated sales revenue in the Second Quarter of 2012 was BRL10 billion, BRL965 million more than in the Second Quarter of 2011. That 11% of positive variation as you can see in the second bar of the EBITDA. The increase in the net sales is due because of the greater net revenue per ton sold in all these business operations, which is very important.

The cost of sales in the Second Quarter, 2012 was BRL944 million, the third bar of the chart showing an increase of 12% vis-a-vis the Second Quarter of 2011. The largest cost of sales was a reflection of the higher costs of raw materials and these increases they tell us the growth of a net sales but thinking about a reduction of the gross margin.

Now, if you look at this -- this Second Quarter compared to the last years it was important, there was an important difference regarding the expenses with general and administrative expenses, even with the slight increase of the absolute value which is the fourth bar of the graph or the chart will share regarding the net sales, shares of reduction in the Second Quarter when compared to the Second Quarter of 2011 due to the great growth of the net revenue in the period and in the last quarter should be about 6% of the net sales.

The EBITDA in the second semester -- or in the Second Quarter was BRL1.2 billion a drop of 5% vis-a-vis last year at the same time -- lower EBITDA 12% against 15% in Second Quarter 2011 and this reflects the increase of the raw materials cost.

And on the other hand, in the Second Quarter 2012 compared to the first the EBITDA increased 23%. So, a negative financial result in the Second Quarter, negative when compared to the Second Quarter of 2011 stands particularly because of the exchange rate variation, BRL157 million, BRL800 million of debt taken in Brazil and it is important also to mention -- that we have mentioned with regards a non recurring debt of BRL70 million when we have to bring forth our interest rate swaps. So -- and we cancelled then the swap and this brings about this difference between the two quarters.

The consolidated net income of 2012 showed an improvement vis-a-vis the second of 2011 because of neutralization of the exchange rate variation, to which I have already referred about the debt taken in foreign exchange, as I have mentioned, which did not occur before. And year to year, the Second Quarter it has increased 9%.

If we look at the Second Quarter this year compared to the first we show a good recovery growing 38% in net income.

Now on slide 10 we have done business operations. First of all the Brazil business operations. The sales volume in the Second Quarter reached 1.9 million tons, a drop of 2% over the Second Quarter of 2011, of which 74% about 11.4 million tons come from the domestic market as you can see on the chart to the left.

The sales in the internal market increased 10% vis-a-vis the Second Quarter 2011, a result of the good demand of long steel for civil construction. The sales -- the net sales reached BRL3.7 billion in the Second Quarter 2012 as you could see in the chart to the right. At this moment, the increase of the domestic market was the main factor which lead to the growth of net sales.

And this business operation contributed with 36% of the consolidated net sales for the Second Quarter and EBITDA was BRL589 million in the Second Quarter 2012. And this is comparable to the First Quarter, it was a growth of 43% and a margin going up from 14% to 16%.

North America, slide number 11. American growth there was a reduction of 5% in the volumes sold into the Second Quarter 2012 compared to the Second Quarter 2011. The drop in the sale of long steels made the reflection of the early demand of the First Quarter 2012 because of the seasonal variations and early demands.

The winter was much more mild and the First Quarter 2012 showed a greater volume of sales since the beginning of the crisis in the United States as we have already said and excluding the seasonal factor, we conclude that there is a continual good demand of the industrial sector and that of energy and the gradual recovery of the non residential sector.

And as far as numbers go, the net sales in the Second Quarter 2012 reached BRL3.2 billion, 18% higher than last year as you can see on the chart to the right. The growth was a result of the growth of net sales per ton sold and this business operation contributed with 31% of consolidated net sales for the quarter.

EBITDA in the Second Quarter '12 was BRL328 million, slightly below that of the Second Quarter 2011 because of higher costs, more general and administrative expenditures and less equity income. So the EBITDA margin was 10% in the Second Quarter compared to 13% in the Second Quarter of 2011.

Slide number 12 in Latin America. Sales reached 685,000 tons and you can see on the chart to the left that 6% above the sales of 2011 especially for Peru and Chile which reflects strong demand from the construction sector in these countries.

The net sales were BRL1.3 billion compared to BRL958 million in the Second Quarter of '11 as you can see in the chart to the right, showing a growth of 33% due to the better net sales per plant. And better price and better volumes. This business operation accounted for 13% for the consolidated net sales of the quarter. Cash generation was BRL70 million less than last year due to higher costs, more general and administrative costs and less equity income. The EBITDA margin on the other hand showed a drop going from 13% in the Second Quarter of '11 to 5% in the Second Quarter of 2012.

Specialty steel, slide number 13. In this business operation a drop of 8% in the sales volumes in the Second Quarter when compared to the Second Quarter of '11, a drop of 8% therefore because of a lower demand in the Brazil and Spain units.

In Brazil, we still have the effect of the earlier demand of heavy vehicle production at the end of 2011 because of a new regulation called Euro 5 for diesel engines which came into force in January of 2012.

Spain, on the other hand, has lower sales because of the effects of the European crisis now in the comparison with the First Quarter of 2012, the sales of specialty steel as those units in Brazil show a growth influenced by the recovery of demand because of the government incentives given to the automobile sector and the First Quarter compared to -- the Second Quarter of 2012 compared to the First Quarter of Second Quarter in 2012 shows then a growth.

Net sales showed a growth of 2% showing -- for BRL2.1 billion as you can see in the chart to the right because of the greater net sales per ton. Sales which offset the reduction of the sales volume, this via Brazil accounted for 20% for the consolidated net revenue in the quarter, the EBITDA 2012 was BRL362 million, practically equal to the Second Quarter '11 and EBITDA margin 17% and the comparator for the First Quarter, the margin goes from 14% to 17% and the absolute value of cash generation grows 13% quarter to quarter.

Some considerations about the country's liquidity and indebtedness, slide 14. Net debt from December to June increased 29%. Gross debt reached 19.9% with a BRL3.2 billion in cash, we had a net debt of BRL11.7 million in the comparison which is a consequence of cash reduction and also an increase of the gross debt.

Cash reduction occurred, particularly because of the payment of debts which ensued in the First Quarter of 2012 and the need for more working capital because of greater activities in the period and also because of greater CapEx. From this cash 27% was held by Gerdau companies abroad particularly in America dollars.

And the gross debt compared to the June 2012 was broken down into 20% in reals, 48% in foreign currency contracted by companies in Brazil and 32% in different currencies contracted by subsidiaries abroad. From the total of debt, only 20% was short term and 80% long term.

Gross debt when compared to 31st of December 2011 showed an increase of 9%, particularly because of the exchange rate effect which occurred in the Second Quarter 2012. 59% of the gross debt originates to the capital markets, debentures and bonds. The weighted nominal average cost of our gross debt on the 30th of June of 2012 was 6% -- 5.9% to be more specific. And of this 7.3% was for the amount taken -- denominated in reals plus 5.7%, plus exchange variation for the total denominated in dollars taken in Brazil and 5.6% was the amount taken by subsidiaries abroad.

The debt payment schedule, as you can see, on the upper chart to the right shows a comfortable situation for the next years vis-a-vis available cash and the prospects of cash



generation for the Company. At the end of June the average term for debt payment will be six years -- or was six years.

The financial cycle, which is working capital divided by the daily net sales of the quarter in June 2012 showed an increase of four days vis-a-vis March 2012. These increases stem from the growth of 13% more of working capital because of the effect of exchange variation on inventories and receivables abroad compared to the increase of 8% in the net sales in the Second Quarter 2012, compared to the First Quarter 2012.

I'd like to conclude saying that Brazil has done everything to keep its capital structure in the best shape possible, vis-a-vis the world economic scenario and we will continue to work to improve our cost management and will be very selective in our strategies always trying to improve our operating margin as Andre has already mentioned.

So we believe that Gerdau will continue to stand out among its peers in the market and receive the attention of our investors. So, now we will go on to our Q&A session. Thank you, very much.

## Questions And Answers

### Operator

(Via interpreter) Thank you, very much. (Operator Instructions) Our first question comes from Ivano Westin from Credit Suisse. You may proceed.

#### Q - Ivano Westin {BIO 17552393 <GO>}

(Via interpreter) Andre and Osvaldo good afternoon and thank you for the call. Congratulations for the results, particularly the Brazil operations. Would you talk a little bit please about your market vision, the demand scenario and compared Brazil to United States, especially in the second half of the year and with these price increases which were announced for July whereas before plants in Brazil and what do you expect from the government in the incentives for the rest of the year?

Second question is about monetization and can you give us a guidance as to when you will announce this to the market and if there is no agreements about evaluation with possible strategic partners, do you -- will you develop the budgets without the participation of these strategic partner.

#### A - Andre Gerdau Johannpeter

(Via interpreter) Good afternoon, Andre. Well about the scenario, what we can see I'll talk first about Brazil. So long fields and civil construction generally speaking with the residential or commercial building are not looking good. We will have many -- a lot of construction for the World Cup and this is only to help occurring. But in other fields we will not have so much goods and this has been effected by the reserve cost and competitiveness and the deindustrialization.

So, Brazil will develop into more construction but not so much in the industrial sector and there might even be a slight drop according to the data which has been published.

If we take -- well, you were asking about government incentives. The government has made -- taken some steps. The automobile sector has had a reduction the IPI. The government has said no that other incentives might come along and energy -- where energy sectors might be favored and we do see this favorably.

The steel sector and all the steel chain what would help if we were more competitive? So we have nothing specific as yet but there are some prospects and we have heard of things. And regarding price, I will not say anything specific. Plus we will secure in different regions it depends on clients and regions but I don't have any specific point that I'd like to discuss.

We'll see when the world a pressure in the spot markets regarding more materials but if there are some operations or markets which produces some forms we see questions whether margins or places where the margins are very tight indeed. Rodolfo.

### **A - Unidentified Speaker**

(Via interpreter) Sorry it wasn't Rodolfo, it was Ivan.

### **A - Andre Gerdau Johannpeter**

Regarding the mining, we talked to the press about this this morning we are in the second phase of what -- or the first phase was to interview candidates or companies in Brazil and the United States and Europe and Asia so refer so incumbent to receive proposals online and we are now in the second -- or the second phase, we would do diligence, management presentations and now we're in the second phase, we're in that phase from now on as those pages are processed then the binding offers will come in.

And you also ask well if the proposals received are not acceptable and according to the Company's expectations we will carry around with the project on our own. It's difficult to answer that question. There is a lot of interest, there is a unanimous recognition by all those interested to those working on the project but the quality of our mines is above the average of the market and we are considering going alone. But let us see what is going to happen.

### **Q - Ivano Westin {BIO 17552393 <GO>}**

(Via interpreter) Thank you, very much Andre.

### **Operator**

Our next question comes from Mr. Rodolfo de Angele from JPMorgan. You may proceed.

### **Q - Rodolfo de Angele {BIO 1541593 <GO>}**

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(Via interpreter) Good afternoon, Andre. This is Rodolfo speaking now. I would like to ask you if you could say a little bit more about the project. The Mexican mill and a little bit about the technological route that you've chosen. Have you chosen something along the lines of -- what lines have you taken. And also, as for unions you always had a lot of rain there?

And in the Second Quarter of last year were things better than the third? Well, could you just elaborate on that please?

### **A - Andre Gerdau Johannpeter**

Hello, Rodolfo, this is Andre. About Mexico, this joint venture with our local partner, 50/50 and the route is an electric furnace, 600,000 tons of world products and 700 million tons of steel. So, that's the Mexican project.

And now Schirmer will take over.

### **A - Osvaldo Schirmer {BIO 1754610 <GO>}**

(Via interpreter) You asked whether the rain affected the steel sector in three of the -- in First Quarter, did it continue to affect the region in this Second Quarter? Well, at the beginning of the Second Quarter it was still bad, the impact of the rain that we had at the beginning of the year but we managed to recover our production level. This did reflect in the new costs but this was not long lasting.

### **Operator**

(Operator Instructions) Our next question comes from Mr. Carlos De-Alba from Morgan Stanley. Please, Mr. Alba, you may proceed.

### **Q - Carlos De-Alba**

Yes, thank you very much gentlemen. My questions are regarding the India project. Could you tell us how much the CapEx will be and signing for that. And second, also on the growth volumes, it seems that you are now more flexible in terms of the projects that you may be going ahead with as well as the timing of those projects. So if you could prioritize for us what projects will be more important as you go either in terms of -- go ahead and also in terms of timing. Thank you.

### **A - Unidentified Speaker**

Problem in the line, if you could speak a little bit louder it would be much easier for us to understand. So interpreter and the mediator please ask him to repeat the question.

### **Operator**

Sir, could you please repeat the question.

Bloomberg Transcript

## Q - Carlos De-Alba

Sure, my question is regarding the Indian project, how much is the CapEx for stage two when you're going to put the rolling mill and (inaudible)? And second question is regarding the flexibility that you highlighted in terms of your CapEx plans, what projects would be a priority for Gerdau and where would those take place in case you need to reduce the total amount of CapEx that you have planned for the next few years?

## A - Unidentified Speaker

First of all, I would like to ask the gentleman to repeat the question because I think the question was around two issues, one referring to our CapEx schedule and what are the priorities. And I think he wants to know a little bit more about the second stage of our CapEx in India.

And I would say that vis-a-vis our CapEx program, we will fix the BRL10.3 million, which has been scheduled for the next few years which is one point some building a year and there is a very selective evaluation schedule of our investment. So in terms of the Acominas rolling mill or coil hot rolls strip rolling mill should be concluded at the end of this year and a rolling mill for heavy plates will be ready by 2014. So these are the priorities and as announced before by Andre, we have Mexico with structural shapes rolling mill for 70,000 tons. So these are the priorities.

Now, in terms of the more specific CapEx in the second stage of the plans in India, we have to give you that number later on because we don't have that available for 300,000 tons a year as the market already knows and followed by investment in the rolling mill. But we can resume -- we can go back to the question later on. Thank you.

## Operator

(Operator Instructions) Our next question is from Hernato Jusadido Antoni [ph] from Sol Coratheda. You may proceed sir.

## Q - Hernato Jusadido Antoni

(Via interpreter) Good afternoon. And thank you for the call. The first question is concerning specialty steel figures for the second half of the year. In Brazil how do you see the demand landscape currently and we've heard that there will be lower production of heavy vehicles. So what is your expectation in terms of the volume for specialty steels in Brazil in the second half of the year when compared to the first half of the year.

And the second question relates to a possible extension of your iron ore planned and logistics. I think you also said it's here that there are several alternatives about that and I would just like to understand it better because I know that Gerdau has always been very careful in terms of controlling all of the links of this chain in terms of (inaudible). And logistics for iron ore and certainly that is depending on contract terms. Should we see Gerdau adopting the use of outsourced ports to ship your goods?

## Operator

Ladies and gentlemen, please remain on the line.

### A - Unidentified Speaker

(Via interpreter) I do apologize there was a problem with the connection, it was mute and I was not aware of it.

The question related to the mining process and you also asked us about the logistics system and I was saying that logistics account for road transportation. Gerdau is already negotiating things with MRF Logistics, we anticipate to them what is the expected volume and this is absolutely under control.

The second part of this issue refers to the ports in our project we already contemplated the construction of a port. We already received a license for that construction and there is also the (inaudible) to use existing port facilities. So we are working with these two alternatives.

### A - Andre Gerdau Johannpeter

(Via interpreter) It's Andre now, the second question was about Brazil and the outlook for the country.

I would like to begin by referring to civil construction which is a segment that still presents increasing demand. In the civil construction industry, we are still building a lot of instant structure projects, highways and ports and we see some BPP in the port authority area, all of the stadium for the soccer cup so the build and rebuild. So, in general, the landscape is very positive and it's a landscape of growth. So, commercial construction and light construction is still growing as well.

Looking to the inventory side, things are not so good, especially in terms of imports and machinery, competitive -- the competitive environment is increasing so growth should be zero or close to zero.

In terms of vehicles, what do we see more particularly? There was a move in terms of trucks because of Euro 5, the industry experienced a significant decrease but we see some recovery coming for the second half of next year and we will see the pickup of sales of trucks.

Input, there was a reduction in consumption, increases of inventories in the Third Quarter and the government came up with some tax incentives and we are now experiencing the results. July experienced one of the best sales of light vehicles and this will certainly help the industry to clear their inventory and according to future projections, sales of vehicles should grow still by 4% not only due to a government incentive but also economic growth and increases in family household income.

There was a reduction in the projection for GDP. They -- once we call it 3%, now 1.9%. But depending on the industry, we will be able to see different growth levels and this is the case of civil construction and steel.

## Operator

Our next question comes from Leonardo Correa from Barclays. You may proceed.

### Q - Leonardo Correa {BIO 16441222 <GO>}

(Via interpreter) Good afternoon. The first question has to do with costs. Could you quantify or each give us an idea of the price of scrap. We were seeing scrap prices dropped, for example, in the United States and here in Brazil there are some signs saying that the price has also dropped in the last few weeks. So, I'd like to know if you -- if you have felt this as well and it would be interesting if you could let us know. First question.

Second, the investments in Acominas in the hot rolling mill, could you elaborate on this investment and maybe Schirmer could tell us what the cost of transformation is. The mix of the Company will obviously improve in the next few months and also 2013. So, maybe you could tell us what will improve or give us a parameter to transformation costs. That would be interesting. Thank you, very much.

### A - Andre Gerdau Johannpeter

Well, this is Andre speaking. Regarding scrap, ever since the beginning of the year there has been a tendency to a reduction of the price of scrap in the global markets and also of coal and of ore and this in Europe and reflects in the United States the largest exporter as well and this influences other markets.

However, what we do see is what we will see in the second half of the year will not be rebound but might be an increase of these prices in some markets because most of the producers have stopped buying or cut down in the buying of the scrap and apparently it has reached a price where probably will not be recovering now in August and saw it coming up again. What is more important for us is to keep the spreads, not only whether the scrap is going up or down. But to maintain our spreads and in North America we have managed to do that. And that's important. And also there for other markets.

And you have asked about hot rolling steel mill and operating costs and CapEx. Well the CapEx we have already published it several times, with projects of the rolling mill and the heavy plates rolling mill is BRL2.4 billion.

You asked about the operating costs of the transformation costs. We generally don't talk about our costs. But I could say with our equipment makes us very comforted that it's extremely competitive and it is based on very modern technology so all our indications show that it would be competitive with -- on the competitors in this section.

### Q - Leonardo Correa {BIO 16441222 <GO>}

Thank you, very much. Could you tell us, Andre what the current level of the scrap is? And in the United States as well?

### **A - Andre Gerdau Johannpeter**

About \$450, 460.

### **Q - Leonardo Correa** {BIO 16441222 <GO>}

Thank you.

### **Operator**

(Operator Instructions)

Our next question is coming from Mr. John Brandt from HSBC. Please, Mr. Brand, you may proceed.

### **Q - Jonathan Brandt** {BIO 5506998 <GO>}

Hi. Good afternoon, thank you for taking my question. Two questions, first is related to the previous question, just on the spreads. With the expectations that scrap prices in the US are set to rise as we said the second half and with demand being a little bit weaker than what you had expected in the Second Quarter, do you think demand will rebound sufficiently enough for you to increase your volumes and keep those spreads and see some margin expansion in the third and Fourth Quarter. Or do you continue to see margin pressure maybe around the 9%, 10% level for the rest of the year?

And secondly, you mentioned in the press release that you're still looking to take advantage of opportunities that emerge in the marketplace. I read that to mean M&A. Is there anything at the moment that seems interesting to you and I'm thinking specifically about CSA and Brazil or Sparrows Point in the US. Those are my two questions. Thank you.

### **Operator**

Ladies and gentlemen. please remain on the line.

### **A - Andre Gerdau Johannpeter**

Well, to answer the question about scrap, whether there'll be a rise or not in the Third Quarter and as it happens what will happen to the margins? We have seen sometimes that it might go upwards. Very difficult to be specific, to know what the balances of scrap will do.

But as the world's market has been dropping in the last few months and many buyers have stopped or reduced their inventories, there is a possibility of a rebound of the crisis of the producers come back to purchase. But this is speculation in the market and we can certainly -- have no certainty. The important thing for us is to keep our margins. So we'll maintain our margins in the second half of the year in general.

And then there is the second question which Schirmer will answer.

### **A - Osvaldo Schirmer** {BIO 1754610 <GO>}

(Via interpreter) Whether we group on the M&A group will be interested in the -- talking to (inaudible) and somebody here in the group said that this question might have to do with our release where we still talked about market opportunity.

So, (inaudible) company in the United States have mentioned and we are not -- none of these two projects are official. Neither the (inaudible) TOC and our release talked about market opportunities to direct our investments and prioritize our (inaudible) next investments to take the best opportunities in the market.

Thank you, (inaudible) to answer.

### **Operator**

(Operator Instructions) Our next question comes from Thiago Lofiego from Merrill Lynch. You may proceed.

### **Q - Thiago Lofiego** {BIO 16359318 <GO>}

(Via interpreter) Good afternoon, Andre and Schirmer, thank you for your questions. My question has to do with CapEx and could you give us an idea of how much you have spent regarding this budget and you talked about BRL2.2 billion for the HIC. And what is your expectation in terms of plans for the next few years? Will you -- and what about the sales mix for the project? Will it be from Mexico there when will be distributed or will part of this be for your -- for exports? That's my first question.

### **A - Andre Gerdau Johannpeter**

This BRL2.4 billion of CapEx total, we are not breaking down this number in equipment. But the spreads also are important. It's difficult to separate this number. This project we will be concluding at rolling mills and have it we've already said then heavy mills -- heavy plate is being built. It's difficult to estimate. We don't have the exact number here. But about 60% has already been spent. So we can get back to you on that.

About the mix of this project it's important to understand we want to always have the learning curves and increased output particularly on the first part of the year and then it will reach its peak in a second year.

We will focus on the domestic market and domestic according to opportunities. And further on, for the second go around, we will focus more on the domestic market as soon as we have new clients and supply in the domestic market.

However, in our project there will be a good export percentage, because have markets in North America, we have the opportunity to sell also outside results. So its first of all

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exports to the domestic markets or domestic markets or also export to Latin American countries.

**Q - Thiago Lofiego** {BIO 16359318 <GO>}

(Via interpreter) You said 60%, which referred to the BRL2.4 billion as of all.

**A - Andre Gerdau Johannpeter**

Yes, more or less.

**Q - Thiago Lofiego** {BIO 16359318 <GO>}

My, second question complements the first one of when I asked this question about mining, do you have the timing regarding these down (inaudible) offers in the next three to six months perhaps?

**A - Osvaldo Schirmer** {BIO 1754610 <GO>}

(Via interpreter) Well, this is Schirmer, as I have always said in this other offer, we are in the second phase of due diligence, management presentations, et cetera. Therefore, once this sales is up of potential investors which is important, there are interested parties in the United States and Europe and others in Brazil where we have come to make the offers. It is difficult to set aside a date. This will be result of negotiations. We have scheduled with (inaudible) that we are within our schedule. It'll be very difficult to specify the date exactly.

**Q - Thiago Lofiego** {BIO 16359318 <GO>}

Thank you, Schirmer.

**Operator**

Our next question is from Marcos Assumpcao from Itau BBA, you may proceed.

**Q - Marcos Assumpcao** {BIO 7474402 <GO>}

Good afternoon. I have two questions, the first related to the pricing landscape in 2013 in the domestic market. Could you tell me something about new price increases early next year due to the end of the government incentive steelers exports and whether you could draw a parallel between longs and short steels?

Which market you believe they will be further possibilities to increase prices and the second question relates to the Brazilian operation, it was clearly -- it was clear to me that you had a recovery in your margin then there should be further recoveries when certainly the demand in Mexico also picks up. Could you please give me your outlook for margins and EBIT in the long run, please for the long market?

**A - Andre Gerdau Johannpeter**

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Good afternoon, it's Andre. In terms of pricing and forecasts, considering that we have a mix of different products and so on and so forth, this expectation according to resolution 72 that terminates all of the incentives for the courts must help in the competitive landscape of the industry. But it also depends on the Mexican market, foreign exchange.

There are many aspects that influence pricing, not only that resolution. That's why at the moment it's very difficult to do any kind of forecasts and I am mostly referring to longs. While flat steel is still too early to say, we will start rolling at the end of the year so it's still too soon to talk about flat steel.

And the second question, I will give it to Schirmer.

### **A - Osvaldo Schirmer** {BIO 1754610 <GO>}

Marcos, your question about the pricing landscape and margin recovery in 2013 or even till the end of this year considering EBITDA margins etc. We do not give out guidance as you well know. We just talk about what we will produce. We are working very hard to decrease and optimize our working capital as we mentioned before.

We have growing volumes of supply of iron ore and this adds up to our efficiency performance. We are almost self sufficient. We are also working hard to replace coal exports bringing more coal exports, bringing more coal from Colombia to Acominas. We always invested except for the particular year of 2010.

There is a guideline from the Company that is very clear to management that we must improve costs and at the same time improve efficiency.

It's difficult to anticipate any pricing scenario but whatever we can do internally we will do and we believe that we will continue in that effort to interest margins. But I will -- I do not want to say anything about at what level. Thank you, very much.

### **Operator**

Our next question is from Humberto Morales from Goldman Sachs. You may proceed.

### **Q - Humberto Morales** {BIO 17178450 <GO>}

(Via interpreter) And Marcelo. Thank you for this opportunity. Schirmer, I wish you all the best in your new life. I think I will miss you a lot. Now, going to my question, most of my questions were previously answered. But in terms of Cosigua, I think -- I don't know whether I understood it quite well. Whether you were -- what is the position of Cosigua and how is that project moving along and what about the start up in CapEx.

The other thing is whether you could -- I mean I know that you don't give five year CapEx. But I think you already have a budget for next year so what would be the annual CapEx and when do you expect the rolling mill to operate? Would it be by the end of 2013, early 2014?

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## A - Andre Gerdau Johannpeter

Marcelo, this is Andre. Okay, let me answer the first part of your question CapEx. You refer to priorities that maybe we didn't mention Cosigua our CapEx plan was maintained and this in a way is geared towards adding value. So it is Cosigua rolling mill in Rio, the other one for (inaudible) steel in Sao Paulo, the flat rolling mill.

So we will use those two capacity to add value and start rolling. So when we say that we will be more selective in terms of where we will use investments. So that's what we will use it for. These projects and these are the projects that will get our focus.

In terms of the annual CapEx, we do not disclose these numbers. But maybe we can take the five year figure and divide it in five years. So I think it's BRL12 billion a year when there is more in Acominas it goes up a little or less in Acominas it goes down. Now, we have the flat rolling mill in Acominas.

And for the second part of the question, Schirmer will answer that.

## A - Osvaldo Schirmer {BIO 1754610 <GO>}

In fact, the question referred to the utilization of the coil hot strip rolling mill and what it reaches 100%. You know that there is around that process, a learning curve that has to be followed and we do believe that in the first year maybe 50 to 60% of the rolling capacity of that rolling mill will be the case going towards 100% in a year or a year and a half. I think this is our internal expectation.

## Q - Humberto Morales {BIO 17178450 <GO>}

If I am allowed a second question related to government incentives and the decrease in your payroll, I know that Gerdau is working and discussing that issue with the government. Could you please mention what impact is expected in terms of the government measures?

## A - Osvaldo Schirmer {BIO 1754610 <GO>}

It's difficult to specify but in general maybe I am now speaking as a representative of the entire steel industry. We are working with the government towards reducing the tax burden so that we could be more competitive and whenever we talk about lowering the tax burden or lowering the impact of the tax burden on the payroll, half of the cost comes from taxes.

These are issues that the entire steel industry is arguing or debating it with the government. We are trying to lower the tax burden because when the tax burden is lower we could be more competitive. And then we would be able to invest more in logistics, infrastructure, interest rates are still very high in Brazil and the exchange rate despite the fact that its around two something.

In our view it's relatively low. It could be higher than that to help the industry to be more competitive. So we are working towards lowering the tax burden, because at the end,

what we want is to dupe demand for steel in Brazil because it is still very low when compared to the consumption of other countries which should be around 400,000 kilograms.

I've also forgot to thank you for your good wishes for my next phase. So thank you very much.

## Operator

Our next question is from Raphael Biderman from Bradesco BBI. You may proceed.

### Q - Raphael Biderman {BIO 1529743 <GO>}

(Via interpreter) Good afternoon. I would just like to -- like Marcelo, wish you the best of luck in your next phase. I speak on behalf of my colleagues on the buy side because we all know that you've been a source of great inspiration to all of us. You are a model executive not only in Brazil but through all of the Americas.

Now, I have a question about the LBQ rolling mill and whether when it starts to operate you will continue to export semi finished. Could you give me a guidance about the percentage of products or whether you export more than in the internal markets and what are the exports of BQ in the beginning and the first few years and if you could mention a technical characteristic that maybe you maybe could bring any commercial advantage PVC.

### A - Unidentified Speaker

He's referring to PVC.

### A - Osvaldo Schirmer {BIO 1754610 <GO>}

Thank you, Biderman. It was -- thanks very much for your good wishes. It was very kind of you. Thank you.

Now, in terms of your very specific question about the BQ rolling mill and how much of it will be able to place it in the domestic market and how much we will have to export, this is -- I must say that we will still have products to be exported as semi finished. We are talking about an 800,000 ton a year rolling mill on year one there will not be a ramp up, there will be a learning curve still in process, maybe in the first year.

We may reach 50% of output. We have a very good distribution capacity in Brazil which is assuring. But we will place part of the production in the domestic market and part of the output in the foreign market. As we get more productivity, we'll try to increase the output to the domestic market in terms of the steel volume that we'll still be geared towards being to the other rolling mill, we will still have to export semi finished products.

In terms of volume, it's difficult to say anything at the moment. We have an idea of how much -- at what level we want to operate and we will operate with these two markets, the

surplus of steel and semi finished.

**Q - Raphael Biderman** {BIO 1529743 <GO>}

(Via interpreter) But when you have the heavy plate you will not have semi finished anymore, right?

**A - Osvaldo Schirmer** {BIO 1754610 <GO>}

Well, there will still be some left over. We -- there will still be some steel left that will be sold one way or another.

**Q - Raphael Biderman** {BIO 1529743 <GO>}

Thank you.

**A - Osvaldo Schirmer** {BIO 1754610 <GO>}

Thank you.

**Operator**

Due to our time we will now close our Q&A session. I would like to ask Mr. Andre Gerdau Johannpeter to make his final remarks.

**A - Andre Gerdau Johannpeter**

I would like to thank you all for your attention and your interest. To thank all the analysts and all who tuned in and we hope to meet you at the next quarter call and thank you for all those who wished Schirmer his good wishes.

**A - Osvaldo Schirmer** {BIO 1754610 <GO>}

Schirmer is speaking now. Thank you, very much for your participation and we with the investor relations are always available to answer your questions and complement your question if we were not clear.

**A - Andre Gerdau Johannpeter**

And Schirmer will still be with us at the next call on the 1st of November. And I would like to invite you all for the Third Quarter results. Thank you, very much and thank you for tuning in.

**Operator**

Gerdau's call is now completed. Thank you, very much for your participation and have a good afternoon.

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