

## Q2 2020 Earnings Call

### Company Participants

- Alberto Ono, Investor Relations & Corporate Planning Vice President Officer & Member of the Executive Board
- Miguel Homes, Commercial Vice President Officer & Member of the Executive Board
- Sergio Leite de Andrade, CEO & Member of the Executive Board

### Other Participants

- Carlos De Alba, Morgan Stanley
- Daniel Sasson, Itau BBA
- Gabriel Galvao, Credit Suisse
- Thiago Ojea, Goldman Sachs Group

### Presentation

#### Operator

Okay. Alberto Ono, Finance Investor Relations and Corporate Planning Vice President Officer; Mr. Americo Ferreira, Industrial Vice President Officer; Mr. Kohei Kimura, Technology and Quality Vice President Officer; Mr. Miguel Homes, Commercial Vice President Officer; Mr. Carlos Rezzonico, Managing Director of Mineracao Usiminas; Mr. Ascanio Merrighi, Managing Director of Soluções Usiminas; Mr. Atur Takaki, Managing Director of Usiminas Mecanica; Mr. Bruno Paulino, Head of Legal Department; Mr. Julio Arroyo, Controller; and Mr. Leonard Ducadam, Head of IR.

At first, Mr. Sergio Leite will make some initial considerations. Then Mr. Alberto Ono, will present the results for the Second Quarter, 2020. Then the officers will be available to answer the questions asked. I turn the call over to Mr. Sergio Leite.

#### **Sergio Leite de Andrade** {BIO 6771322 <GO>}

Thank you very much. Good morning everyone. Thank you very much for attending our conference to discuss the results of our Company.

We are addressing you at a scenario which is very different from what we saw in May when we announced the results of the first quarter at the peak of the pandemic. Today at Usiminas we are confident that what's about to come, the pandemic continues. However we have a perspective of growth recovery.

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Market indicators for the positioning of several players -- economic players have been very positive so that we can move towards a positive scenario.

We are confident that the scenario will continue and we would like to communicate to you and we do this with a lot of pleasure, that we are returning our blast furnace of Ipatinga. We are reforming the operations at [Bataui]. And we are also increasing our guidance for investments considering the healthier situation of the Company.

In -- all in all we are starting the Third Quarter in a very different scenario that we saw in the second quarter. In the second quarter, pandemic was a moment for reflection and action.

We worked intensively during this period to minimize the effects that we had -- the serious ones that we had in relation to the pandemic affecting the economic situation of the country and preparing our country for the moment of recovery. And this is the time we are going through right now.

As you all know, we restructured Usiminas Mecanica, we concentrated the businesses of this Company in order to provide services and also in the other four companies of the Company.

We -- the Board approved unanimously some action and Usiminas Mecanica will be a company that will add positive EBITDA. We also restructured our activities in Cubatao where we are now adopting a new configuration in this month of August and will make it ever more competitive.

We have made and we are going to continue working on the increasing the competitiveness of our operations in Ipatinga and Soluções Usiminas also goes through a moment of increasing its complexity and a change in its structure. So this has been propelled by the pandemic that led us to profound reflections and we made immediate actions related to resilience and adaptations.

It was a period that will remain in our memories of the time of a lot of suffering, a lot of fight, a lot of struggle. And in March when the pandemic was -- is stalled in Brazil, on 26th of February, when the first case was recorded, we adopted deep and immediate measures.

We formed a Coronavirus Crisis Committee and we worked seven days a week in the beginning, and they did a great job and we have a social part which is very important, which is from the Sao Francisco Xavier Foundation that allowed us to follow this path in a scientific and professional way and we have competent professionals working at this Foundation and this will always -- this will be the -- our greatest priority to preserve safety, health, and the life of everyone.

And this is a work that we have been doing not only involving our operations and employees but also the trade partners, the third parties that work with us, and also the

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communities.

We invested more than BRL 27 million, providing support to the communities for the operations of four hospitals, and it's important to mention that we have four hospitals located in the Steel area in Itabera that has a very large influence in the region and where [Vale], our partner also works and also in [Vale Cintesta].

And it's important to mention that our hospitals provided services to 90% of our communities, all those people who needed support and we were there. So we did a very important job.

In March -- our second priority at that time, was to do a proper management. And we had to manage our cash as our second priority so we worked hard on this and we are very happy to mention that we have had good results -- as our cash management results, the Controller, cash ended the quarter as the third-highest cash level of the previous years, and the result is very important and brings -- brings us a very healthy situation in terms of finances.

And if you look at the consolidated cash -- since the second quarter of 2019 every quarter we have presented consistently an increased cash. Today we have the consolidated level, more than BRL 2.5 million so the cash management work that included all the team of Minas, when we looked at the working capital, doing an excellent job, we are going to see the details during the presentation.

And the good news is that we will have an inflow of BRL 300 million that Eletrobras has already deposited and we are just -- in the -- in the management of how to do the transfer, so we have this additional amount in our cash. And so we are going to add BRL 311 million to the positive results that we have already achieved.

The third focus that we have and we are going to work on this in the next quarters are the results generation. In the Second Quarter we had an excellent performance of our operations in mining [boozer]. We generated EBIDTA which was record of all quarters of the Company, that has been in operation for 10 years so it was the best quarter.

In the second quarter we also granted the installation permit of the dry stacking for the mining. We are working hard on this investment already and this is going to go live in the First Quarter, 2021.

We eliminated the operation of our last dam which is downgrading dam and we are going to work with dry stacking so we have been working on mining and the result has been very positive.

So all in all we have been working hard on this restructuring, preparing our Company to the new periods to come. We are increasing our investment guidance in 33% from 600 to 800 million, which is also a very important aspect to consider.

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And today we are bringing to you together with the results of the Second Quarter, that we are going to present in a short while, so it's a perspective on our work that has been done in order to prepare our Company for the new challenges, the new scenarios in Brazil and I believe the rest of the world so that we can build together the present and the future of our companies.

Thank you very much for your attention. And I turn the floor over to our Investor Relations Corporate Planning Vice President Officer, Mr. Alberto Ono.

**Alberto Ono** {BIO 20633628 <GO>}

Good morning everyone. Again I would like to thank you for attending this Earnings Call.

And let's move on to the slide number 2 of our presentation, and these are the main figures of the Company. First, Steel unit sales. We can see here that the largest impact of all the Coronavirus Pandemic effect can be seen here.

We had a significant reduction by 42% as we have said before. On the last call, we said that the Brazilian company had its industries nearly come to a stop in April so this impacted the sales quite significantly.

In relation to Iron Ore sales we can see there has been a small reduction of our -- in our sales, this is a result of planned stoppage for maintenance activities but this is not likely to repeat in the quarters to come so we are likely to recover the volumes that had been lost in this period, up to the end of the year.

In terms of EBITDA margin, we can see the results of the impact especially in the [COE net] but also other businesses were affected so we had a drop of 66% with 8% of margin. And it's important to mention here as we will show in more details during the presentation, we had non-recurring effect of that -- affected the results of the Second Quarter.

In relation to the net profit again, we had -- we reported a loss, a bit smaller, 395 million. And here we can see the next net exchange variation was smaller. In the previous quarter we had tax effects change of 174 million, 5% so it's a result of the operating results that impacted the -- this loss.

Next slide, we can see a sequence of EBITDA of the latest five quarters. We would like to draw your attention on the slide that there is this information of non-recurring effect and if we do not consider those effects, our EBITDA would've been 281 million.

Out of those non-recurring effects we have the provisions associated with the COVID-19 impact, that affects the production perspectives because those are provisions associated to what is likely to be observed in the quarters -- in future quarters, more specifically in the Third Quarter.

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And then we have the impact of doubtful accounts and the associated provisions. This is considered nonrecurring because the sale was related to an Energy sale in 2019 and the client who purchased that Energy had problems to pay. We were negotiating the payment but unfortunately in this quarter, this client went bankrupt so we had to recognize this provision of loss which was related to Energy sale, related to 2019.

And lastly, the restructuration cost of Usiminas Mecanicas which will be reflected in other quarters. It's a nonrecurring that will -- was done now but the effect will be felt in the future quarters. Without those effects that amounted to 89 million, our EBITDA would've been 281.

In relation to Steel unit, as can see -- can be seen on slide 4, we can see the nonrecurring effects that has its operational aspect that was impacted by the [expressive] drop in volume so we can show the number of 102 but the impact is more than double of what would've been the negative operational EBITDA.

Our next slide, Mineracao Usiminas as mentioned by Sergio, in spite of a volume which was a little slow -- lower than the previous quarter so we reached 380 million -- which is the highest result of the quarter with 50% of margin so this is very favorable to us. And this was action that was well used by our Company.

Our next slide, we can see the steel transformation, Soluções Usiminas, and we can see there has been a reduction in sales affecting the EBITDA so we had a negative EBITDA of 11 million.

And moving on to the next slide, lastly Usiminas Mecanica, in addition to the provision for the restructuring of Usiminas Mecanica we also had for this specific company COVID impact in the quarter, they were recognized in the quarter, and they were associated to a lot of stoppages of some construction works that were being carried out at clients and they stopped -- and they had to follow the guidelines established by their own companies, related to COVID-19 crisis so we had these costs that were recognized in the quarter.

Now talking about other financial indicators on the other slides as has been mentioned by Sergio in this presentation, as for working capital we had 5% reduction and we went back to a level of BRL 4.1 billion, and as we have already mentioned and also contained in the release we had a judiciary deposit in relation to the deposit received by Eletrobras, so if we do not consider this aspect we would have reached the level of working capital of 3.8, so it is the lowest working-capital level in the past quarters.

In relation to Steel inventories as we can see on the next slide, during this quarter we had a 4% reduction so we can see that we have been managing this drop in the volume of inventories so that we can have a more stringent control of our inventories.

So this shows that the measures adopted led to good results and this can be seen in the results of the work -- our working capital -- in function of this drop, the working capital has been increased but the physical volume has been reduced.

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Our next slide, we talk about cash position and indebtedness. As Sergio mentioned we have been going in this continuous trend so if we look at the cash position today in a consolidated manner we can see that as of the second quarter of 2019 we have our cash doubled. Now we reach 2.5 billion and FX variation affected the debt as I mentioned, and this makes our gross debt increase, so BRL 300 billion.

So the cash -- was balance partially but it was impacted by a lower -- EBIDTA at the increase of gross debt which was not totally affected by the increase of the cash. We have an increase of our leverage but we believe that even though we have seen this increase, the levels are still quite reasonable considering everything that is happening now.

The focus now as Sergio mentioned is to preserve our liquidity and you can see this very clearly in -- that we have reached this objective.

Our next slide, we will discuss our CapEx. And in this quarter we reached BRL 193 million of realized CapEx, 11 million more than the previous quarter but practically at the same level.

And as mentioned before by Sergio, we have extended our guidance to 800 million, and this is basically due to the projects and the main one is the dry stacking but there are other projects as well connected to the mining activities and they all make a lot of sense considering everything that we have been observing along the previous quarters, so we are going to concentrate this increase allocated in the mining activities. So this is the presentation. And we will now open the Q&A session. Thank you.

## Questions And Answers

### Operator

(Operator Instructions) Our first question comes from Mr. Gabriel Galvao, with Credit Suisse.

#### **Q - Gabriel Galvao** {BIO 22424237 <GO>}

Good morning everyone. Thank you very much for taking my question.

My first question is related to how do you see this recovery of steel demand in the -- this month; could you provide more details on the comparison on the monthly basis and as the last year; and could you give more details and how the assemblers are doing; so you would -- you said you would expect those levels to normalize and what about the pricing - price increase in the domestic market?

You announce an increase of price in July, I would like to understand the -- this increase has been approved and there has been a movement to increase prices, do you intend to accompany this price increase and how big would this increase be? And how you see parity today and what would that mean after the -- after the increases? Thank you.

## A - Miguel Homes

Good morning. This is Miguel speaking.

This is a very complete question right so you're talking about demand and price. So it is important for us to understand how the recovery is happening, the demand recovery.

We -- it's important to understand what happened in the previous quarter. The result of the sector was announced together with a forecast for the apparent consumption of steel for 2020. When this -- when -- [USSA] Brazil announced this, it said that the sector had a drop in the -- in its [plants] of 17% in relation to the -- year on year so there was a drop in the apparent consumption for the whole quarter of 13.5%.

When we consider the whole year [USSA] Brazil estimates there will be an apparent total -- consumption in -- but it gives no details of which is [bulk] and which is short and we should expect a drop in apparent consumption, higher than 14.5%.

And as for Usiminas, Usiminas follows those indicators and is -- because it is an active part of [USSA] Brazil, in relation to the minutes for the second quarter, as you know, Usiminas, we are -- we have a very important presence in the automotive sector so the drop of production was very high and the recovery has been important considering the demand so there was a drop in production.

But in May there was a drop of 105%. In June there has been a recovery in the production of vehicles reaching a level of 1,000 units which is a drop compared to the previous year of 60%. This drop in the vehicle production is 31%, it's a very strong impact on Usiminas. When we consider this important drop and together with a strong drop in the home -- household appliances, this can account for 40% of impact.

So -- but we can see that along the quarter the sales have been evolving but with a drop of 44%, and this is how the sales evolved a company -- companies in the sectors where we operate. And -- [inaudible] has estimates that production will be kept at 45% with sales drop in exports of 50% in the auto -- automotive sectors.

We are looking at the future with good expectations so we can see that the level of cars put in the market is higher than the previous periods so this would lead to the increase in production because the inventory levels are very low in the auto -- automotive sector.

And we have to watch closely because when consumption recovers the inventory which is very low in all industrial chain. So we are in other words prepared for this consumption recovery both in our inventory levels and as well as our production levels.

In relation to the price, it's also important to say that we are showing the -- of -- an average price of 1% in comparison to the previous quarter. In May -- we mentioned that we are facing of -- a scenario of negative parity. At this time what happened? As you said, we had an increase in price in July, yes, as you mentioned about 10% for the sector. And also there was a drop in the value of the dollar.

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If we consider the parity of 10%, the -- and also the evaluation of 5% of our currency, and we consider all this, we would have parity -- a positive parity of 5%. But what happened in the international prices is that there was an adjustment of nearly 50%.

This leads to a negative parity and as we said in different opportunities, we cannot have negative parity, it's not very good for our -- to the health of the Company so we are going to return to a healthy parity in the short time.

Gabriel Galvao: Okay. Thank you. What about the increase that you're planning for September?

We do not talk about future events. Maybe you should -- you could come to a conclusion after all we've said today and what we would do to return to a healthy parity.

**Q - Gabriel Galvao** {BIO 22424237 <GO>}

Very clear. Thank you.

## Operator

Our next question comes from Mr. Thiago Ojea with Goldman Sachs.

**Q - Thiago Ojea** {BIO 17363756 <GO>}

Hello, good morning everyone. Thank you very much for taking my question.

My first question is in relation to the restart of the blast furnace especially in Cubatao. How do you see the first dynamics of plates. What would be a healthy price for the production of plates after you start the operation of Cubatao? And with the improvement in the cash position, do -- you mentioned the increase in capex but you see any possibility of adopting a different policy for dividend pay-out and/or allocation of capital? Thank you.

**A - Alberto Ono** {BIO 20633628 <GO>}

Thiago, this is Alberto speaking. I'm going to talk about allocation of capital first. We do not have any estimate to make any changes. We are still very focused on preserving the liquidity of the Company.

And as for CapEx, as we have said before, it's focused on improving our efficiency and also on sustaining the mining so this is the main point for us. Obviously we are watching closely the result. So for the time being, we still do not have any estimates of making any changes to the liquidity preservation.

In relation to the balance and the blast furnaces, well what I have to say is that first the restart of the blast furnace makes sense to start resuming production, so we can see that there is a positive scenario to recover or resume the activities -- our activities with our clients so this is in line with our decision to restart the -- blast furnaces.



As for Cubatao, what we have to say is that we'll consider the market price. We see what the supply and demand of the market is. The prices are regulated at the international level. There's nothing different. So those prices make sense for us to do business and this is what we have been observing in the domestic market.

So basically major -- a big part of the volume that we have been observing will be supported by this -- by the domestic market. And this is what we can say so of course it makes sense to start producing so the plate price is different because the -- when -- the purchases we'll have to add it on margin so about this decision make sense considering the projections for the domestic market.

**Q - Thiago Ojea** {BIO 17363756 <GO>}

Thank [you all back.]

## Operator

Our next question comes from Daniel Sasson with Itau BBA.

**Q - Daniel Sasson** {BIO 19234542 <GO>}

Hello. Thank you very much for the opportunity. I have two questions.

It -- we have follow ups on the previous question. As for -- as for production costs per ton, help us understand the evolution for the third quarter or in the future so that we can balance the start of Blast Furnace 1, may be the cost will be higher and we also have to consider the fixed costs and -- which will improve sequentially so this can help us understand the modeling of costs?

In relation to prices you talked a little bit about the scenario and the prospects for the third quarter but if you could make some comments on what you managed to do for the prices in the second quarter so that domestic market prices should be in stable -- stable in relationship to first-quarter and how we saw those differences in results?

**A - Alberto Ono** {BIO 20633628 <GO>}

Daniel, in relation to production cost, I could say the following. During the second quarter we had high cost that was allocated to the production cost and also to the cost which was related to high idlers of the comp -- of the product.

We had some stoppages or the shutdown of our blast furnaces in April. And also Cubatao that also had some shutdowns. This is likely to be reduced in the second quarter -- in the third quarter.

As I stated with restart, as for blast furnaces, I believe Ipatinga, Blast Furnace 1, has ramped up which will not affect the production, considering its ramp-up.

And in August you are likely to have efficient cost and a reasonable level of production so it will help us to decrease the idleness of [blast] furnaces so the fixed costs that you mentioned has to idleness that you mentioned in your question will be reduced quite significantly and this will make the cost per ton to be improved. The level of improvement we cannot -- we cannot tell for sure so it will depend on how things play out.

In relation to prices, I'll turn the call to Miguel.

## A - Miguel Homes

Good morning. In relation to prices, yes, you're right. When we look at the average price for the second quarter with a drop of only 1%, considering the situation of the worst mix, considering the automotive sector, if we look at the results in more details, what we can see the following, when we consider each family of the product, [EG], [HDG], so each one -- each of the product family will present average price which is higher than the average price of the first quarter of -- comparing the same family of products.

If you consider the mix of products of the first quarter and consider the average price of each product in the second quarter, if we remove the mixed product, in fact but still maintaining the impact of the whole mix, we will have average price higher than 2% in relation to first-quarter, 2020.

How was that possible? We had businesses, projects, that were negotiated when the sales price or better. As we mentioned in the previous call, they allowed us to increase the prices.

Along the quarter we had to remember that we mention -- I just mentioned the sector and all the projects that needed to be implemented so we also had our contracts that are adjusted on quarterly basis or an semestral basis so this period we could mention that some of those agreements that had adjustment on a semester basis they had positive adjustments.

## Operator

Our next question in English comes from Carlos de Alba with -- Morgan Stanley.

## Q - Carlos De Alba {BIO 15072819 <GO>}

Thank you very much. Good morning everyone.

So my question is on your product mix so considering that the auto sector to which you have a lot of exposure is struggling a little bit more in coming back and it may remain subdued, while construction is doing better, is it possible, do you have any flexibility to maybe switch some of your coated products, galvanized products into the construction sector, would you do that and would that require any issue, if it is possible and what that require any capex or investment in order to do -- in order to do that?

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And then just wanted to understand a little bit more about the restructuring of Usiminas Mecanica. I wasn't of the impression that it was going to basically cease to provide -- supply services or services to their bodies and would really focus on -- to service other internal units of Usiminas but you just mentioned the EBIDTA should be positive after the restructuring so I may be a little bit confused, we'll -- could you explain a little bit more what exactly are you planning doing in Usiminas Mecanica, what will -- what will be the focus of the unit after the restructuring?

And if you can comment what are some of the initiatives that will allow the Company to post positive EBIDTA in the future? Thank you very much.

### **A - Alberto Ono {BIO 20633628 <GO>}**

Carlos, thank you very much for your question. Thank you very much for your question. I will start with your question related to the structuring of Usiminas Mecanica, and the question related to changes of mix of sector. And then I'll turn to Miguel for him to answer,

In relation to Usiminas Mecanica as Sergio mentioned in his initial consideration, services that are provided by Usiminas Mecanica to the companies of the Group is a competitive service in terms of cost and results. And this business segment, so is to say, is the only one where we observe that Usiminas Mecanica's results are generated, therefore we are going to preserve this business segment because it brings positive results. The result is to preserve this business, okay.

The other businesses, they are not profitable so these are the ones we are discontinuing. So the part which will remain which is related to service -- services provided to the Group, it's profitable already for Usiminas Mecanica because it's competitiveness level shows the -- better than the competitors because in the relationship between Usiminas and the companies of the Group and Usiminas Mecanica it's also market conditions, we have no preference in this regard.

So it's competitiveness is intrinsic and it shows results in this segment so the restructuring is being done so that we can optimize the overhead structure so that we can meet the needs of this business segment alone.

And -- with positive results being generated, we believe that we are going to present positive EBIDTA, yes, we believe that but for sure it's not going to be at the -- that we used to have in the past when volumes were more significant because it's a segment but still it's a small business considering the Company as a whole.

If you compare this from historical viewpoint, this is our basis, it's going to be a smaller business, the results are going to be positive but smaller. So this is the idea we have, okay.

So I'll turn the call to Miguel.

## A - Miguel Homes

Thank you Carlos.

I thought your question is exactly related to what we did along the quarter considering the critical sector of the sector and we have an important participation here. We developed the product and then we increased our portfolio of products so that we can have a higher share and be more resilient because it's doing the COVID Pandemic.

With this objective we were successful when we developed products for our construction sector without the need for capex as you mentioned, only by making adjustment to the processes and by using our Research and Development Center.

And Usiminas has its quality recognized along the years especially focused on the automotive sector so this has made us possible to add and implement new products to our portfolio to participate not only in the construction sector but also in other products and offer more products that we -- in sectors, where we're still not participating.

Concrete results are that we can produce products for construction sector, and also galvanized products for storage, in silos, and this has been all favorable to our sectors so the answer is yes, we have the capacity and this what we have done and Usiminas is much better prepared to meet the demands of any sector that has -- that presents any demand for steel in Brazil.

## Q - Carlos De Alba {BIO 15072819 <GO>}

All right. Thank you very much. Good luck.

## Operator

Excuse me? Is there are no further questions, we close the Q&A session. If you have any questions, the IR Team is available to take your questions. We would like to thank you for your participation. Have a good day, you all.

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