Q2 2013 Earnings Call

Company Participants

- Alexandre Santoro, CEO
- Rodrigo Barros de Moura Campos, Chief Financial Officer
- Unidentified Speaker

Other Participants

- Mark Suarez, Analyst
- Unidentified Participant

Presentation

Operator

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to America Latina Logistica, ALL, second quarter of 2013 earnings conference call. Today with us we have Alexandre Santoro, CEO; Rodrigo Campos, CFO and IRO; and Pedro Albuquerque, IR Superintendent for ALL. We would like to welcome everyone that this event is being recorded and the all participants will be in a listen-only mode during the company's presentation. After ALL's remarks are completed, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions)

We have simultaneous webcast that may be accessed through ALL's IR website, www.all-logistica.com/ir. The slide presentation may be downloaded from this website. Please feel free to flip through the slides during the conference call. There will be a replay facility for this call for one week. Before proceeding, let me mention that forward-looking statements are based on beliefs and assumptions of ALL management on information currently available to the company.

They involve risks, uncertainties and assumptions because they are related to future events and therefore depend on circumstances that may or may not occur in future. Investors should understand the general economic conditions, industry conditions and other operating factors could also affect future results of ALL and could cause the results to differ materially from those expected in such forward-looking statements.

Now I turn the conference over to Mr. Rodrigo Campos, CFO and IRO for the company for a brief explanation of how ALL figures are presented and then Mr. Alexandre Santoro, CEO who will start the presentation. Mr. Campos, you may begin the conference.

Rodrigo Barros de Moura Campos {BIO 16203706 <GO>}

Good morning. Thank you everyone for holding the second Q conference call of ALL. Just some brief comments here on the numbers we are releasing here. The first comment is on the adjusted EBITDA. This adjusted EBITDA is according to the methodology of CVM, which was released at the end of last year. So all the numbers of 2013 are in the new methodology and for better comparison also, the numbers of 2012 are also in this new methodology. So the numbers of 2012 may differ a little bit from the previous year's numbers in terms of adjusted EBITDA.

One more comment on the released numbers, you know that we are trying to leave our operations in Argentina since 2012 and it was largely announced that our concessions in Argentina was we signed it in June 5th. So since grant, we do not operate the concessions in Argentina anymore and therefore, the result coming from ALL Argentina is now showed -- now presented as results of discontinued operations in a separate line of our income statement. So members of Argentina are not consolidated on our numbers anymore and are showed in a separate line. This is done in 2013 and for a comparison basis, it's also done in 2012, okay.

With that, I would like to transfer to Alexandre Santoro in order to give (technical difficulty) start the presentation.

Alexandre Santoro {BIO 7120418 <GO>}

Hi, good morning. Thank you everyone. We will start now with a summary about our second Q results. First of all, our consolidated EBITDA grew 13%, on the Rail Operations 12%, Brado 25% and Ritmo 32%. We concluded successfully the capitalization of Brado. We started our operations in Rondonopolis yesterday and at the other hand, the volume did not grow. Even a good cost scenario impacted import restrictions that we will explain further. And we left Argentina, as Rodrigo said, an operation that we will contribute to our results and had been mainly our disproportional focus by the management.

Looking more details, our EBITDA grew 13%, impacted by (inaudible) in the Rail Operations and a good quarter in Brado and Ritmo. Our first half EBITDA grows 14% to almost R$1 billion. Talking about volume, in the first half we grew 3%, positively impacted by a 6% increase in agricultural commodities and a 5% reduction in industrial products, but improved when compared to the last quarter the industrial products.

We were impacted by capacity restrictions at the ports we serve and our volumes didn't grow as we expect in the second quarter. We had a good market condition, but those restrictions at the port made our volume the same as last year.

We had a favorable crop scenario. This positive market environment was not converted into material volume growth, as we've done historically. Important to mention that we have been faced with different problems at the Port of Santos. Reducing the capacity at the terminals, we serve innovation [ph] impact on our productivity.

The ports became important bottlenecks due to slight restrictions at important terminals and excessive rains more than the double of last year. The huge increase of 12% reflecting the pass through inflation and diesel on our contract and recovery of freight price in the spot market.

When we look at Brado, the volume grew 30% which can be the main causes and a 25% increase of the EBITDA. We are proud to announce that we concluded that the capitalization of R$400 million through a capital injection of by FIF GPS. This quarter (technical difficulty) R$1.4 billion (technical difficulty) and $1.2 billion [ph] post (technical difficulty). 62% of the company and this is injection we will have the confidence to deliver constant growth in the future as we planned.

When we look at the other business that we have with Ritmo, our EBITDA increased 30% to (technical difficulty) at the second Q and (technical difficulty) volumes increased 2% (technical difficulty). You know that we concluded investments on the expansion of our large (inaudible)network to Rondonopolis in the end of 2012 and we have obtained the position of license from (inaudible) operations yesterday. We started our testing period and volumes should grow gradually and we believe that we will be at full capacity at the middle of September.

It's important step in our history and (technical difficulty) very proud to see this brilliant project operational. The Argentine government talking now about Argentina we signed the concessions of ALL in the country. Now as we informed before, the company was planning to discontinue its operations there. The results from the operations represented a minor share of ALL consolidated results but had been demanding disproportional focus.

Now I will ask Rodrigo, our CFO to present more details about the results. Then I'll come back with additional comments at the end of the presentation. Thank you.

Rodrigo Barros de Moura Campos {BIO 16203706 <GO>}

Thank you, Santoro. Going to slide six, which shows ALL consolidated results, you can see that adjusted EBITDA increased almost 13% in second Q to R$580 million more or less and grew 14%, close to R$980 million in the first half 2013. Our net income in first half 2013 was negative in R$40 million and it was basically because of the impact of the discontinuation of our operations in Argentina. You know that we used to have the concessions there as we don't have any more, you have the impairment of the -- the CapEx we have there, also of fiscal credits we have there, so we made all the impairments, the accounting which generates an accounting, a negative accounting in fact this quarter. If we exclude the results of operations in Argentina, our net income reached 200, almost R$220 million in first half 2013, which represents a 30% growth as compared to last year.

Moving to the slide seven, looking through the rail operations, you can see that that the volumes were literally the same in the second Q as compared to the past year, which surely is not what we expected. We expected to grow, but we faced a severe capacity restrictions on the port that we will explored a little bit further. And in the first half of 2013, the volume increased 3% as compared to the last year. The yields, average tariffs earnings grew 11.7% in the second Q and 10.2% in the first half 2013, which reflect basically the inflation pass-through and the increase in diesel price that's to take-or-pay agreement -- agreements and also an improved -- and a recover of the freight prices in the spot market.

So, it was a good quarter in terms of freighting. And the adjusted EBITDA of our rail operations reached R$560 million in the quarter from 500 in this same period of last year, with a margin expansion of 0.4% in the quarter. In first half, EBITDA grew almost 14% to R$943 million.

Going through slide eight, one which shows the performance of our agricultural commodity business, the volumes in the quarter increased 0.4% and here this volume was pretty much impacted by the performance on the ports. We know that we face a good market environment, but I mean ports became an important bottleneck for our operation this quarter. We know that you must see [ph] logistics has a system.

When you look the logistics, you have the trucking connections, the terminals on the countryside, you have the railroad and you have the ports, and everything must work as a system. As the ports do not work, which was the case in the second Q, also in the month of March we already faced some problems on the ports.

It impacts all the productivity in all the system in the railroads, in the rolling stock after turn. So it has a very important impact in our operations.

And when we look the ports, we have a very good market. We have a huge increase in the traffic of the trucks inside the port, which increased the traffic jam on the port. Also, we have some mixed strikes on the ports in May and also in March, and we had some specific impact in terminals which are very important terminals for the railroad, especially in Port of Santos.

If you take Port of Santos in the quarter, the TGG, which is the main terminal in terms of unloading for the railroad, it represents almost 40% of the day-to-day unloading of the railroad, had a fire incident which burn one of the four towers of the terminal of TGG in June. So this was the one incident. Another incident we faced was in the terminal 39 where a ship heat one of the two shiploaders of the terminal and destroyed the shiploader, so the terminal started to operate with 50% of the capacity. Now we are -- the terminal 39 is working, changing the maneuvering of the ships, creating additional maneuverings to better -- to take advantage of the -- to improve the productivity of the shiploader which is operational (technical difficulty) but it's also (technical difficulty) and in the sugar terminals, our (technical difficulty) have a plan of increased capacity of those terminal. They have works of expansion of capacity of these terminals, but these works should be concluded only in August. And during the works, the capacity of these terminals are 30% below last year.

So just to summarize (inaudible) we have a pressure on the demand for the ports much higher traffic of trucks inside the port and at the same time, we have problems on very important terminals during this quarter. The part of these problems will be solved along the third Q and in the fourth Q. So that the performance we saw on the port which impacted the performance of (technical difficulty) in the second quarter, we (technical difficulty) 0.4% and in the year, when we see first half 2013, agricultural volumes are down 6% as compared to the same period of last year.

In slide nine, we see that net revenues grew almost 13% basically -- in the quarter, basically reflecting a yield growth of 12% and a marginal volume growth. Adjusted EBITDA increased 15% and here it's important to mention an improvement in the margins for (technical difficulty) percentage in the quarter and in the first half, the EBITDA increased 18% with an expansion in EBITDA margin of 0.6% as compared with the same period of last year.

In slide 10, which show our industrial products business. During the quarter, the volume decreased more or less 2% as compared to the same period of last year, which is a negative number but is -- it is an improvement if you compare with the previous quarters.

We know that the industrial business was suffering (technical difficulty) inflow activity in our area, also with some changes in some of our clients' operations, but I mean now we are ramping-up volumes in the industrial business and we are improving as compared with the previous quarter. And this improvement is a result basically of the ramp-up of the operation with our client Eldorado which is a project that when it is in the stead stage, will be a project of a million tonnes and unrealized volumes, so it's a big project and also the recovery in volumes are related to the improvement in volumes of containers basically through our clients Brado.

When we go to slide 11, we see that net revenues of industrial segment increased 6.2%, EBITDA was almost in line with last year around R$90 million. But I mean, EBITDA margins in the industrial segment went down basically because of the mix between transported products. I mean, we increased the volumes of containers, which are volumes that naturally have smaller margins, I mean, remember that Brado is doing now the CapEx in order to grow containers very well. So as a counter part, this is a discount so it means that tariffs for Brado are lower, which generate, I mean, reflect, and of course, the volumes are a little bit lower than last year which means that the operational leverage of the railroad -- and with an impact in margin at the end of the day.

When we go to page 12, we see that Brado has a very good quarter. Volume is increasing 30% as compared with last year with an important volume increase in all four corridors of Brado. So volumes are growing 45% in Wide Gauge corridor, and 13.6% in Mercosul corridor, remember that Mercosul corridor, where volumes are Brado were decreasing, so they are starting to recover volumes in Mercosul. Brado had all the problems with customs restrictions in Argentina which reductions of imports from Brazil in Argentina, so volumes are recovering which are good news. In Parana volumes also increased almost 40%, which is also good news and volumes increased 17% in Rio Grande corridor at Brado.

And in slide 13, net revenues of Brado increased 20% reaching R$66.4 million and EBITDA of Brado increased 25% in the second Q with a margin growth of 0.7%. In the first half, the net revenues grew 22% in Brado, which is more or less the growth in the adjusted EBITDA in the first half 2013.

Going to slide 14, we see the result of Ritmo. Ritmo is our (inaudible) subsidiary and Ritmo also had a good, very good quarter in terms of volume and in terms of EBITDA. The volume increased 16%, basically is supported basically by an increase in the volumes of our intermodal unit. Remember that when we created Ritmo, the intermodal transportation which are these stretching connections that you must do to feed the rail road was the main opportunity we used to see for Ritmo and Ritmo is increasing volumes quarter-over-quarter as compared with last year.

So in the second Q, volumes in the intermodal units increased 80% and in the first half volumes grew 90% as compared with the same period of last year. In the other units and in general cargo and specialized assets, volume grew 8% in the second Q and 3% in first half. And automotive segment, we kept reducing volumes in the same trend we had in the previous quarters, as we left some, a role of profitable operations just concentrating our focus on operations which have better margins.

So as a result and we see in page 15, net revenue increased 10%, but adjusted EBITDA grew 32% in the second Q, from 5.4 million to 7.1 million, gaining margin from 8.9% to 10.7% in the second Q. So the margin improvement with the focus on most profitable operations and also increase in the scale of our intermodal business as volumes have been growing quarter-over-quarter. And in the first half, net revenues grew 8.2% and EBITDA grew 23%, also its material margin grew from 9.2% to 10.4% in Ritmo [ph].

When we go to slide 16, we have our consolidated revenues. Important to mention that when you compare first half 2012 to first half 2013, the effect of Argentina are not part of consolidated net revenues anymore, because it's showed in a separate line of our income statement. So revenues grew 14% as compared -- in first half 2013 as compared with first half of 2012. And EBITDA increased 14%, slide 17, with margins -- consolidated margin is stable in 52%.

Important to mention that when you look business by business, all margins are growing. It's growing in rail business, it's growing in trucking business, it's growing in container business. But given the needs that our container business and our trucking business are growing more than the rail and those are business that have lower margins, the margin -- the consolidated margins are stable when you compare year-over-year in 52%.

When we go to slide 18, we show our net income. Our net income, as we mentioned before, is 40% negative. But I mean when you exclude the impact of our (technical difficulty) would be around R$220 million and a 30% growth as compared with last year. In slide 19, which show the leverage of our balance sheet. The net (technical difficulty) to EBITDA and the first half in 2.4 times, net debt to EBITDA (technical difficulty) at the end of 2012.

And with that, I would like to transfer the presentation to Alexandre Santoro (technical difficulty).

Alexandre Santoro {BIO 7120418 <GO>}

Thanks, Rodrigo. I have three points to conclude. And first of all, CapEx, we have to, we are progressing as expected aligned with our long-term guidance of R$700 million. The second point is about volumes, we still see the market scenario, it's favorable but the capacity restrictions at the ports we serve should extend through the third Q. There are several infrastructure improvements expected to be in the placed on the following month. At the same time, we have some project that will help us to increase our volumes on the industrial projects.

Like (inaudible) Eldorado, Ethanol and Brado. And the third is the Rondonopolis that yesterday we start operations and we will go through a testing period and volume should grow gradually. Now, I will -- we will open for the questions, you have and we are happy to answer you.

Thank you. Thanks, everybody.

Questions And Answers

Operator

Thank you. This call is now open to the questions. (Operator Instructions). Mark Suarez from Pacific Capital would you like to make a question.

Q - Mark Suarez {BIO 16366613 <GO>}

Hi, there. Good morning, everyone.

A - Alexandre Santoro {BIO 7120418 <GO>}

Good morning.

Q - Mark Suarez {BIO 16366613 <GO>}

Just to go back on the, you were talking about the capacity indications at both terminals Port of Santos in addition to the construction work that you're trying to increase capacity in sugar terminal. How should we -- if we put all those things together (inaudible) you mentioned in the press release, how should we be thinking about agricultural volumes through the end of the year?

A - Rodrigo Barros de Moura Campos {BIO 16203706 <GO>}

Mark, when we look at the ports and we should still see restrictions at the port in the third Q and in July, it was the amount that had an additional impact which was the -- the rainfalls in Santos was the double of the same period of last year. So it contributed to -- with all these scenario of impact in capacity, the move in capacity of the terminals on the port, but I mean, there's a lot of things going on in order to recover the capacity in the terminals which were affected by accidents, particular TGG and Terminal XXXIX.

And in sugar terminals, the works of expansion should be completed in August. So if you take the TGG, the recover of the tower which was fired should be completed only in the fourth Q in October, maybe November, so this restriction should be there. But in Terminal XXXIX, lost one of the two shiploaders which reduced the tax tradition capacity of the terminal by 50% that I mean, the terminal sat with the ships and other procedure where the ships do additional maneuverings and it increased the productivity of the existing shiploader.

So at the end of the day, the part of the loss capacity should be recovered in this different process. And estimates are that in September, we should be the shiploader -- back the shiploader which was lost by this accident back. And the terminals of sugar should be operational, they are operational, sorry, but they should be -- with their works concluded in August. So longer the quarter, we should see some of the capacity restored. So in the ports too, we should have our ports much more in line with what would be normal. I don't want to anticipate any projection of volume for the year. For the quarter or the second half, we normally don't do that. Market, it should be good also as it was in the first half.

And I mean -- but there is still some restrictions on the port. What I believe when I look ahead is that ports can be a huge opportunity for our business, because I mean you are looking that you are -- probably you are hearing [ph] that the government has a new model for the ports. The government intends to put to -- beat against some of the existing ports. And the model that the government is prioritizing is a model that focus on the productivity gains. So today in Port of Santos, for example, you have a terminal like TGG, which moves like 7 million tonnes per year in its bus.

And there are terminals that by the end of the day, that moves like 1.5 million tonnes in its bus per year. So it's not acceptable that in Port of Santos, terminals move less than 5 million tonnes in a bus. I mean bus is the main restriction that we have in Port of Santos. New bus cost a lot of money.

There are projects of new bus, I think which are more long term. But I mean you got to improve a lot in this short to medium term, the capacity of the ports only making marginal investments and gaining productivity in the existing terminals. So there is no problem in having a private terminal, a private bus, but if you only move like 1.5 million tonnes, you should tempt other guys and you should have goals of volume movement in your terminals and this is the model that the government wants to follow and there are some things that should be on market at the end of this year.

So we look carefully for the ports. I believe that few things have so many synergies as railroads and port and in -- if you have a port which is efficient, it generate a big gain in terms of productivity of the railcar, of locomotive with the same railcars and locomotive we tend to support much more. And at the same time the railroad can migrate, can bring a lot of cargos for the port terminals, so there is a lot of synergies in both business.

But in (inaudible) of ALL, we're managing terminals on the port for a third guy being managing the ports, the terminals on the port. The important thing is to have a productive port and I believe that the model of the government is very focused on that.

Q - Mark Suarez {BIO 16366613 <GO>}

That was very helpful. Now you mentioned Rondonopolis. You started basically transporting since August 6 through the Rondonopolis line. Is it bottlenecks at Port of Santos impact a ramp-up as you reach presumably full capacity or at least near capacity as you're projecting September of this year. Would that have an impact whatsoever?

A - Unidentified Speaker

No, I mean, no. The ramp-up of Rondonopolis is basically operational. Our agreement have with the clients already have a precision of hauling from Rondonopolis. We have tariffs hauling come out of (inaudible) and tariffs already hauling from Rondonopolis, so this migration is hurting that is we are -- easy and I mean -- but there is the normal operational ramp-up. You have all the engines of the terminals, the team of the terminal that should start to be -- that will be sat in other and it will be sat with this ramp-up of growing volumes. I mean, the port has no connections with Rondonopolis, because Rondonopolis is only to create the same cargo in terms for our longer distance. So at the end of the day, you starting, start the operations from Rondonopolis, you do not change the volumes how do you move at the ports at the end of day, so --

A - Rodrigo Barros de Moura Campos {BIO 16203706 <GO>}

(technical difficulty).

A - Alexandre Santoro {BIO 7120418 <GO>}

Yeah, so the (inaudible) will increase with the same tones being moved, so at the end of the day, no connections between Cambe and Rondonopolis and ports at the end of the day.

Q - Mark Suarez {BIO 16366613 <GO>}

Got it. And you mentioned the Brado Capital Injection of 400 million. Can you explain to me how that came about, how do you guys came together with that project and is there the potential, for the same partner to potentially fund the entire 1 billion for the first five years or you think, you will need to involve several partners into the mix?

A - Alexandre Santoro {BIO 7120418 <GO>}

Mark, I don't believe, we don't need, I don't believe, we need 1 billion in equity for Brado because and, we have a CapEx of 1 billion in five years, you are completely right. But remember that 80% of the CapEx of Brado is locomotives and railcars and we have a special lines from EMBS called PSI which align with some loan in our to risk rate all we, around 3% to 4% (inaudible) interest rate. So this 400 million, gives the Brado enough equity and leverage capacity to fund all the -- growth. And more than that, I mean, when you look the cash flow needs of Brado, the Brado generates cash flow very fast.

As the main CapEx is railcars and locomotive, you buy railcars and locomotives in six months after you are operating. So there is not a big CapEx to be done, which will blend cash flow and that will be operational, all the years ahead I mean in the case of Brado, you buy railcars and locomotives and we start to generate cash from this additional (technical difficulty). So the cash (technical difficulty).

Q - Mark Suarez {BIO 16366613 <GO>}

Okay. Great. That was very helpful. Thanks for your time. That's all I have for now.

A - Alexandre Santoro {BIO 7120418 <GO>}

Thank you.

Operator

Mr. (inaudible) from Citibank would like to make a question.

Q - Unidentified Participant

Yes. Good morning, guys and thanks for taking my question. I was unable to hear the entire call, I had a technical (inaudible) on Santoro, sorry if you've already mentioned this. But there seem to be some local news this morning suggesting that you might be having some discussion with the government about returning some lower utilization sections of the track and I was wondering if you had any terminal of that?

A - Rodrigo Barros de Moura Campos {BIO 16203706 <GO>}

Actually, Stephen, the talks are in very beginning, so nothing new at this stage. But just to address the point, we are talking here about two specific tracks. One that goes from Sao Paulo to Rio Grande do Sul, the state, which represents more or less 5% of our EBITDA and the government would like to make a big corridor, one of the projects of the government is to make a big corridor from the north portion of this view connecting with our rail line in Sao Paulo and going all the way to (inaudible) Rio Grande do Sul. So -- and Port of Rio Grande. So in this connection, pass through our rail line at the end of the day.

So we are starting discussions, but I mean discussions here are very simple. We have some investments with -- and we have the economics of those tracks for rail. So what we are discussing is to have some indemnization or something equivalent that could have a good economics in order to give back those track to the government. Otherwise I just keep my track there. So this is -- this conversation which are beginning but it's simple like that. We have -- we know the economics of those rail lines and we are talking about the government how we would receive -- exchange these rail line for indemnization or to the same economics at the end of the day.

So it's a discussion it can happen or cannot. We are in the very beginning, so no -- nothing to present here, but simple as that, I mean. So -- and there's another track, very small track in Port of Santos, which is the track which reached Port of Santos, which is from MRS, the major and there is a bus which is from ALL to concessions. And today, to be frank with you, operation there does not go smoothly, I mean. As there is two concessions there, there is always operational discussions in order to entering Port of Santos, which impacts in terms of productivity. So due to these small track back to the government and being a new guy, a white flag guy that would manage this concession, could be an operational model that could improve the productivity entering in the Port of Santos.

So this is the mindset of the government. We believe with that, but I mean different from the line to Rio Grande do Sul which is a small part of our results. This line Santos receives a large portion of the volumes we hold. So we should be very confident on the operational model in order to go through this step of giving back to the government and having a white flag guy in Port of Santos. So at the end of the day, we think that the model that the government is thinking to Santos is a very good model. It could bring a lot of gains in productivity of having just one concession there, a white flag concession there. But we must be very comfortable with the operational model in order to do this move.

So also, as in the case of the track to Port of Rio Grande, in Santos, also we are in the beginning of the talks and there is nothing decided. We can go through with that or we just can keep the rail line as it is. It's the decision we should take and we are starting to talk with the government.

Q - Unidentified Participant

Okay. Thanks, Rodrigo, very helpful. And just one more question, just in case, I missed any comment. I'm assuming at this point, no update on what might be occurring with Cosan's conversations with ALL's controlling shareholders?

A - Rodrigo Barros de Moura Campos {BIO 16203706 <GO>}

Yeah. Unfortunately, no update given. No news on that.

Q - Unidentified Participant

Okay, fair enough. I'll leave it at that. Thanks Rodrigo.

A - Rodrigo Barros de Moura Campos {BIO 16203706 <GO>}

Thank you, Stephen.

Operator

(Operator Instructions). I will turn over to Mr. Alexandre Santoro, for the final considerations. Mr. Alexandre you may give your final considerations.

A - Alexandre Santoro {BIO 7120418 <GO>}

Okay. I want to thank you and say that we talked here a lot about Port of Santos. There that we are working hard with our clients and the terminals in Santos to recover the operational capacity. And our operation at Rondonopolis that is remarkable. It's remarkable in our history. Able to help us, deliver cost and growth as we did in the past and it will still continue grow this company. So, thank you again, if you have any additional questions please contact us directly. Bye, bye. Thank you.

Operator

Thank you this concludes today our ALLAY SA earnings conference call. You may disconnect your lines at that time.