

## Q1 2019 Earnings Call

### Company Participants

- Joao Alberto Fernandez de Abreu, CEO
- Ricardo Lewin, VP Finance & CFO & IR

### Other Participants

- Alexandre Falcao
- Bruno Amorim
- Josh Milberg
- Joshua Milberg
- Rogerio Araujo
- Victor Mizusaki

### Presentation

#### Operator

Good afternoon, ladies and gentlemen. At this time, we would like to welcome everyone to Rumo's First Quarter 2019 Results Conference Call.

Today, we'll start with a message from Mr. Beto Abreu, Rumo's CEO, and then the conference call will be led by Mr. Ricardo Lewin, Chief Financial and Investor Relations Officer.

We would like to inform you that this event is recorded. (Operator Instructions) The audio and slideshow of this presentation are available through live webcast at [ir.rumolog.com](http://ir.rumolog.com). The slides can also be downloaded from the webcast platform.

Before proceeding, let me mention that forward-looking statements will be made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of Rumo's management and on information currently available to the company. They involve risks, uncertainties and assumptions because they relate to future events and, therefore, depend on circumstances that may or may not occur in the future.

Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of Rumo and could cause results to differ materially from those expressed in such forward-looking statements.

Now I'll turn the conference over to Mr. Beto Abreu, reminding that after his first considerations, Mr. Ricardo Lewin will conduct the presentation.

Mr. Beto Abreu, you may begin the conference.

## **Joao Alberto Fernandez de Abreu** {BIO 20362451 <GO>}

Good afternoon, everyone. It is with great pleasure today that I take the opportunity to finally share my first consideration of Rumo's future with our stakeholders and shareholders. There have been several remarkable developments for Rumo in the last few months.

On our Investor Day, in March, we presented to the market our 5-year plan. With relevant investments and impressive levels of returns, this ambitious plan will enable the company to double its results over the course of the next 5 years.

Also, this quarter, we won the bidding process for the North-South Rail, which will expand our area of operation and consolidate our presence in Brazil's Midwest region. We're already working to start operating this rail, while maintaining focus on the results of our current operations.

At the same time, the Paulista Network renewal process has progressed. The Federal Audit Court's, TCU, technical units recognized that renewing the Paulista Network would bring benefits to Brazil. We remain confident about this subject and expect to conclude the renewal process soon.

The company's future looks promising. Brazil has a solid agricultural profile and Rumo connects major regions of grain production with major exporting ports. But Rumo is not only about agricultural products transportation. We are effectively reducing the distance between areas of different industrialization levels through our Container business. Moreover, we are expanding our fertilizer and pulp operations.

Finally, before presenting the first quarter results, I would like to share with you my expectation for 2019. We delivered positive results in the first quarter, but we also recognize that the rest of the year will be challenged with the soybean harvest scenario, but with expectation of a record corn crop. Nevertheless, we are optimizing our operation and increasing volume transportation with commercial contracts in line with our plans.

Having said that, we are confident we will deliver 2019 results. Thank you very much.

## **Ricardo Lewin** {BIO 20342706 <GO>}

Thank you, Beto, for your opening thoughts. Let's start our first quarter '19 results presentation with Slide number 2.

FINAL

Bloomberg Transcript

FINAL

First, I would like to illustrate how we reported this quarter's figures using the chart on this slide. As of January 1, we implemented IFRS 16, a unique accounting model that significantly changes the financial information policies. As a lessee, the company recognizes the right to use assets representing its right to use underlying assets, and leasing liabilities recognition of its obligation to pay for lease. In its operational results, the company no longer records leasing expenses by amount incurred and now records amortizations expenses of the rights to use and financial charges of interest rates over leasing liabilities. Thus, to ensure that the data is comparable, we reported 2018 pro forma results using the same criteria adopted in 2019. Having said that, let's move to the next slide to discuss our operational results.

Our volume performance grew 12.5% this quarter. Although we had operating restrictions in February due to heavy rains that caused landslides at Santos downhill. The good performance in January and the volumes in March resulted in a double-digit growth of transported volume in line with the plan. This result was mainly driven by: soybean performance that had its crop harvest as anticipated, resulting in higher volumes in January, a month traditionally impacted by off-season; fertilizer transported volume in the North Operation; pulp volumes, which grew 22.5%; and the increase on container transported, evidently a fast-growing operation focused on cargo diversification, narrowing the distance between the Southeast and the Midwest regions of the country.

Now let's move to the next slide. On the financial side, EBITDA grew 12.7% versus 2018 pro forma results and consolidated margin contracted to 49.1%. In the South and Container Operations, both margin and EBITDA posted improvements year-over-year. However, the North Operation lost margin due to lower volume expansions related to higher sugar trucking costs to accommodate higher soybean volumes; the acknowledgment of obligation from take-or-pay agreements due to low performance of volumes in February; lower tax credits this year compared to 2018. Now let's discuss the financial results and net income. Our financial results improved by 14.4% year-over-year reflecting the process of lowering cost debts as well as a CDI interest rate drop. Again, we delivered a quarter with net income, reversing the net loss in the same period last year, having the effect of EBITDA growth and improved financial results. Let's discuss our indebtedness on the next slide. Rumo's indebtedness came in line at 2.1x broad net debt EBITDA. We reaffirm our commitment to maintain our capital discipline, always seeking to sustain leverage within acceptable levels for the company.

On the next slide, I would like to share with you the market scenario for the upcoming months. Despite a domestic soybean production in line with market expectation, the grain export scenario is not favorable in the second quarter. A global oversupply and lower demand from China have been pressuring the international prices of soybean, thus, restraining exports. However, our take-or-pay agreement should increase Rumo's market share during this period, reducing impact in this conjuncture. On the other hand, the corn scenario is very positive. An excellent corn crop and anticipated harvest is expected, which should allow higher transported volumes in June. The high inventories of soybean will boost additional corn transportation pressure, which should remain strong during the second half of the year. As already mentioned by Beto, we will have the necessary conditions to deliver 2019 results.

FINAL

On our next slide, I would like to leave you with a message regarding our long-term guidance. In March, we held our Investor Days in Sao Paulo and New York, where we presented our 5-year plan. I have already mentioned this, but I would like to reaffirm here that this plan will bring even more returns than investments made up to now. Rumo is far from exalting its investment possibilities. We are prioritizing the best investment alternatives to create value for our shareholders, always with capital discipline.

Finally, going to our last chart. As everyone might know, we won the bidding process for the North-South Railway. This move expands Rumo's operational area, cultivating synergy among our networks while consolidating the company in Brazil's Midwest region. We already started to deepen our strategies and to incorporate this project in our strategic plan. In the third quarter, it will be operational as soon as possible after we sign the concession contract. That should happen in this year's second half. Therefore, it's expected that this railway starts to post revenue in the first half of 2021. We will keep the market informed on any development concerning this.

Here I finish our presentation. I'll now turn it over for the Q&A session. Thank you.

## Questions And Answers

### Operator

(Operator Instructions) Our first question comes from Josh Milberg, Morgan Stanley.

### Q - Joshua Milberg

You guys mentioned that you're seeing a pretty tough volume scenario for the second quarter. And I was just wondering if you could talk a little more about that and if you're seeing potential for your customers to incur take-or-pay penalties in the second quarter, rather than using their full capacity allocations? And I also wanted -- actually, if you could -- I was also hoping you could comment a little bit more on this opportunity that you mentioned to maybe anticipate some corn volumes in June?

### A - Ricardo Lewin {BIO 20342706 <GO>}

Josh, thank you for your question. Basically, we never were expecting the payment of take-or-pay from our clients, but that they will be able to load the -- our grains, okay? So we don't work with these expectations and we expect them to fulfil with the contracts that they have. The take-or-pay is basically a protection for us. That's not based on that, that we work our expectations. Regarding the corn harvest, we do expect an anticipation of the harvest and what can help the transportation of corn be anticipated. Basically, besides the anticipation of the harvest also that their warehouses are, in our opinion quite full. So it's expected that the start of transportation of corn is earlier, okay? Does that answer your question, Josh?

### Q - Joshua Milberg

Yes, that addressed it. And if I might just ask one more related to the take-or-pay contracts. Can you just remind us how much of your expected volume for the second half

of this year is covered by the take-or-pay contracts? Or do you prefer to frame it may be in terms of how much of your expected corn volume is covered?

**A - Ricardo Lewin** {BIO 20342706 <GO>}

Josh, unfortunately, we are not getting this -- anticipating this number for the market, okay? This is quite important for us in our negotiation with our clients and we are not supposed to disclose these numbers, okay?

**Q - Joshua Milberg**

Okay. Fair enough.

**Operator**

Bruno Amorim, Goldman Sachs

**Q - Bruno Amorim** {BIO 17243832 <GO>}

So I have two questions. The first one is on BR-163, assuming that the construction works at BR-163 would be concluded, let's say, by the end of the year, by mid next year. I know there are some trade tensions there, but assuming that's the case, to what extent that impacts your operations? Should that imply that you will likely have to decrease prices to some extent or not and why? And the second question is I understand that the second half should be much stronger because of the positive outlook for corn exports, but do you believe it's going to be enough to offset the eventual loss of soybean in the second half? Usually, soybean is exported in the first half of the year mostly. But last year, we saw very strong volumes vis-a-vis historical levels of soybean exports, possibly on the back of the trade tensions between China and the U.S. So are you comfortable with the better corn scenario fully offsetting the eventually lower exports of soybean in the second half of the year? Those are my two questions.

**A - Ricardo Lewin** {BIO 20342706 <GO>}

Bruno, thanks very much for your questions. Let's go to the 163 first. So I think you are being quite optimistic on having this -- on foreseeing that 163 will be ready in 1 year or so, okay? 163 is not only about finishing the unpaved piece of the road but also about maintenance of the entire road, okay? So in our opinion, you're being optimistic. But believing in what you said that this may be ready by the, I don't know, at the end of the year or so, that's not supposed to affect our operations, neither in volumes nor in prices, okay? This is a different -- up to now, this is a different area of -- East-West area, okay? And we don't expect to affect in the short term. Talking about the long term, once we view what the extension to Sorriso and as we're giving like our guidance, we are starting the first step of this expansion. We are supposed to be much more efficient than trucks. So we are supposed to get huge part of market share in the East-West area, okay? So it's not 163 that changes our plans in the future.

Regarding the second part of your question, that if corn will be enough to -- that there will be enough volume of corn to be in place of the losses regarding soybean. As Beto said in his message, we believe that there will be -- we foresee a record harvest of corn this

FINAL

year, okay, even what we put in our release that the most recent forecast that we have, that it will increase 23% of corn production in relation to last year. So we do believe that the reduction of soybean transportation will affect the final result, the guidance that we've provided to the market due to the quantity or the amount of corn that we'll have in the -- starting in the first quarter and finishing in the first half of the year and finishing in the second half. So we are very quiet positive with the portions of corn that we can transport. Does that respond to your -- or answer your question? Bruno, do you have any other doubts?

**Q - Bruno Amorim** {BIO 17243832 <GO>}

Yes, sure. No, that's clear. So just a quick follow-up on the first one. So you said that on your numbers, if you calculate the cost of the solution through the North, so assuming that BR-163 would be paved, the cost of transportation by road plus the cost of the transportation through waterways, that would be more costly than your cost as you go towards the north of Mato Grosso. Is that correct?

**A - Ricardo Lewin** {BIO 20342706 <GO>}

That's correct, okay. Don't take into consideration the truck prices that you see right now. The average truck prices, we have talked a lot with the market about that, are supposed to increase. Remember that the fleet is quite old without maintenance. Once -- if we have new ones, even if we believe that the minimum price table will work, truck prices are supposed to go up, okay? And on the other side, we are every year improving our cost and getting much more competitive. So in this sense, we don't believe that they will be competitive compared to us.

**Operator**

Our next question comes from Victor Mizusaki, Bradesco.

**Q - Victor Mizusaki** {BIO 4087162 <GO>}

I have two questions here. The first one is kind of a follow-up on your take-or-pay contract. I mean, for this year, results or the goal is kind of protect the company's take-or-pay contracts, but I don't know if you can comment about the time line, I mean what can we expect for next year? So what's the strategy here, given that I mean the tough situation in China? And the second one about your long-term business plan that you announced back in March. Just after you got the North-South Rail, so I'd like to know, first, if you need to prioritize the projects so that's why you didn't change your CapEx plan. And second, if it makes sense for us to assume that probably, I mean despite the concession fee payment, you talk about a project that can have returns similar to that related to Malha Paulista renewal.

**A - Ricardo Lewin** {BIO 20342706 <GO>}

Victor, thank you for your question. Regarding the first question about 2020, the take-or-pay contracts and the scenario, the tough China and other things. First, remember last year that the take-or-pay contracts were signed by the end of the year and in the beginning of next year for the first half of the year, okay? Remember that corn is always

FINAL

signed during the first half. This year, it's not supposed to be different. So we are not -- we haven't started to negotiate with our clients the take-or-pay contracts and we'll have the first indications by the end of the year, okay, maybe third quarter. So up to now, our expectations are positive, okay? And regarding 2020, many people have been doing questions about that, but just to be clear, the scenario for soybean for the first half of 2020 is quite unclear, okay? It's difficult to give any precise answer for that as we have several sectors or several issues affecting any forecast. So we can talk about China that -- our approach to the lack of bids, how much they can increase their poultry and fish farming, how much will have to be provided by other countries? So we have the swine flu that we don't know what percentage of hogs will be (inaudible). We have this discussion with the U.S. that is not improving the discussions. So there are many, many factors to give any forecast for 2020, okay.

Regarding the long-term business plan, if I understood your question, first question -- first half of the question was about prioritization of projects. We do -- we already have -- whenever we presented to the market our guidance, we do have -- we've prioritized our projects, okay, basically based on our obligations and the return of the project that we have. So this is done there. Remember that what's included there is part of Paulista corridor. Also the first step of the expansion to Sorriso, okay, that -- the road, the terminal. Okay, the truck terminal, the halfway between Sorriso and Rondonopolis. Part is maintenance or CapEx. So we do have a prioritization using this project, okay? After, you can say if you need any additional information on that.

And regarding North-South, we are not still providing -- if I talk to you about returns on that, I would give you a guidance on that. And as I said in my speech, we are working on including North-South in our long-term guidance and also in our budget for next year. So a bit more by the end of the year when we provide additional -- we'll provide the guidance and the budget, we will provide additional information on North-South.

## Operator

The next question comes from Rogerio Araujo, UBS.

## Q - Rogerio Araujo {BIO 17308156 <GO>}

I have a couple of questions. The first one, there has been some local news flow talking about pulp projects that could arise in Mato Grosso do Sul state and could use Rumo's Malha Norte services. So my question is regarding your expectations for pulps projects and also pulp volume for upcoming years. It would be great if we could hear some color on potential volume in new projects that could arise. This is the first question.

## A - Ricardo Lewin {BIO 20342706 <GO>}

Rogerio, if you're talking about the pulp project that we have been reading in the newspaper, what I can tell is that we are continuously talking to our clients, okay? So we are very close to the pulp producers in Brazil. You know about the projects that we already have with them. The point here is that you need to -- any pulp project will depend on the location of the plant and also the availability of terminals in the areas that we serve. So having this combination obviously, we are the best model, and the cheaper and more

efficient transportation model to do this, the transportation of this kind of cargo, okay?  
Does that answer your question, Rogerio?

**Q - Rogerio Araujo** {BIO 17308156 <GO>}

Yes, if you could give a little bit more color on volume. I think you do a little bit more than 1 million tons in North Operations currently. I think Malha Oeste did almost 1.5 million tons. So do you have any expectation for maybe 2023 where your long-term guidance is? How much you could be doing of pulp volume in the future?

**A - Ricardo Lewin** {BIO 20342706 <GO>}

Okay. Regarding 2023, right now, I cannot provide these volumes. I can tell that we do, in the North Operations, something around 3 million tons -- sorry, not only in the North but North and South Operations, basically, West, yes. Okay, part of the North-South system and we do -- we can do more than that, but we -- and we do consider that into our long-term business plan. However, we are not providing right now the breakdown of volumes, something that we can think about for you in the future, okay?

**Q - Rogerio Araujo** {BIO 17308156 <GO>}

Okay. Yes, sounds good. So my second question is, any update on Malha Paulista concession renewal? So the technical area from the Audit Court from -- TCU already analyzed it. They are renewed, so now it's in the hands Public Prosecutor and then ministers from TCU. Do you have any expectations for timing of either Public Prosecutor and then ministers of voting? And also after that, does the company expect the ANTT to sign the renewal soon or do you think the process could take a while? So any expectation for timing on that?

**A - Ricardo Lewin** {BIO 20342706 <GO>}

Thank you, Rogerio. I was missing this question, so thank you very much. Just to align everybody in the call, it's what basically Rogerio said, recently, we accomplished a very important milestone. The process received the endorsement of the technical body of TCU. Now the process is under analysis of the TCU Prosecutor, that's Julio Marcelo. And after that, it's going through the Minister of TCU in charge of the case that will present its recommendation to the other ministers who will then vote for this case, okay? And Rogerio, now answering your question, you know how TCU works. Of course, there is no deadline for this process. What we know is that the process is evolving very well. It's very much through the process, as I always say. We went through all the phases of the process and we do expect to be -- accomplish the renewal very soon. Unfortunately, I don't have a specific date to give to you.

**Operator**

The next question comes from Alexandre Falcao with HSBC.

**Q - Alexandre Falcao** {BIO 5515455 <GO>}

FINAL

Bloomberg Transcript



Just on the perspective, you said that it's going to be a tough year for -- it's going to be a tougher year for soybean. In your projections, do you already see an impact from the trucker's line figure that's impacting your numbers? And did you run any sensitivities that you could share on what could be the impact and is that basically diverting soybeans from exports to your local markets who produce pork and poultry?

**A - Ricardo Lewin** {BIO 20342706 <GO>}

Thank you very much. Let me start with what happened this year. The soybean production is in line with the market expectations and the grain export scenario is not as favorable as in the second quarter, okay? So we had an oversupply of soybean in the market that was caused by several different factors, there's the all-time high inventories in the U.S., unexpected all-time high harvest for soybean in the U.S. and the recovery in production, which you remember had a severe drop last year.

On the other hand, on the demand side, we had a weaker demand on China and this is the reason you said, the swine flu, which coupled with the oversupply -- or with the oversupply pressuring the international market for soybeans, okay? With the take-or-pay contracts, the agreement that we have, it's expected that we have a good ability of gaining market share during the second quarter, reducing the impact of all these factors for the company. With the answer that I gave in another that I had, like we have a very good scenario for corn. So the corn is anticipating its harvest, it's expected to be a record harvest that's going to allow us to transport more volumes in the end of this half of the year through the second half, okay?

So the soybean part of -- because of the demand, based on swine flu. As I have said in 2020, it's very unclear what will happen with the soybean, okay? Important thing to say that somehow -- and you gave some examples of what can happen, but somehow the market will have to adjust and to this new scenario, for current scenario. And one thing that's very important and few people talk about this, that 40% of this volume -- Rumo volume is not grains, okay? And in the other 60% that represents grains, we are talking about 50% being soybean and 50% being corn. And remember that corn is not exported to China, okay? So this must be taken into consideration while you make the analysis of the effects of swine flu in soybean exports to China, okay?

**Q - Alexandre Falcao** {BIO 5515455 <GO>}

Okay. And just a follow-up on North-South. So realistically, when can we expect anything on in terms of volumes coming from that? And what is necessary for -- to integrate that, just trying to understand, and importantly so that I'm aware, when should we see any sort of volumes coming in from that operation?

**A - Ricardo Lewin** {BIO 20342706 <GO>}

So basically, as what we said in our last few slides or pages, just so you have an idea, we are supposed to have the contract signed in the beginning of the second half of the year, so 2019. Then we will start to do our investments in the North-South for the next 1.5 to 2 years. And in the second half of 2021 is when we are expected to have the first volumes or significant volumes transported in this quarter.

## Operator

The next question comes from Rogerio Araujo, UBS.

### Q - Rogerio Araujo {BIO 17308156 <GO>}

It's a follow-up on the contracts actually. So just to confirm, if I heard it well, I think you mentioned that you signed soybean and corn contracts separated. Is that right? So if it is, how is the corn contracts going into this -- so are you negotiating the corn contracts at this moment? How are them? And when do you expect to start the negotiation of soybean?

### A - Ricardo Lewin {BIO 20342706 <GO>}

Rogerio, remember that Brazil has two very clear and different harvests. In the first half of the year, this first quarter, you have the soybean harvest. So you usually sign contracts with your clients in October, November, December, okay, through this first half of the year. Then, you'll start to have an idea how the corn crop will be in the next year, that usually happens in the second half, and we start to sign contracts in February and March, okay? So there are two different timings for signing this contract.

### Q - Rogerio Araujo {BIO 17308156 <GO>}

Okay. So can you give any color on how those negotiations went on February and March?

### A - Ricardo Lewin {BIO 20342706 <GO>}

As I said I think to Josh, Rogerio, this is a very important information and it is very key for the negotiation with our clients. So we don't disclose this kind of information.

## Operator

(Operator Instructions) The next question comes from Josh Milberg, Morgan Stanley.

### Q - Josh Milberg {BIO 19336060 <GO>}

You guys addressed pretty well the factors behind your yield performance in the first quarter. But looking forward, I was just hoping you could give us a little bit of a sense of what we might see in the second quarter and in the second half of the year yield wise. You guys did have a bit of an improvement in the first quarter relative to the what we saw in the fourth quarter and we understood that some of the factors there, you highlighted the mix factor. In the Northern Operation, it was still somewhat on the weak side. So again, I was just hoping you could maybe address what you're seeing for the second quarter and beyond?

### A - Ricardo Lewin {BIO 20342706 <GO>}

Josh, let me just start saying that I always say to the sell side and our investors that this is not a company based in yield but a company based on margins. So you know our use case is based on being more competitive, reducing our variable cost, diluting our fixed costs. What make us every time more competitive, getting more volumes and having this virtuous cycle that we are seeing in the last three years in the company. So I think that I will

FINAL

repeat that because it's very important: this is -- the company is more about margins than yield. Having said that, I think that just to understand, remember that we are -- the pricing system change gives more -- is different through the year. So when you have -- and please don't take it that I'm evading that question. I will try to be clear here. The first part to that, we have a more strong soybean transportation. There is higher prices in the second quarter, in the second half -- I said in the first quarter of the year, and you have prices that are changing during the quarters, depending on basically the size or the volume that are transported. I'm not saying that this is connected to -- this is not contracted and that means it's not in our contract, but this is how the market prices the transportation. So different quarters have different prices. And you will see this in the variations of what we provide. Additionally to that, there are changes in the yield, depending on the mix of volumes that you transport. So when you have more fertilizers, you have more pulp, these products have lower yield and this can affect the total yield. So there are different factors that can affect the yield. And this is important for you to know. Regarding the second quarter, the second half of the year that you're asking, so it's basically like I said, you can see a flat yield for the next -- the first quarter of the year and for quarter, maybe a bit low priced as it stands of the corn crop, okay? If there is any change on these scenarios, we will provide additional information in the releases of the respective quarters.

## Operator

That concludes the question-and-answer session for investors and analysts. Now I would like to turn the floor over to Mr. Ricardo Lewin for his final consideration.

## A - Ricardo Lewin {BIO 20342706 <GO>}

Well, once more, I would like to thank the active participation of our investors and sell side, and thank you very much. Hope to talk to you in the next quarter. Thank you.

## Operator

That concludes Rumo's first quarter results conference call. Thank you.

*This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2022, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.*