

## Q1 2021 Earnings Call

### Company Participants

- Gustavo Werneck, Chief Executive Officer
- Harley Scardoelli, Executive Vice President, Chief Financial Officer and Investor Relation
- Rodrigo Maia, Investor Relations General Manager

### Other Participants

- Caio Ribeiro, Analyst
- Carlos de Alba, Analyst
- Daniel Sasson, Analyst
- Eduardo Cavalheiro, Analyst
- Geraldo Mellone Junior, Analyst
- Leonardo Correa, Analyst
- Marcelo Audi, Analyst
- Marcio Farid, Analyst
- Rafael Barcellos, Analyst
- Thiago Lofiego, Analyst
- Unidentified Participant

### Presentation

#### Operator

Good afternoon, everyone. I am Rodrigo Maia, Investor Relations of Gerdau. Welcome to Gerdau's First Quarter Earnings Results in the first time using video conference platform. Here today is Gustavo Werneck, CEO of Gerdau; Harley Scardoelli, CFO, who will present to you today. All analysts and investors can send your questions through the chat, and then the questions will be answered by both Gustavo and Scardoelli after the presentation.

I would like to clarify that any information, forward-looking statements that might be made during this conference call related to Gerdau's business outlook, projections and financial and operating goals are mere assumptions based on the management's expectations related to the future of the company. Even though Gerdau believes that its comments are based on reasonable assumptions, there is no guarantee that future events will not affect this evaluation.

I would now like to turn the floor over to Mr. Gustavo Werneck. You may proceed, sir.

## **Gustavo Werneck** {BIO 20318216 <GO>}

Thank you, Rodrigo, for this brief introduction, and good afternoon, everyone. I would like to start by welcoming each one of you to our conference call to discuss Gerdau's results related to the first quarter of 2021. This is the first time we present with audio and video. And this is an attempt to be more aligned to the reality of our society today. I hope you are still well and healthy and also going through this period the best possible way. On our side and speaking on behalf of our 30,000 employees, we've managed to remain healthy and safe and keeping our well-being, and also pursuing an adequate routine in all of our operations by rigidly comply with all of the health and sanitary protocols established by the local authorities.

In this last quarter, we did not have any interruption in the production of our industrial plants attributed to COVID-19. As mentioned by Rodrigo, also joining us today is Scardoelli, and for both of us it's always a pleasure to talk to you about our performance and also clarify possible issues that may come up during this presentation.

Scardoelli will start by talking about the highlights of the overall results of the quarter and also he will talk about the performance of our operations. After that, I will return to talk about the markets where we operate and also share with you some thoughts about what we see the landscape going forward. And then at the end, we will both be available to talk to you and discuss any issue you want us to elaborate further.

So, Scardoelli, the floor is yours. And we can then start talking about our results.

## **Harley Scardoelli** {BIO 7283603 <GO>}

Thank you, Gustavo, very much, and good afternoon to you all. It's a pleasure to be with you using this new format, which I think will be very good both for us and for those joining us today.

We will start the presentation with the first slide, when we look at our financial results, and we will also talk about the main factors that impacted our consolidated EBITDA. We went from BRL3.1 billion in Q4 of '20 to BRL4.3 billion in Q1 of '21, and this was a record EBITDA for Gerdau in a single quarter.

All of our operations had an excellent performance in the first three months of the year. And this was not only due to a favorable moment for the steel industry, but also as a result of our diligent capital allocation of the last few years in our operations. These investments helped us to be more agile and efficient to capture all the profitability gains brought about by the current scenario. This quarter we also had an excellent performance of our North American BD that reached BRL843 million or 50% above the EBITDA of the last quarter of 2020 with an EBITDA margin of 14.3%, approximately 4 percentage points above the margin of the fourth quarter of 2020. This result reflects the rebound of the non-residential construction sector and industry in addition to the gradual return of the activities that favor our industry as the vaccination campaign advances in the country.

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Brazil's BD posted a strong performance once again with an EBITDA of BRL2.5 billion in Q1 and an EBITDA margin of 36.9%, which is another record figure for Gerdau in terms of a single quarter EBITDA. Brazil remains strong in the main steel consumer sectors, and therefore we are allocating a large portion of shipments to the domestic market. I can even say that this quarter we were focusing almost 100% in Brazil, leaving only 4% of shipments to the foreign market.

The South America BD posted a performance similar to that of Brazil with an EBITDA of BRL550 million in a margin of 38%. This operation has also benefited from the good performance of the civil construction industry particularly in Argentina and Peru.

And last but not least, our Special Steel operation due to the rebound of the automotive industry in Brazil and the gradual recovery of the United States showed a very good performance in the first quarter of 2021, posting an EBITDA of BRL409 million and an EBITDA margin of 16.8%. In the first three months of the year, the steel utilization capacity of the Special Steels operation was 83% when compared to 78% utilization in the fourth quarter of last year.

Now moving to next slide, Slide number 3. We will talk about free cash flow and working capital. As we can see, on the left hand side of the chart, our positive free cash flow was BRL1.1 billion in Q1. I would like to emphasize that this is an unusual cash flow for the first quarter at Gerdau. But this result was possible due to a substantial improvement in the indicators that contributed to this calculation. Starting with a historical EBITDA, as explained in the previous slide, it reach BRL4.3 billion.

In addition, this performance was also attributed to the way we manage our assets in the past few months, which reduce the exposure to our growth -- of our growth that to foreign currency, and as a consequence minimize the impacts from the exchange variation effects over interest of the debt. In the last 12 months, cash flow was positive by BRL6 billion, reflecting our efforts and commitments to the adequate remuneration of the invested capital, coupled with the company's commitment to its liquidity position which has been kept quite strong.

And the chart on the right shows the cash conversion cycle that went from 49 days in December of 2020 to 57 days in March of 2021, mostly attributed to the accounts receivable and inventories, given the fact that global demand for steel remains at all-time high levels. This is a more balanced cash conversion cycle for our industry and Gerdau.

Now moving to our next slide, we will talk about our debt position. I would like to underline that at the end of March, our net debt was BRL10.8 billion slightly higher than the net debt reported at the end of 2020 due to the impact from the exchange rate on the debt denominated in foreign currency. The Brazilian real depreciated approximately 10% vis-a-vis the U.S. dollar between December 2020 and March of 2021.

Currently, 77% or approximately BRL14 billion of our total debt amount is denominated in U.S. dollars. It's worth mentioning that in the last few quarters, we implemented a strategy to reduce the foreign exchange exposure of the debt and take advantage of the

opportunities brought about by the current scenario of interest rates in Brazil. Therefore, we increased our exposure in Brazilian reais to about 23% of the total debt to protect ourselves from the high volatility of the dollar as seen lately. This level puts us closer to a natural hedge given that a substantial part of our EBITDA is generated in U.S. dollars, in addition to the fact that a significant portion of our assets and operations are located in North America.

I would also like to highlight the 99% of this debt is long term. As we can see, if you look at the right side of the slide, with an average life of eight years and nominal average cost of 4.8% in the year, the debt amortization schedule is distributed along the next coming years and more concentrated only after 2027 or 2028.

And finally, on Slide 4, it's important to mention the result of the financial leverage, measured by the EBITDA over net debt ratio of the last 12 months, which went from 1.25 times in the fourth quarter of last year to 0.96 times in the first quarter of '21 as a consequence of the strong EBITDA generated in the first quarter of 2021. With this kind of leverage, we would like to point out that for the second consecutive quarter, we have reached the goal set forth by our financial policy and approved by the Board of the company which still keep this ratio between 1 and 1.5 times net debt over EBITDA ratio.

Moving now to next slide, Slide 5. Here I would like to show you the evolution of the company's return on capital employed. This is a very simple slide, but it shows that in the last 12 months, we were able to reach returns of 14.2% on capital employed and this was higher than the return of the last four years. And certainly this is translated into value generation to our shareholders and investors and also is translated into higher value of our shares traded in the stock market as we have seen in the last quarters.

Now going to Slide number 6. Now here we can conclude and the last slide shows the evolution of net income and dividend payout in the last few years, demonstrating that a combination of better results and the significant reduction of our net debt had a very positive effect on the dividend yield, meaning the percentage of dividends and interest on equity paid over the closing share price at the beginning of each period going from 0.7% in 2017 to more than 8% in the last 12 months. This is a very significant increase.

So thank you very much for your attention, and I will turn the floor back to Gustavo, who will comment on the market outlook.

**Gustavo Werneck** {BIO 20318216 <GO>}

Thank you. Scardoelli. Thank you for the first part of the presentation.

So please let's go to our next slide, Slide number 7, and here we will talk about how Gerdau's -- we'll talk about Gerdau's performance in the first quarter of 2021 and the global landscape for the steel industry. As we heard from Scardoelli's comments on Gerdau's performance in the first quarter, I would like to split this slide in two blocks. So first, we will talk about the market. But we also understand the part of the results that we achieved in the first quarter stem from all of the benefits we are reaping through this

intense transformation we've been going through in the past few years. This led us to be lighter, simpler and more agile. And I would also say that we are ready to deliver greater value to our customers.

As a result of this simplification of the company, SG&A expenses this quarter accounted for less than 3% of net revenue or net sales when compared to 6% that we had five years ago. And this is the equivalent to savings of approximately \$300 million every year. By the same token, our digital view that aims at integrating and optimizing all of our operations, ensuring total customer focus, ensure this financial gains of almost BRL700 million since 2018. I think a good example of this initiative is the number of new customers in business that were captured through the digital channels. More than 3,500 customers bought still online in the first quarter of the year, and another BRL35 million came from new sources of digital revenue. And all of that was added to our long and flat steels operations in Brazil. And as I was saying, we also benefited from the strong consumption of steel in the countries where we operate, particularly in Brazil and in the United States.

Global production of crude steel grew 10% in the first half of 2021 when compared to the same period of last year. According to data from worldsteel, and still according to the association, demand for steel should grow 5.8% this year, and another 2.7% in 2022 when compared to 2021. So these numbers stress the importance of steel as an essential input, and also a moment of strong recovery of the global economies. And to conclude the comments about this slide, in the last 12 months, we continued to put emphasis on the health, safety and well-being of our people as the pandemic continues to unfold.

Now let's move to the next slide, Slide number 8. And here, I will talk about the markets and how Gerdau's operating these markets [ph] and also the outlook looking forward. This time, I will start by talking about our North America business operation. And our volumes in North America are still very high in the first quarter of the year with a very strong order inflow coming from the construction industry and we are also posting better economic indicators with the advance of the vaccination plan in the U.S.

Metallic spread experienced a significant increase in the period, despite the higher prices of scrap in the local market in the U.S. Also it's important to mention that our internal efforts to reduce costs and increase our portfolio focused on fully serving our customers, which allowed us and still allow us to capture new business opportunities, and in turn deliver even sounder results.

With this backdrop, and as part of our strategic roadmap for North America, we recently concluded the modernization and technological updating of the structural steels and profiles, rolling mills of the Petersburg and in Cartersville units in the states of Virginia and Georgia, respectively. This allowed us to expand our product mix to the market and we were able to offer steels of higher added-value. In addition, we are moving forward with our expansion and technological updating project at the Whitby's melting shop in Canada. So coupled with these other investments that are part of our roadmap, as I said before, we offer a product mix of higher added-value.

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Looking ahead, still speaking about our North America operation, the landscape there is quite positive. Just to give you an idea, currently our order backlog in the U.S. is the equivalent to approximately three months of purchases, mainly attributed to the robust activity coming from the construction sector, with construction projects in progress from December to February, accounted for approximately \$300 billion. And this represents an increase of 6% year-on-year according to the statistics agency of the federal government of that country.

Also we remain very optimistic with the possible effects of the investment package for infrastructure, recently announced by the Biden administration, that contemplates the generation of several jobs and investments of over \$2 trillion in the country in the next eight years, including \$115 billion of investments in highways and bridges. So these are two strong steel consumers. And the North American Steel Association, known as AISI, estimates that every billion dollars spent in infrastructure generates steel consumption of approximately 50,000 tons.

In this regard and if you add up, steel demand is anticipated to add another 3 million o 4 million tons of steel a year, according to the analysis from KeyBanc Capital Markets. Moreover, we believe that the executive order that focuses on increasing federal purchases of local content made in America, together with all of the measures -- commercial measures to imports [ph] to contribute further to maintain the utilization capacity of North American mills at high levels. And in our case, this would be above 90%.

Well, now we'll refer to our Special Steels operation both in the U.S. and Brazil, and I would like to start with the United States. There demand follow the higher-than-expected performance of the automotive sector, heavy vehicles, distribution and also oil and gas. 3,600,000 units were produced in the first quarter of the year, growing 11.3% when compared to the same period of 2020, where 78,000 units of heavy vehicles were produced between January and March compared to 60,000 the year before. And for this year 2021, the forecast points to a significant growth going from 214,000 units to 298,000 units, indicating increased investments in logistics due to the economic rebound in North America.

Another number that I always like to mention is sales of tractors. Sales of tractors are also showing a gradual recovery with a 41% increase in sales in February, reaching 16,200 units. By the same token, the oil and gas segment posted growth of the so-called rig counts with 527 units opened in this first quarter. The forecast indicates an increase in the activities in the coming months following the recovery of oil prices, and this is something new in terms of our shipments when we compare it to previous quarters.

And in addition to that, I would like to mentioned the successful transfer of capacity from the Jackson mill capacity in Michigan to our other special steel plants in the United States, allowing us to grow shipments and deliver more innovative products with higher added value to our North American customers.

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Now going to Brazil and still talking about Special Steels, the demand for Special Steels in the first quarter was very strong in line with the move to replenish the inventories of the automotive industry that posted a 2% increase in the number of units produced in the period when compared to the same quarter of last year. And this was mostly boosted by the excellent results coming from trucks and light commercial vehicles according to data from Anfavea.

We anticipate a positive scenario for the sector in regards to Special Steels with continuous replenishment of light vehicle inventories and increased production of heavy vehicles, due to the favorable momentum of agrobusiness with a record crop season and also the renewal of the fleets that are already taking place this year. We also noticed an increased demand abroad for Brazilian products of the automotive chain and this has led many of our customers to redirect shipments to the international market in a very competitive way.

So in view of all of these good prospects in the markets, we continue to invest in our Special Steels operation. And more recently, we announced that we invested BRL1 billion in the modernization and the expansion of our Special Steels operations in Brazil. This investment of BRL1 billion contemplates the installation of the new continuous casting that is scheduled to start up in the midst of 2022 in the Pindamonhangaba unit in Sao Paulo, and also the inauguration of our new annealing furnace and spheroidizing of steel bars at the Charqueadas plant in Rio Grande do Sul to be inaugurated also next year.

This investment in Charqueadas will certainly bring the leading-edge technology and increased capacity and higher productivity to the thermal treatment process of the unit. Also recently, we announced, and I would like to stress that, we announced the restart of the melting shop at our mill in Moji das Cruzes also scheduled to start in the second half of 2021. We continue to closely follow the needs of our customers making quick decisions all in line with the current trends in the market.

Well, now, I'll shift gears and I will talk about our operations of long and flat steels in Brazil. We can see a very positive landscape. The performance in the first quarter of the year reinstate the rebound of the sectors that are heavy steel consumers, and we also see a positive outlook for the remaining of the year, not only in the second half of the year, but for the entire year of 2021. According to data from Instituto Aco Brasil, the apparent steel consumption in the country was up 32.8% in Q1 year-on-year with domestic sales growing 29%. And our internal number reflects the number of construction sites, which continues to increase. Sales were up 4% in the first quarter vis-a-vis the fourth quarter of 2020, thus reflecting the positive trend in the real estate sector.

Another important indicator is the increase in mortgage loans that at the end of 2020 reached almost BRL124 billion, growing 57.5% year-on-year. And we do believe that mortgage loans should experience an additional increase of 27% this year, reaching BRL160 billion according to the Brazilian Association of Mortgage Loans and Savings. Our deliveries to the construction sector grew between January and March of this year. They grew 8% when compared to the previous quarter and 45% when compared to the same period of the previous year.

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We also believe the real estate launches should continue to grow. And we follow (inaudible) estimate, which poses growth of 38% this year. On the other hand, retail sales, I mean we saw a certain stability in the last quarter, but still retail sectors are kept a high level. So for 2021, retail is expected to grow 3.5%, according to estimates from Abramam and Anamacom.

I would also like to say that we welcome the recent news about privatizations and infrastructure projects announced by the government, which points to the rebound of the segment with estimated investments of around BRL127 billion this year, according to data from the Brazilian Association of Infrastructure and Basic Industries.

Now moving to the Industrial segment, another important segment for our Brazil BD, this quarter we saw the continuity of the strong recovery of all consumer segments, driven by the growth of the domestic market. But also this quarter we saw the reorganization of the global supply chains that offered important opportunities to our customers to expand their exports of capital goods, agricultural machinery, yellow line equipment and road implements our shipments of longs and flats. We're up 3% in the first quarter when compared to the fourth quarter of 2020, and 25% year-on-year.

Moreover, there was a shift in consumption from imported materials to locally produced steel in the period. Therefore, the landscape remains positive and the industrial GDP should be up 3.5% in 2021, according to the National Confederation of industries, and this also encompasses agricultural segment, yellow line equipment and road implements. I would like to emphasize that our focus remains in the full supply of the domestic market. Therefore, we reduced our exports in this first quarter.

Also, we are very pleased with the investment in the Silat mill in Ceara that allowed us to serve the specific needs of the market in the North and Northeast regions of the country. These markets usually consume expanded and ready-made products. And so we expedited the progress of these products to help them boost their construction projects. We intend to increase our presence in these regions with the production of these items at our Silat unit, and we believe this will be an important asset to serve the future market for steel, not only in these regions, but also we will be able to redirect the production today from our units in the Southeast that we sent to the North and Northeast. So when we localize the production, in these regions, we can certainly expand our footprint in the Southeast as well.

I would like to state when we announced that risk -- with the intent to strengthen the supply of products to clients all over the country, to strengthen the existing capacity, we decided to restart of production of steel in our Araucaria mill in the state of Parana starting in the second half of this year. With this additional annual capacity of 420,000 tons of crude steel, which is the capacity of the mill. So with that, we strengthen our capacity to fully serve the demand of the domestic market, particularly in the sectors of civil construction, infrastructure and the industry.

So very quickly speaking about our last business operation in South America, demand for longs in Argentina is quite positive, and this is mostly attributed to the recovery of the



industry, mainly driven by the agriculture and livestock sector, white line and automotive sectors, combined with the good performance from civil construction, boosted by private investments and also public infrastructure projects.

The last figures from the Institute of Statistics of Argentina, INDEC, indicates that the construction activity in the country grew more than 23% in the first two months of the year, meaning January and February, and we believe that this points to a very positive trend in March.

Shipments to the domestic market in Uruguay are also quite positive and we were able to reach all-time records in terms of product shipments in the first quarter of 2021. And another country, I would like to mention, is Peru. In Peru, steel consumption remains at high levels, mostly driven by the civil construction sector that has been posting positive performance in the last six months, as a result of public investments and the good performance of the retail sector.

GDP and Peru grew for the first time in five quarters, growing 5% between January and March, and then year-on-year comparison according to the central bank of that country.

So that concludes that slide, and now we will move to Slide 9 to talk about CapEx. Here we invested globally throughout the first quarter BRL435 million in fixed assets. The estimated use of CapEx for 2021 remains at BRL3.5 billion, already contemplating the amounts that were postponed at the beginning of the pandemic, in the beginning of last year. This amount includes, for instance, investments in (Technical Difficulty) in Brazil, as mentioned earlier. And I would also like to say that we continue to be very rigorous in our decisions to allocate capital and approve new investments, maybe as part of all of the lessons learned from past CapEx disbursements.

I will now go to Slide 10. Here, I would like to make a few comments, on this slide and next slide as well. They reflect important investments. As I mentioned before, when I talked about our strategic roadmap in North America, once again I would like to highlight the conclusion of the investment in the long steel mill of Petersburg and Virginia, which is an important landmark that will better serve customers in North America. With an investment of \$33 million, we modernize the plant including the technological updating of our structural steel rolling mill.

With that, we will ensure greater efficiency and higher productivity of that unit. And by the same token, we will be able to expand the mix of products of higher added-value like beams and sheet piles which are two products that are very much in line with the future needs coming from the construction sector in North America.

Now let's move to next slide, Slide 11. Here, I would like to highlight development of construtech Brasil ao Cubo, where we hold an equity interest, which has been announced some time ago. In addition to building a new center for the treatment of COVID-19 offering 14 new beds in Sao Paulo and delivered at the end of April. Brasil ao Cubo concluded last month the construction made in only a 100 days of the first eight-storey high commercial building in the town of Tubarao, Santa Catarina, using a technique of

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modular construction that uses steel as the main raw material. This is the first modular multi-storey offside building in Latin America.

Therefore, we remain firm in our commitment to contribute to reduce the productivity gap of construction in the country with constructions of this kind. And by the same token, we will continue to encourage the industrialization of this sector. Furthermore, last month, we announced the launch of Gerdau Graphene, a company focused on the development and commercialization of products with the application of graphene. This new company is part of the portfolio of Gerdau Next, new business division. And as I said in previous occasions, this division is focused on venturing into new segments besides steel. The company will offer more technology to the civil construction industry, Industrial and Automotive lubricants, rubbers, thermoplastics in general, paints and sensors not only in Brazil, but also in countries in Latin America and North America.

More recently, we announced a capital injection of BRL100 million proportional to the stake of every partner at Juntos Somos Mais. It is the largest marketplace of civil construction in the country and this investment is a sign of our optimism with the steel market in Brazil and also reflects our strategic view of innovation and distribution.

To give you an idea, today, about 30% of all the retail business from our distribution arm (inaudible) Gerdau already come through this platform, with the fund -- this funding is part of a growth plan to be accelerated in the next coming years, and the injection will be used to grow the ecosystem and its functionalities like the technological updating of the virtual store and also the development of other new business opportunities.

Furthermore, still speaking about Juntos Somos Mais, this capital injection will be used in the implementation of new initiatives in the B2C sales channels, because Juntos Somos Mais since 2020 has been working not only to strengthen the B2B marketplace but also focuses on the final consumer.

And finally, I would like to highlight that steel sales via the platform Juntos Somos Mais grew more than 16 times in the first quarter of 2021 when compared to the first quarter of previous year.

It's also important to mention that we concluded our inventory of greenhouse gas emissions. This inventory was audited by the Totum Institute that indicated a carbon intensity of 0.93 tons of greenhouse gases emitted for each ton of steel produced. This amount is almost half of the average of the global steel -- the global for the steel industry of 1.83 tons of greenhouse gases emitted, and this was disclosed by worldsteel.

Also Gerdau adopted the curve methodology MACC, the famous MACC curve, which stands for Marginal Abatement Cost Curve to restructure its targets for short, medium and long term targets. The purpose of the study is to learn about the technologies available and also technologies still in progress that are pertinent and feasible to the steel-making process used by the company. Also, it will allow us to analyze those that are more eligible, we will be able to prioritize and plan the initiatives and investments. And then we will be

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able to disclose them to the external public over the years, what are our goals for greenhouse gas emissions reduction based on that methodology called MACC.

And finally, approaching a conclusion, I would like to render a special thanks to all of our employees for their dedication in the first few months of 2021. Certainly your efforts combined allowed us to reach sound results and to be even closer to our customers. This is a special thanks on my behalf and on behalf of all of the other colleagues that are present here today.

So now, Scardoelli and myself will be available to answer your questions and clarify possible issues. I will now turn the floor back to Rodrigo, so Rodrigo can help us organize the Q&A session. So, thank you.

## Questions And Answers

### A - Rodrigo Maia {BIO 19840176 <GO>}

Thank you, Gustavo. We will now initiate the Q&A session. We received many questions through the chat box. The first question comes from Carlos de Alba from Morgan Stanley.

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

Do you see any possibility of further improvement in the landscape in 2021? Do you see any further potential for the company to deliver a special dividends, to pay out special dividends? Thank you.

### A - Gustavo Werneck {BIO 20318216 <GO>}

Well, thank you. Let me answer Carlos' first question about the landscape and what we see going forward. And then I'll give the floor to Scardoelli who will help us with the second part of the question about dividend payout.

Well, certainly we see the possibility to expand our results in the second half as -- and the second quarter as well, as I said during my speech, whatever we look in different geographies, in our different businesses, we see many positive signs not only in terms of maintaining demand, but growing the demand for steel. I mentioned the case of Brazil, where the demand for steel in the construction industry remains very strong. Without mentioning more numbers, all of the numbers are public, but looking at our own case, we just look at the growth in construction sites. So this is increasing every month, and I believe that this is a sign that shows how strong the sector is. More recently, we had some infrastructure auctions, and we anticipate an increase in the demand for steel.

The industrial sector as I said, not only the domestic market is quite strong, but our customers are also identifying many opportunities to export locally made products, products made in Brazil. So this has encouraged demand and consumption of steel. And in the U.S., I just gave you this very positive outlook going forward. This deal recently announced by President Biden reinforces the positive outlook, not only if you look in the

short term, but looking forward -- going forward next year and this encourages to say that we believe that we will be able to expand or to grow our results further down the road.

So now, I'll give the floor to Scardoelli to elaborate on the dividend payout issue.

#### **A - Harley Scardoelli** {BIO 7283603 <GO>}

Perfect. Thank you. Thank you, Carlos, very much for your question. This is a very recurring question especially in view of the good improvement in our results. I would like to say that our dividend payout policy set up a percentage over net income and not as it's common in the U.S. when companies set up dividend payout based on cents per share, but this has an automatic adjustment based on the results. So with the improvement of our EBITDA -- in terms of EBITDA and net income, we have some fixed expenses. So the EBITDA improvement, represents a better improvement in terms of net income.

So dividends are in fact increasing, the dividend payout is increasing. At first, we are not contemplating any changes to our dividend payout policy. I would like to remind you that now that the Board just approved BRL0.40 per share for Gerdau and BRL\$0.20 at Metalurgica. This is the equivalent to almost the totality of all of the dividend paid out last year. Therefore, dividend -- the dividend payout has been adjusted. Going forward, certainly we can revisit that topic, but the dividend policy still remains at 30%. But again, we are generating some strong dividends and I showed during my presentation that the dividend yield considering the beginning of the period, if you consider the last 12 months is already at 8%. And if we take the dividend that is being paid out this quarter, and if we just annualize it, the dividend yield would be at around 5%. Therefore, it is quite strong due to our more robust results.

#### **A - Rodrigo Maia** {BIO 19840176 <GO>}

Thank you. Our next question comes from Caio from Credit Suisse.

#### **Q - Caio Ribeiro** {BIO 18420483 <GO>}

And the question is related to your last comment. Capital allocation with leverage going below one time the net debt over EBITDA ratio, do you think there is a likelihood of dropping even further? So what would be Gerdau's capital allocation going forward?

#### **A - Harley Scardoelli** {BIO 7283603 <GO>}

Well, in a way, part of that question that is linked to the dividend part, and I think I already answered that in my previous answer, in terms of capital allocation, we should also remember that we will still have a very strong cash generation. But we also have a more robust CapEx program for this year. Even though we spent BRL400 million in the first quarter, we intend to spend BRL3.5 billion throughout the year. And I link CapEx investments with a slide that we also showed you related to return on employed capital. So our level of ROCE is 14% with lower leverage, that means the return that goes straight to shareholders.

So what do I mean by that? Dividends remain strong and CapEx based on ROCE, today the return is already quite high. Therefore, we believe that the return in terms of results to shareholders is well equated in view of the good returns of our employed capital and as a consequence our CapEx.

## Operator

Thank you. Our next question is from Daniel Sasson from Itau Bank.

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

Now looking beyond the second quarter in terms of contracted volume better prices international market in Brazil, do you believe that the margins could be sustainable going forward, margins above 35%? If you could elaborate a bit about the global dynamic related to steel exports to China, I think this could be helpful? Thank you.

### A - Gustavo Werneck {BIO 20318216 <GO>}

Let me answer that question, and Scardoelli, please feel free to add. As I was saying, Daniel, it's a pleasure to talk to you. Today we see a structural condition in the next coming quarters. We believe that these margins will be maintained. But even more than that, to answer the second part of your question, which was a very good question, my reading right now about all of the variables that I can see before me is that may be there is a structural change in the worldsteel scenario.

Maybe, if you look at those landscape in the longer term, it will be different than what we saw in the past 10 years. And a good part of that is linked to the moves coming from China. And as you know, China has a very intense influence on the global steel market. Changes like that not only this -- this thing that you've mentioned, the discount rate for several steel milling products that was in force since May 1st like rebar, wire rod, et cetera. But at the same time on the same day, we heard about a policy to readjust import taxes and various raw material aiming at reducing import costs. And these changes can be seen in the short run, but for me, I see them in the long run, in a long-term.

Another point that also indicates long-term changes in China refers to the very strong growth in steel production in China through electric furnace or through scrap. So China increase it's production of electric furnace from 15 million tons a year to a production close to 200 million tons a year of steel production via electric furnace. This will put pressure on the global cost of scrap and this is something that we haven't seen in the past few years. And this represents an important structural change that should be noted.

And also the Chinese government is making continuous efforts to reduce GHG emissions, and this is something that is here to stay. China is giving clear signs according to my reading that very important changes will take place in the next coming years. I would just like to emphasize that the next quarters, I mean the fundamentals are very sound. But if you look in the long-range, I believe that we will experience a cycle of many years where results will be more robust unlike what we experienced in the past 10 years.

So, Scardoelli, if you want to add anything, please feel free to do so.

**A - Harley Scardoelli** {BIO 7283603 <GO>}

No. Thank you. Gustavo. You said it all.

## Operator

Our next question comes from Thiago Lofiego from Bradesco.

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

The margins of your North American BD are still growing in the second quarter as volumes are better and the spread is higher. And his second question is in your Special Steels business do you feel any impact in demand for lower -- because of the lower production of automobiles?

**A - Harley Scardoelli** {BIO 7283603 <GO>}

Let me answer that. Thiago, thank you for your questions. Our long steel operation. In that regard, we see an even more positive landscape. Demand is quite strong, and with this good outlook of an expansion in the next coming quarters, with the recently announced infrastructure package, in fact what we see is that our spreads are growing even with the increased price of scrap. So, in North America, the landscape is positive.

Now speaking about Special Steels, we haven't been quite impacted with the difficulty to produce vehicles, not only in the U.S., but also in Brazil because we see a strong recovery in the inventories of steel. In the U.S., there are about 400,000 vehicles still parked in the yard of the OEMs, still waiting for electronic components. This obviously increases the difficulty to expand the fleet of vehicles. But in our case, we didn't feel any strong drop, because of the renewal in inventories. And this happens in Brazil as well. And what we anticipate in the next quarters is that this will be gradually stabilize and to be finally stabilize in the fourth quarter. And in our case, in the case of Special Steels, right now we believe that the impact in our case will be very mild and much lower than the rest of the chain.

## Operator

Okay. Thank you. Our next question comes from Leonardo Correa from BTG Pactual.

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

How is your order portfolio and inventory levels in Brazil? How long do you think it will take for the inventories to be replenished? Are we looking at a new level of EBITDA margins in Brazil? The competition is -- there is a big debate about re-currency. They see 30% margins as being the new normal. This is a similar question as the one to ask before in relation to the margins in Brazil?

**A - Gustavo Werneck** {BIO 20318216 <GO>}

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Okay. I can answer that as well. The inflow of orders, as I said in all segments, remains very strong. We see new portfolios being very robust looking forward and has allowed us to have a more intense replenishment of inventories. But I would like to say that we serve our customers, we provide full service to our clients. So they do not suffer from any scarcity of steel. Basically now in March and April, inventories are very similar to what we had in February and March. And at the moment, we believe that these inventories will resume normal levels by June or July.

And maybe, Scardoelli, if you can something about the new normal of margins? I think, this is very much related to my previous comments, when I said that the fundamentals of steel demand remains very robust in Brazil in all segments. And that's what we see in the next coming quarters. So, I think, I already answered this question before. But Scardoelli, if you want to add anything else, please feel free?

### **A - Harley Scardoelli** {BIO 7283603 <GO>}

Now maybe that has made you think about our business model in Brazil has been very resilient in the lower part of the cycle. Even in the most complicated moments, our model proved to be very resilient, and we were able to be above average when compared to the global industry. And obviously, it's also a very good model if you consider that the markets are very positive, very bullish, which is the case right now. I think you already mentioned what is happening in China, which is something very structural. And we noticed a trend going forward for the next quarters or even years. Therefore, our business model responds quite well to this momentum.

In terms of being the new normal or not, it's something that will depend on other circumstances or assumptions. But certainly in a situation of a more prolonged cycle of commodity, it's more positive. So the trend is that our margin -- margins will still be kept at very good levels.

### **A - Gustavo Werneck** {BIO 20318216 <GO>}

Scardoelli, when you say that we learn to deliver results even in dire scenarios, I would like to mention our efforts in reducing SG&A. I mentioned \$300 million of annual reduction and also the fact that we successfully adapted the ZBB methodology, zero-based budget methodology. And in more positive scenarios, we were able to keep the company very lean, very simple and agile. We are always able to capture the benefits from the transformation that we started years ago. Rodrigo, back to you.

### **A - Rodrigo Maia** {BIO 19840176 <GO>}

Thank you. Our next question comes from an individual investor. And I take this time to say that Gerdau has 200,000 individual shareholders. Thank you. (inaudible) has the next question.

### **Q - Unidentified Participant**

(inaudible) question is in terms of the company's governance, has Gerdau intend to migrate to Novo Mercado? And what about the payout? Do you intend to increase the dividend payout? Thank you.

**A - Gustavo Werneck** {BIO 20318216 <GO>}

We can answer that, Scardoelli.

**A - Harley Scardoelli** {BIO 7283603 <GO>}

In terms of dividend payout, I think I already answered that earlier on. Dividends are increasing significantly because of our payout of 30% of net income.

In terms of governance and Novo Mercado, one thing that is important to mention is that today, we are at Level 1 at BOVESPA, which is a very good governance level. And one of the main points in terms of Novo Mercado, we are already complying with that. We are 100% tag along. We -- many of our governance practices are well advanced. In terms of Novo Mercado, I mean a company with a very defined control as is our case is something that at this time, it's not something that we look forward to because we already have several practices that put us in a very advanced and good governance level.

**A - Rodrigo Maia** {BIO 19840176 <GO>}

Thank you. Our next question is from Rafael Barcellos from Santander.

**Q - Rafael Barcellos** {BIO 20593721 <GO>}

Could you comment on the utilization capacity in Brazil and also talk about the strategy behind the restart up of the Araucaria unit in Parana? Thank you.

**A - Gustavo Werneck** {BIO 20318216 <GO>}

Well, I'll answer that question. Rafael, thank you for the question. Utilization capacity in Brazil is not close to limit. We do have available capacity and the restart of Araucaria is a good example of that. Our utilization is around 75% in Brazil. The highest utilization today of Gerdau assets in the U.S., as I said, or in North America, is close to 91%.

The restart of Araucaria aims at increasing the availability of crude steel to our operations. In our Brazil operation, we have great flexibility between our plants, not only in terms of steel production and rolling mill, but also in regards to raw material. Scrap is something that I often mention. Scrap can be mixed. I mean, we can mix the use of scrap through our buyer reducer. We have pig iron also in the state of Minas Gerais.

So, we have great flexibility in Brazil from raw material to the end to the final product. So the idea with Araucaria is to increase the steel production that will be used in our several rolling mills from (inaudible) into the (inaudible). In terms of production planning and logistics, aiming at better serving our customers and reducing our costs, the restart of Araucaria aims at increasing the delivery of crude steel to be used in our rolling mills in all of the corners of the country.

**A - Rodrigo Maia** {BIO 19840176 <GO>}

Our next question comes from Marcio Farid from J.P. Morgan.



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**Q - Marcio Farid** {BIO 21017394 <GO>}

Thank you for this opportunity/. Could you comment on the levels of premium in Brazil versus the same parity abroad? What is the balance level considering supply and demand in the steel industry?

**A - Gustavo Werneck** {BIO 20318216 <GO>}

Premiums are still low, due to the continuous increase in the prices of international products and effects. In general mentioning longs and flats, premium is around 10%. So when you look at historical figures, it's still low. And this balance between supply and demand in Brazil with the end -- with the advent of new capacity and the restart of production is already in place. As I mentioned before, what is happening now is the recovery of inventories. Well, it's happening slower than expected, but we believe that by May, June or July, the entire chain will be able to recover their inventories, but demand and the inflow orders will remain strong.

**A - Rodrigo Maia** {BIO 19840176 <GO>}

Thank you, Gustavo. Our next question comes from Geraldo Mellone Junior from Bresser Asset Management.

**Q - Geraldo Mellone Junior** {BIO 19799454 <GO>}

What is the amount of recurring CapEx for Gerdau considering 2022 and looking forward?

**A - Gustavo Werneck** {BIO 20318216 <GO>}

Can you answer that, Scardoelli, about CapEx?

**A - Harley Scardoelli** {BIO 7283603 <GO>}

About CapEx, this is something recurring. Right now we are investing more intensively in our Ouro Branco mill, because that's an integrated operation that follows a different investment cycle when compared to the investment cycle of our other mills that are scrap-based. They have a more continues and constant CapEx cycle, as we cannot use as recurring CapEx. The low levels we experienced in past years where we have to have a tighter operation, we cannot afford to perpetuate a stronger CapEx spend, we are investing more in our integrated mill of Ouro Branco.

In terms of the long-term to -- to draw a long-term projection, I would say that will be slightly below depreciation, slightly below or equal to depreciation. Obviously, this is not something that will happen every year, one year and also the next, but you have to look at longer period of time. But in terms of our projection, I would say that it should be something close to depreciation. But what will really happen in the next few years is that we will continue to inform the market about our intention to spend. We know that this is a very dynamic market, therefore we decided to inform the market every year in the beginning of the year how much we intend to spend in terms of CapEx to give a clear view to analysts.

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**A - Rodrigo Maia** {BIO 19840176 <GO>}

Thank you. Our next question comes from Marcelo Audi from Cardinal Partners.

**Q - Marcelo Audi** {BIO 1550731 <GO>}

Capital allocation, we talked a lot about that today. He would like to know how can we ensure that right now capital allocation will produce a return on the investments that are being conducted? And whether there is current cash and consideration, considering cash flow generation, whether you think that ROE should come down because of access cash? What should be expected going forward in view of this new scenario of Gerdau's cash generation especially considering the discipline of capital investment?

**A - Gustavo Werneck** {BIO 20318216 <GO>}

Can you answer that, Scardoelli?

**A - Harley Scardoelli** {BIO 7283603 <GO>}

Yes, certainly. Marcelo, in terms of our discipline in capital allocation, it's something truly important to the company. You know that we experienced a very strong period of growth, and then a period of crisis in the industry, especially when China decided to export high volumes of steel. And we as a company, we had to revisit our portfolio. We had some divestments which was something we did for several years, and that brought us back to a level of return on employed capital, which is the level we intend to keep going forward.

We are -- so Gustavo and the other executives of the team and the Board as well are very, very rigorous whenever they consider CapEx and investments. So we want to ensure adequate returns to the capital invested. Well, in regards to cash generation, today with the level of interest rates, we can certainly work with a lower level of cash when compared to our historical levels. We had something like \$2 million of cash in the company. So today we were closer to \$1 billion. We could even work with a bit less if that is the case, because today we already have a credit line that is -- sure, I mean, this is something that has a line of credit where we can withdraw at any given time. So that line of credit is available in 24 hours. So we are very comfortable to work with a lower level of cash from now on.

**A - Rodrigo Maia** {BIO 19840176 <GO>}

Our next and before last question is from Eduardo Cavalheiro from Rio Verde Investimentos.

**Q - Eduardo Cavalheiro** {BIO 15879680 <GO>}

In terms of the cash of Metalurgica Gerdau S.A., which is very robust, do you already have a destination to that cash?

**A - Gustavo Werneck** {BIO 20318216 <GO>}

Scardoelli, up to you.

**A - Harley Scardoelli** {BIO 7283603 <GO>}

This cash is invested and very safe instruments with good liquidity. That's why this is not separate or destined to anything specific. It's invested and it has a lot of liquidity, but we do not know exactly what we will do with it. But Metalurgica will stick to its core business which is to be a holding of Gerdau S.A. So our intent is to keep that cash and liquid instruments.

**A - Rodrigo Maia** {BIO 19840176 <GO>}

Our next question Marcus [ph] from GTI.

**Q - Unidentified Participant**

In relation to your financial cycle or cash conversion cycle, do you think that this can be consider something recurring going forward? And this is our last question from the chat. And I would like to thank you all.

**A - Gustavo Werneck** {BIO 20318216 <GO>}

Well, I'll leave that last one with you as well.

**A - Harley Scardoelli** {BIO 7283603 <GO>}

So I understand that we are talking about our working capital financial cycle. So at the end of 2020, the level was probably below normal. Today, the cash conversion cycle is 57 days. So I would say between 55 and 60 days is a very adequate level of cash conversion cycle in terms of working capital. We had to consume cash to adapt to working capital in this first quarter because of the moves in the market, and that's the trend going forward as well. Possibly in the sector, we will still see some consumption of cash for working capital because level of activity remains very strong as Gustavo mentioned during his presentation.

**A - Rodrigo Maia** {BIO 19840176 <GO>}

Thank you, Scardoelli. We now conclude the Q&A session. And I would like to reiterate that this was our first video call. So if there was any connection issue, you can get in touch with our IR department to clarify your possible issues. Now, I would like to turn the floor back to Gustavo and Scardoelli for their final remarks.

**A - Gustavo Werneck** {BIO 20318216 <GO>}

Well, Scardoelli, I will then conclude this conference call. And I would like to thank you all for joining us today. It's always a great pleasure to talk to you. We remain available not only myself, but Scardoelli and our entire IR team. So please talk to us if you have any additional question. And right now I take this opportunity to invite you to our next conference call related to the second quarter of 2021 to take place on August 4. So, thank you very much. Please take care and take care of your health. I wish you all a very good end of week.

**A - Rodrigo Maia** {BIO 19840176 <GO>}

Thank you, Gustavo. Gerdau's conference call is now concluded. Thank you all very much for joining us. We had more than 200 participants with us today. Thank you and have a very good afternoon.

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