

Q4 2014 Earnings Call

Company Participants

- André Bier Gerdau Johannpeter
- André Pires de Oliveira Dias

Other Participants

- Alan Glezer
- Alexander Hacking
- André Pinheiro
- Carlos F. De Alba
- Leonardo Correa
- Marcelo Aguiar
- Milton Sullyvan
- Renan Criscio
- Roy Yackulic
- Thiago Lofiego

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon, and welcome to Gerdau's Conference Call to discuss the Results for the Fourth Quarter of 2014. All participants will be in listen-only mode during the company's presentation. Later on, we will hold a Q&A session.

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

Today with us are, Mr. André Gerdau Johannpeter, Director, President and CEO; and Mr. André Pires, VP and IR Officer.

With no further ado, I would like to turn the floor to Mr. André Gerdau Johannpeter. Please, Mr. André.

André Bier Gerdau Johannpeter

Good afternoon, everyone. Welcome to our conference call for Gerdau's results. We will start with an overview of the world landscape for the steel industry then we'll talk about Gerdau's performance in the 12 months of 2014 and in the fourth quarter of the year. After that, we'll give you some details on investments for 2015.

It's important to stress that we'll analyze the performance of consolidated results of 2014 and 4Q 2014 vis-à-vis the same period of the prior year. After that, André Pires will present Gerdau's financial performance and then we will be available for your questions.

For those of you that are following us on the Internet, on the slide two, we're going to talk about steel in 2014. We have faced significant challenges in the world, an overcapacity of around 690 million tonnes of steel and a weaker steel demand in markets like Brazil and other countries in Latin America, causing a high volatility in the results.

In Brazil, there was low economic growth in 2014, which has impacted steel consuming markets, such as civil construction, manufacturing and the auto sector. According to the Brazilian Steel Institute, the apparent consumption of steel in the country in 2014 was the lowest since 2009, amounting 24.6 million tonnes, 6.8% down.

In Latin America, except for Brazil, the steel industry was affected not only by slowdown in the economy, but also by the increase in steel imports according to the Latin America Steel Association, Alacero. Latin America is the second region with the largest volume of rolled steel import from China, second only to South Korea.

In the American market, Gerdau's steel demand was more or higher vis-à-vis 2013 with highlights the manufacturing and non-residential construction sector. But we remain concerned about the high imported steel inflow. Just to give you an idea, imports of long steel in the U.S. went from 17% of total consumption in 2013 to around 20% in 2014.

And the specialty sector that we highlight the continuous growth of the auto market in the U.S. Also, there has been a gradual development of European and India markets. On the other hand, Brazilian auto industry is still negatively impacted long steel sales or rather specialty steel sales in the domestic market.

Now on slide three, let's talk about the main figures of Gerdau for 2014, starting on shipments. We have consolidated 17.9 million tonnes of steel in 2014, 3.5% lower vis-à-vis 2013, mainly due to weaker steel demand in Brazil and other Latin American countries. Shipments in the fourth quarter amounted 4.4 million tonnes, 3.4% less than 4Q 2013.

Net sales have reached R\$42.5 billion, 6.7% higher than the prior year, especially because the expansion of revenue in the American market and the positive foreign exchange effect and the currency conversion of revenues from foreign operations. In the fourth quarter, net sales amounted R\$10.8 billion, 5.1% higher vis-à-vis the same period of 2013.

Earnings before interest, taxes, depreciation and amortization, also known as EBITDA, was R\$5.1 billion in 2014, 7.1% higher vis-à-vis the prior year. This performance was impacted by

earnings from the sale of our interests in the American Gallatin Steel totaling R\$637 million and by the impairment of assets in Latin America in the amount of R\$339 million. Not factoring both operations, adjusted EBITDA was R\$4.8 billion, stable vis-à-vis 2013 and despite the challenging scenario of the world steel market.

In the fourth quarter EBITDA was R\$1.5 billion, net of nonrecurring items of R\$1.2 billion, a drop of 9.6%. Net income was R\$1.5 billion, 12.2% lower vis-à-vis 2013. And in the last quarter of 2014, net income totaled R\$393 million, a drop of 20% when compared to the same period.

On page four we'll talk about investments. In 2014 they totaled R\$2.3 billion. Those were investments in fixed assets. The amount was 21% lower than we initially planned for 2014, in line with the company's position which we talked about along the year, to be judicious in investment approvals. It's important to highlight that investments made in 2014 were towards projects already approved, they were ongoing projects in addition to planned maintenance, both in Brazil as well as abroad.

For 2015, Gerdau plans to invest R\$1.9 billion in fixed assets, and that mirrors the global landscape of the steel market marked by the installed overcapacity. Also, we will continue assessing the economic scenario and its impact on operations in order to adjust, if needed, total investments to market moves.

Thank you. And now I'll turn the floor to André Pires.

André Pires de Oliveira Dias

Thank you, André. Good afternoon, everyone. I will start on slide number six for those of you that are following us on the webcast, and I'll talk about the results and annual consolidated performance, and then I'll talk about each business operation and I'll close the presentation talking about capital structure.

In the consolidated, the adjusted EBITDA and the adjusted EBITDA margins for 2014 were rather stable regardless lower number of shipments. That stability was mainly due to the positive effect of the exchange rate variation in the period and foreign operations and exports from Brazil. Here it's important to highlight the rebound of North America BO which has contributed to a consistent EBITDA offsetting the lower EBITDA in Brazil BO.

Now turning to slide number seven and talking about the fourth quarter of 2014, and starting by Brazil, we see that the uncertainty about the economic scenario is causing a lower demand, which is impacting our business. In 4Q 2014 shipments dropped 3% vis-à-vis 4Q 2013 and the internal market had a drop of 4% especially in civil construction and manufacturing. In comparison to 3Q 2014, sales volume grew 5% with increased exports 31% higher in the period because of the improvement in the international market of semi-finished products and also a quicker devaluation of real.

Analyzing the EBITDA for the fourth quarter of 2014, the absolute amount was down 13% vis-à-vis 4Q 2013. Let me remind you that in the last quarter of 2013 there were earnings

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from sale of real estate amounting R\$98.6 million. Net of this effect, EBITDA and EBITDA margin were stable in the comparison for both periods. Vis-à-vis 3Q 2014, EBITDA was up 26% in 4Q 2014 and the margin increased from 16.5% to 20.3%, thanks to greater fixed cost dilution with export increase and to lower cost of iron ore in Ouro Branco mill.

In the U.S., the economic scenario continues to be positive, but the growing pressure from imported products added to the seasonality of the period resulted in shipments down by 5% in the 4Q 2014 vis-à-vis 4Q 2013 comparison and by 15% vis-à-vis 3Q 2014. 4Q 2014 EBITDA grew 43% vis-à-vis 4Q 2013, going from R\$139 million to R\$199 million, mainly thanks to the metal spread gain in addition to the exchange rate variation in the period. So the EBITDA margin went from 4.5% in 4Q 2013 to 5.7% in 4Q 2014.

Vis-à-vis 3Q 2014, EBITDA and EBITDA margin dropped due to lower volumes sold, and that was because of seasonality of our business. It is important to stress that the results of this operation in 4Q 2014 did not take into account the equity in earnings from Gallatin Steel Company once the sale of that was done in 2014.

In Latin America, 4Q 2014 shipments were down 7% vis-à-vis 4Q 2013 due to increased imports inflow, especially from China and Turkey, and the slower economic growth in the region. 4Q 2014 EBITDA was lower vis-à-vis 4Q 2013 due to lower shipment volume and higher operating expenses in the period. When compared to 3Q 2014, EBITDA was stable.

In the specialty steel BO shipments in 4Q 2014 were down 5%, both vis-à-vis 4Q 2013 as well as 3Q 2014, and that was due to lower demand in Brazil. Consolidated EBITDA increase for specialty steel in 4Q 2014 vis-à-vis 4Q 2013 was thanks to higher net sales per tonne, basically driven by specialty steel mills from the U.S. Therefore, EBITDA margin was up from 10% in 4Q 2013 to 12% in 4Q 2014.

For iron ore, comparing 4Q 2014 to 4Q 2013, shipments grew 5% thanks to higher volumes sent to Ouro Branco mill vis-à-vis 3Q 2014. Even facing a challenging scenario, sales increased with already scheduled shipments for the period. A drop in the EBITDA and in the EBITDA margin for 2014 vis-à-vis 4Q 2013 and also 3Q 2014 was due to lower international prices for iron ore.

Now, turning to slide number eight and talking about the consolidated results. In the quarter, the adjusted EBITDA amounted R\$1.2 billion, 10% lower when compared to the same period of the prior year. The top chart shows the reduction was due to lower volumes sold, higher costs, partially offset by a higher net sales per tonne. Therefore, EBITDA margin went from 13.3% in 4Q 2013 to 11.4% in 4Q 2014.

The bottom bridge chart, we see the consolidated net income in 4Q 2014. It was lower than 4Q 2013 due to reduced operating results and higher negative financial result partially offset by the net effect of nonrecurring events.

Now talking about dividends, considering 4Q 2014 results, R\$28.4 million in dividends will be paid to shareholders of Metalúrgica Gerdau, R\$0.07 per share, and R\$119 million to

shareholders of Gerdau SA, also R\$0.07 per share. These will be paid on March 26, recorded at close of business on March 16.

Now on slide nine let's talk about indebtedness and liquidity of the company. Gross debt at December 31, 2014 was R\$19.2 billion, higher than in September of 2014 due to the exchange rate variation. Net of this effect, gross debt would have dropped around R\$412 million. When compared to December 2013, gross debt increased, especially due to exchange rate variations.

The average of debt cost was 6.5% a year with an average amortization term of 7.1 years. Cash increase of R\$1.1 billion from September to December 2014 was mainly caused by proceeds received from Gallatin's sale. That increase more than offset the growth of the net debt in the period reducing the net debt-EBITDA ratio from 2.7 times in September to 2.4 times in December of 2014.

Now turning to slide number 10, I will talk specifically about working capital. And if you look at that chart you'll see that the absolute amount is around R\$10 billion in 2014 and a stable cash conversion cycle of around 85 days. Comparing December 2014 to September 2014, working capital decreased R\$100 million. It's important to stress that the exchange rate variation is accounted for in this drop. And not factoring in this variation, the cash effect of the working capital reduction was R\$469 million.

Now I'll turn the floor back to André for his final remarks.

André Bier Gerdau Johannpeter

Thank you, Pires. To conclude I would like to stress that 2014 was a very challenging year for Gerdau and the steel industry, mainly due to the installed overcapacity worldwide and also for the lower demand in relevant markets, especially Brazil and other Latin American countries.

Just to give you an idea, the use of installed capacity of the steel industry in the world is decreasing on a yearly basis. It has reached 91%, its peak, in 2008, and in the following year the average was 75% to 80%. And in January of this year it has reached 72% of use in the industry. These are data from the World Steel Association.

On the other hand, we were able to minimize the effect of this scenario in Gerdau's operating performance. We have improved the performance of our operations under the difficult landscape. We have divested from non-strategic assets, for instance, the interest in Gallatin Steel, and keeping selective when investing in fixed assets. Regardless the lower net income in 2014, our management efforts can be seen by our adjusted EBITDA levels stable vis-à-vis the prior period.

About the sector perspective, we expect the world steel industry will keep on facing slow consumption growth and installed overcapacity. In other countries where we operate, we believe the developed markets offer positive scenarios. The economy in the U.S. should grow in 2015, boosting steel consumption in the country. The expansion of non-residential

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segment should continue given increasing private investments. In the U.S. infrastructure investments should be moderate, in line with the modest growth of financing available in the public sector. But the continuous increase of imported steel inflow will keep on pressing margins and results of companies in the industry.

Brazil's perspective for 2015 is a difficult (19:22) one, taking into the consideration the potential impact of the economic downturn to consumption levels. Added to the that, the country's systemic (19:31) problems: elevated tax burden, cumulative taxes, electric power cost, and also an appreciated exchange rate. All of those have been impacting the main productive sectors. In addition, other economies in Latin America should have different level growth in 2015 impacting also the apparent consumption of steel in the region.

About specialty steels, specifically here, perspectives are of modest growth in the auto industry in Brazil impacting the demand for specialty steels. On the other hand, North America should continue the development of the auto industry, expanding manufacturing of light and heavy vehicles, therefore, increasing the demand of specialty steels in the region. But the oil price drop is already impacting the oil and gas industry, another great consumer for specialty steels.

In the European market, the slow and gradual rebound of the economy should allow for boost of the production of light and heavy vehicles in 2015. And in India, there should be an increased production of light and heavy vehicles which could also expand the consumption of specialty steels in the country.

About the iron ore market, the oversupply of 2014 has impacted the sales of the raw material and that should remain the case in 2015. Under that scenario, we should follow our strategy of focusing on the iron ore production to supply Ouro Branco mill, increasing its competitiveness. We also consider the chance of continually experiencing margin pressure in the international market and the possibility of steel imports expansion in almost all markets we operate in, an important point of attention to the sector, no doubt.

Also geopolitical conflicts are affecting the economic growth of some regions in the world, impacting steel consumption and sales. Facing this landscape, we'll keep on seeking to adjust our operations to the world steel markets' movements sustaining the operation efficient work and also aiming to ensure business stability.

We now conclude our presentation and are available to answer your questions. Thank you very much.

Q&A

Operator

Ladies and gentlemen, we will now start the Q&A session. Our first question comes from Milton Sullyvan, Brasil Plural.

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Q - Milton Sullyvan {BIO 19085202 <GO>}

Good afternoon. Thank you. I have two questions, first about Brazil operations. Can you tell us what we could expect in terms of costs ahead? Specifically, and strategically speaking, what kind of production we can see from Açominas and what kind of impact we should expect? And second question is still on costs; can you tell us a little bit about the scrap price, what kind of price we should expect for scrap in Brazil, considering you already have some discounts in specialty steels? And is there are any pressure because of prices abroad? Thank you.

A - André Pires de Oliveira Dias

Hello, Milton. This is André Pires. Thank you for your questions. About - let me see if I well understood your first question: if there are more opportunities to send our production to Ouro Branco, to Açominas? Yes, this has been our strategy and we have been successful in it. I believe this strategy has proven to be efficient when we look at the EBITDA margin of Brazil operation in 4Q 2014. So the scenario is still favorable. Iron ore has not increased from back there to today, and so I think we could manufacture good (23:37) steel using our Ouro Branco mill.

About the scrap price, it has been stable. It is not as much related to the international price, but obviously, there is no high pressure right now and the price in the last month has been rather stable.

Q - Milton Sullyvan {BIO 19085202 <GO>}

Thank you.

Operator

Our next question comes from Carlos De Alba, Morgan Stanley.

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

Yeah. Good morning. Thank you very much. First question has to do with working capital. In your year-on-year comparing December 2014 versus December 2013, the cash conversion cycle increased about three days and I wonder if you can comment, how do you see the conversion cycle in 2015? And how much money do you think you can generate from either controlling or hopefully reducing the cycle?

And the second question, also on iron ore. How much volumes of iron ore do you expect to produce in 2015? And if you can give us a sense of the split between internal use or consumed iron ore in Ouro Branco and how much would you be able to export if you have any commitments to export? That will be very useful. And just finally, I guess under the current scenario of iron ore prices, the expansion on the iron ore business is off the table, right? Just to confirm that. Thank you.

A - André Pires de Oliveira Dias

Well. Let me translate Carlos' question. He's asking about working capital and the cash conversion cycle because there was an increase of three days in the conversion cycle in 2014. And what is our expectation for 2015? How much we could optimize in terms of working capital for 2015? The following question is about iron ore and I'll turn to André.

Now let's talk about working capital. Really we have started 2014 with a better expectation in terms of production volume or shipment volume for Gerdau vis-à-vis what happened in the year. There was a drop of 4% in the shipment volume in the year. Therefore the adjustment in the working capital has not been fast enough as we would like it to be in 2014. And that's why the conversion cycle was three days higher than the closing of 2014.

For 2015 we do not have a forecast. But obviously we are working with a very realistic expectation in terms of the deliveries or the shipments for consolidated ones. We are working in the long-term objective of bringing the cash conversion cycle to lower than 80 days getting closer to 75 days. This is our long-term goal. We don't have a short-term goal for this yet.

But if we analyze the way we are working we believe that in the long-term we will be able to bring down the cash conversion cycle to below 80 days. Now, let me turn to André and he will talk about the iron ore.

A - André Bier Gerdau Johannpeter

Okay. The question was about the iron ore and about production, how much is going to go to Ouro Branco export? And the trend of expansion, if that is going to continue or if it is under analysis? We are not going to disclose information about volumes right now, but 80% to 90% of what is going to be manufactured is going to be used by Ouro Branco mill. Our focus is iron ore to be used in our own mill. We have might have some shipments if that is feasible, but right now we are concentrated in taking our production to Ouro Branco and we do not intend to grow exports.

About the expansion project, we are reassessing it as we said. We don't have any further information to provide you right now. Once again, our focus is to bring production of iron ore to supply our mill, and we do not have any commitment. You have asked if we have commitments in terms of railways, ports. No, we don't have anything. That gives us flexibility to decide what we wish to do ahead, when we wish to do it if the scenario changes. But if nothing happens, we will keep on supplying to Ouro Branco. That helps us very much in the competitiveness of that mill.

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

Thank you.

Operator

Our next question comes from Leonardo Correa, BTG Pactual.

Q - Leonardo Correa {BIO 16441222 <GO>}

Good afternoon, everyone, and thank you. My first question is about the streamlining of assets. We have seen efforts from you, from Brazil, closing capacities of higher costs, of the less competitive ones, and they have been providing good results. We see cost controls in Brazil. But if I think globally, considering the impairment that you've done in Latin America, what can we expect? Do you still have idle capacity abroad? Anything relevant? I would just like to understand if there is anything similar to what have you done in Brazil, if you are studying, if you are considering anything, especially Latin America and the United States. That was my first question.

And my second question is still about the U.S. Of course, there was a negative impact on the volumes and quarter-on-quarter it was seasonal, but it might have been some cost impact. It might have been, but I just would like to understand, we are crunching some numbers here and it looks like maybe you have some nonrecurring costs in North America. I just want to make sure if - I just want to understand if that makes sense. Did you have anything nonrecurring in costs in the U.S.? These are my two questions. Thank you.

A - André Pires de Oliveira Dias

Hello, Leonardo. This is André Pires. About the streamlining of assets, as you asked, really in the second half of last year we tried to optimize our assets in Brazil, focusing on the less competitive operations in terms of cost and efficiency. And this is still our goal, not only in Brazil, but also when we look at our global footprint. So we are still focusing on that and we do not have any specific plan, anything to disclose, but we do have to take that into consideration. Depending on the scenario, we might take other measures in that sense, not only in Brazil, but also in other areas.

In North America, there is nothing nonrecurring in the fourth quarter. What happened was the lower volume. Therefore, there was a lower dilution of fixed costs. That's why you end up having higher costs. So also important to say here is that when we compare to the fourth quarter of 2014 with the fourth quarter of 2013 we still had equity from Gallatin. We don't have that anymore. That was something relevant. So this might be an explanation of something that may have drawn your attention.

Q - Leonardo Correa {BIO 16441222 <GO>}

Okay. Thank you very much.

Operator

Our next question comes from Roy Yackulic from Merrill Lynch.

Q - Roy Yackulic {BIO 4201939 <GO>}

Thank you. In the CapEx budget for next year, your estimate of R\$1.9 billion, how sensitive is that to FX? How much of it is U.S. dollar denominated? And does it include any iron ore CapEx? And then my second question is regarding, I guess, the construction industry in Brazil. There was an article out today that 2014 and 2015 are supposed to be the worst years for the construction industry since 1992. And I think construction declined about 6%

in 2014. What are the expectations for 2015? And then in addition to auto sales, they're supposed to decline 10%. So are we looking for a pretty bad domestic year in Brazil?

A - André Pires de Oliveira Dias

This is André Pires. Thank you for your question and I'll translate it. The first question is about the CapEx estimate for 2015 of R\$1.9 billion and the question is how sensitive that CapEx is to FX, and if we are here considering anything for mining within that figure.

André will talk about the construction sector in Brazil and also the auto sector, which was the second question. But let's start by CapEx. Of course, there is sensitiveness to FX, but there are a lot of investments made here in Brazil, investments in which we are at our final stage. I'll give you an example; you'll know it very well. It is the construction of our heavy plate rolling plant. We are in the assembly phase already. That investment is totally made in reais, equipment is already bought.

We have investments done in Latin American countries that end up being impacted by the same factors that real is impacted because these currencies are also depreciating. So there is sensitiveness, but it's not as high. That's why we were talking about figures in reais because with the exchange rate and volatility, it's difficult to have a dollar estimate of that figure in a scenario in which part of the CapEx and the (34:12) dollar are done in different currencies and the real has appreciated vis-à-vis the dollar. About mining CapEx, if there is anything for mining in the figure, very little, I would say that for mining, it's only maintenance. We don't have anything for mining expansion within that figure.

Now let me turn to André. The other question is about the construction market and the auto market as well. You talked about this year and next year being difficult years in terms of growth.

A - André Bier Gerdau Johannpeter

Yes, we see a difficult landscape, we see drops in sales volumes (34:58). That happened already in 2014 and it's very difficult to forecast if this is going to stay like this or if we are going to see any rebound. But this is a difficult year for construction, especially civil construction. We see a little bit of infrastructure that has worked. That has gone forward last year. But now the construction companies and with all investigations for the Car Wash operations in Petrobras itself is a major consumer in the construction sector. So all of that is causing an impact. It is a cautious scenario and difficult to forecast.

In the auto sector we've seen sales drop that we saw in January as well, but in the auto sector we have a possibility of exporting because with the exchange rate close to R\$3 per \$1, there's still a chance (35:52) we could start exporting. There is this possibility. But the whole auto sector is having that possibility of exporting as well due to the FX effect. So differently from construction in the auto sector there is this possibility. Gerdau (36:07), with steel and also auto parts that could be exported. This is a possible scenario for 2015-2016 because we believe dollar is going to grow stronger.

Operator

Our next question is from André Pinheiro, Itaú BBA.

Q - André Pinheiro

Good afternoon, everyone. I have two questions. First, considering the depreciation of the exchange rate and we have seen it stronger now in the beginning of the year, what could we expect for the sales mix for the first quarter of Gerdau? Should we see more exports in the mix? And how do you expect that to progress from now on? And the second question is about the metal spread in the U.S. How do you see that in the beginning of the year? And what do you expect to see the metal spreads progressing from now on? We see more products, imported products coming in and the steel price going down worldwide. And what's that going - how's that going to impact the metal price?

A - André Bier Gerdau Johannpeter

Good afternoon, André. About the FX and the export mix, now, from the third quarter to the fourth quarter there was already a growth in exports. And this should be a trend for this first quarter of 2015 and for the subsequent ones as well. And despite of the drop of price worldwide that depreciation is increasing. That is deeply related in the world, so we become more competitive. So I would say the trend is to increase exports. It's difficult to mention figures, but we have increased that already from the third quarter to the fourth quarter, from the fourth quarter to the first quarter. Slabs and billets as we have seen. Also some exports of rolled products are there already.

A - André Pires de Oliveira Dias

About the metals spread, here is André Pires. It is still there, even with recent price reductions in the U.S. above \$420 and \$430 (38:36) per short tonne. Of course that when there is a price drop the first effect is a margin reduction then later on it tends to normalize due to the drop in the scrap. So the average, I believe, for the metal spread should be stable in 2015 vis-à-vis 2014. We do not believe that the import pressure in the U.S. is going to go down. We believe more imported products are going to go in. The consensus of the several agencies that estimate around non-residential construction, they say that there should be a growth of 7.7% and 8.2% in 2016, so the demand should be consistent and imported products should keep on going in. And there is another driver here that helps this high import, which is a dollar that is strengthening. So we believe the metal spread should be consistent to what it was in 2014, around \$420 for a short tonne. Thank you.

Operator

Our next question is from Christina Roneck (40:14), HSBC.

Hi. Thank you. Can you remind me if you hedged your U.S. dollar bonds into real? And then a follow up that I have calculated you have about \$5 billion of bonds and I think you record that on your balance sheet at R\$12 billion. Is that fair?

A - André Pires de Oliveira Dias

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The question was about our bonds, our dollars, if they are hedged to real. And if I'm not mistaken the second question is about what we have issued at R\$5 billion in bonds and our balance sheet says R\$12 billion. Let me clarify these figures. The first answer to your question is that, no, we do not have an effective hedge vis-à-vis our dollar debt to reais. What we use, the net investment hedge methodology which is allowed by the IFRS, by using this methodology since we have dollar investments due to our operations in the U.S., we assign those bonds issues to finance investments in the U.S.

By doing that, the exchange rate because (41:52) do not impact our P&L, our results, and they go straight to our equity. So that's why you do not see a major FX variation in our income statement because that is transferred to our equity. So what you see in terms of exchange variations are some debts that we have in foreign currencies maybe a dollar operation or some payable accounts that are in dollars, and they are subject to FX variance but they are small. About the debt of our bond, they are in dollars they are around \$4 billion. Basically, we have \$1 billion dollars for our American operations and \$4 billion to the Brazilian operations. So those would total the \$5 billion that you mentioned. That is equivalent to R\$13 billion in our balance sheet.

Q - Operator

Thank you.

Next question is from Marcelo Aguiar, Goldman Sachs.

Q - Marcelo Aguiar {BIO 3721791 <GO>}

Thank you. Good afternoon, everyone. My first question is about your exposure to heavy construction sector. Can you remind me what is the mix if we analyze long steel sales? What was your retail exposure? What is your exposure for residential industry, heavy construction so that we can have an idea of the fluctuations of your domestic shipments for 2015? And my second question is, Brazilian companies will have cost pressure this year due to inflation, energy costs, and so on. I would like to understand from the energy and the power side of view, what is your exposure considering all these changes in terms of taxes and tariffs that the government is going to launch in the next year. So there's going to be an increase of costs with electric power and analyzing the exchange rate at R\$3, would you have an opportunity to re-work on prices on Brazil?

A - André Pires de Oliveira Dias

Hello, Marcelo, this is André Pires. Now, let me remind you of our mix. What is a small consumption that represents basically 40% of long steel. What goes to production, 40% is small. And the other 60% are distributed to residential, commercial and infrastructure. When you talk about heavy construction, I think you're talking about infrastructure. So that represents 20% of 60%, so 12%. In the last years, it has represented even more with the infrastructure awards pre-World Cup and also with the concessions that we had in the last year. That infrastructure is at around 12% usually, but now it's at 15%. Of course, depending on what happens related to infrastructure and construction that might have an impact. That a small consumption is more stable, it tends to fluctuate more even with unfavorable situations. So that is just to repeat, construction, 60%. Of those 60%, 40% are

small, 20% residential, 20% commercial and 20% infrastructure. And André will talk about costs.

A - André Bier Gerdau Johannpeter

Good afternoon, Marcelo. About costs, you mentioned inflation, electric energy and if the exchange rate might impact prices. So first about inflation, we are strongly working and we have started last year and we still are to reveal all contracts of material supply, services, wages, always aiming to be lower than inflation, restructuring and trying to lower costs under that scenario, which is a cost and margin pressure scenario. So we have been doing a consistent work of reviewing contracts, services and so on. So inflation is there. It is going up, we've seen the numbers, but we are trying to go the other way around, not allowing inflation to impact our figures.

On the energy side, let me remind you that it had 5% impact in our final price. So it is important. We do work on it, but that's not the main cost. And then we have several contracts by spot price, so we have contract negotiation. We have alternatives work on generation of energy in Goiás and Rio Grande do Sul. We have Ouro Branco route where 70% has (47:58) self-energy generation, and we have mills all over the country. So it is very difficult to provide you a number in terms of the impact depending on the region. But I could tell you that we are well-positioned in terms of geographic areas, the integrated routes to Rio Branco and self-generation of energy. We have good strategy to face that difficult scenario of energy. About prices, once again we will not mention anything about prices. That is a market matter. Okay?

Q - Marcelo Aguiar {BIO 3721791 <GO>}

Thank you.

Operator

Our next question is from Alex Hacking, Citigroup.

Q - Alexander Hacking {BIO 6599419 <GO>}

Hi. Good afternoon. Thank you for the question. My question is on your balance sheet. Obviously, we know that weaker real is going to increase your gross debt, all things being equal. How do you see the net debt-to-EBITDA ratio evolving in 2015? I know that you've always looked at 2.5 times as sort of a ceiling there. Is that something that you think is realistic? And then the second part of the question will be are there any other asset sales that you're considering or are possible similar to what we saw with Gallatin Steel this year? Thank you.

A - André Pires de Oliveira Dias

This is André Pires. Alex's question is about the balance sheet and the impact of the exchange depreciation and the increase of our debt, and how would - how we would have the net debt-EBITDA ratio? And the second question has to do with asset sales, such as we have done with Gallatin last year. So about the first question, obviously, in a depreciation environment, and real depreciation as we have a high percentage of debt in

dollars, yes, that has an impact in our net debt-EBITDA ratio and also, gross debt. But do not forget, 70% of our shipments are in dollars. So we do have a snapshot impact of the balance sheet depending on which moment the snapshot is taking. But the economic impact is limited due to the fact that we have a natural hedge. Once again, 60% of our shipments right now are in dollars, considering our North American operation, part of North American for specialty steels and also exports leaving Brazil.

We still have the objective of working with a net sales to EBITDA ratio of 2.5 times. I believe this is still a goal for us. It's also, obviously, it depends where the exchange rate is going to go. We should remind you that we have other leverages that we have been using. André in his speech talked about our CapEx expectation this year. That is below what it has been in 2014. And remember, when we started 2014, we expected a CapEx in reais that was higher, R\$2.9 billion. So we are also working with investment plans that are very selective.

And once again, working capital, there was already a question about it. I believe that we can do more with working capital. We had a significant reduction in 2013; 2014 the reduction was not as significant as we expected. But yes, there is an opportunity to work with working capital. About asset sales, we do not have anything in the pipeline, but we are always analyzing as we always study any possibilities. We are always reviewing our portfolio and should we understand that there is an interesting opportunity, we should consider it as a possibility.

Q - Alexander Hacking {BIO 6599419 <GO>}

Thank you.

Operator

Our next question comes from Mr. Thiago Lofiego, Merrill Lynch.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Good afternoon. Thank you for the call. I have two questions, first about cost. Can you tell us a little bit more, in the fourth quarter there was a sound performance in Brazil BO, Açominas especially, and I would like to understand if this is recurring? Or was - is it specific to the quarter? And under that the scope of cost cutting, what do you expect for 2015 to optimize your cost base? Second question about infrastructure market in the U.S. Can you tell us how that market is going? We know that this is very important for you and I would like to hear more about it. We know that non-residential is there also, but if you could talk about infrastructure, I would appreciate. Thank you.

A - André Pires de Oliveira Dias

Hello, Thiago. This is André Pires. So first about Brazilian costs and all the initiatives we have been taking. We have started a plan along the second half of 2014. We already mentioned in the call there was asset optimization. We closed some units. And initiatives we are working on to adjust our structure to the business reality, not only in Brazil, but globally as well. So there's nothing non-recurring in the fourth quarter. We believe this is

part of a plan, of a strategy, that is an ongoing one, and we'll keep on working very much concentrated on costs as well as in SG&A. So these are topics in our balance sheet that will really be important in the next years, not only in Brazil, but also in next (54:47) operations.

Infrastructure in the U.S., yes, this is one of the tripods of the American recovery that is still slower than the others. We have three areas, non-residential construction, industrial constructions, and infrastructure. The industrial was first one, non-residential is now growing stronger in the last two years and infrastructure is a little bit slower.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Thank you. André, can you tell us what is the - can you give us a range for cost cutting potential?

A - André Pires de Oliveira Dias

No. We do not have a goal or a figure that we could give you. This depends upon initiatives we take on a daily basis.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Thank you.

Operator

Our next question is from Renan Criscio from Credit Suisse.

Q - Renan Criscio {BIO 18747357 <GO>}

Good afternoon, everyone. Thank you for your presentation. Two questions. First, about specialty steels, we saw a significant improvement and I would like to know if possible, can you let us know where that improvement came from? You have an increase in 10% in the EBITDA. And the second question is about mining, was the exchange rate depreciation, the drop in freight price, what is that like the iron ore from Gerdau delivered to China? At what level of price you change to sell, or to sell here more or to export more?

A - André Pires de Oliveira Dias

Hello, Renan. This is André Pires. About specialty steels, in fact, this better result, the EBITDA growth vis-à-vis the same quarter of the prior year is basically thanks to our North American operation that offset that drop in Brazil, and also thanks to our Spain and European operation. And India has a role to play there. But India's negative result has decreased it a lot, so there was a share of these three elements, North America, Europe and India. Now let me turn to André for the other question.

A - André Bier Gerdau Johannpeter

Well, the iron ore, before the drop in price, we were working with breakeven figures of \$80 to \$85, and then the iron ore went to \$60 to \$65 as we have seen it was not possible

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any more. It is very difficult to give you today a new breakeven figure because there are four or five factors that impacted there. First, our OpEx and the mine logistics cost, the internal costs to load, to the railroad, to the port, the port prices, and then the sea freight. We see that all those shares of the cost have dropped and are adjusting themselves, but not to the point of being able to export at this iron ore price, right. Now, we are still assessing that, analyzing everything, and we would just resume those operations if they become profitable. Our focus, once again, is internal supply to Ouro Branco. That has helped us a lot in terms of competitiveness, in terms of costs and the integrated route there in Ouro Branco.

Q - Renan Criscio {BIO 18747357 <GO>}

That is clear. Thank you very much.

Operator

Our next question is from Alan Glezer, Bradesco BBI.

Q - Alan Glezer {BIO 17508681 <GO>}

Good afternoon, everyone. I have two questions. First, about energy, Brazil. I've seen that realized price and net sales per tonne has dropped to 2% quarter-on-quarter in the fourth quarter. Is there any effect there of mix change because you've closed some plants in Brazil? Did you have any pressure in the mix change that brought the price down? Or if this is a policy of price reduction in the quarter? If you could take this opportunity to explain the price of the exported steel and the domestic price for steel, I think it would be interesting.

And the second is about LatAm BO. I understand imports are a problem, but haven't you been able to - but the volume has grown 3% in the fourth quarter and the margin is above 7%, so what is the trend for 2015? Do you see more pressure that could change that dynamic? These are my two questions. Thank you.

A - André Pires de Oliveira Dias

Hello, Alan. This is André Pires. About your first question about the price per tonne, it has to do with mix effect. As I said before, we have more exports, therefore, we have different prices, lower margins in some situations and at the same time, we have greater dilution of fixed costs, and that's helps costs. And so basically, this is mix. There is no reduction policy or discount that have happened along the fourth quarter of last year.

About the imports, we don't like to talk about premium because that depends on special details on the product, where it comes from and so on. But it's obvious that in an environment where we have real depreciated vis-à-vis the dollar, it is less competitive for the imported product when the real is appreciating - than when real is appreciated. So I would say that importer today has lower competitiveness due to the real depreciation, and also due to volatility that makes predictability difficult for the importer.

Now André is going to talk about Latin America.

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A - André Bier Gerdau Johannpeter

About Latin America. You mentioned the volumes year-on-year, there was a reduction there, but now in the third and fourth quarters they are stable with some growth in the fourth quarter. Actually, in Latin America, 2014 was a difficult year due to the economic growth and 2015 will be also. But just like in Brazil, when each country is a little bit different, but in all these countries, currency is depreciating vis-à-vis the dollar, therefore, competitiveness increases in terms of imported products and that generates more volume. So we foresee a possibility there in LatAm for some gains, some volume expansion due to - or thanks to this higher competitiveness because of the exchange rate and countries such as Peru, Chile and Colombia that are suffering just as Brazil was the depreciation of the currency. That helps the steel sector and the whole chain. So there is this possibility for LatAm in 2015 to grow a little bit in volume with lower imports. But once again, that is going to depend on the international market price. But it depends also on the exchange conversion.

Q - Alan Glezer {BIO 17508681 <GO>}

A follow-up, please, about the realized price, when I mentioned real per tonne in Brazil BO, I was talking about shipments in the domestic market, the volumes for the domestic market. Can you tell us anything about the product mix sold in the domestic market? Has that changed in the quarter? And because of that, if this would explain a change in the cost?

A - André Bier Gerdau Johannpeter

Yes. In fact, when I - thought I was not as specific. But if we analyze the domestic market, there was a higher share of the semi-finished here. That's why we see that small drop in the net sales per tonne. This is a mix and there we had more semi-finished products.

Q - Alan Glezer {BIO 17508681 <GO>}

Thank you very much.

Operator

Right now we conclude the Q&A session. I would like to turn the floor to Mr. André Gerdau Johannpeter for his final remarks.

A - André Bier Gerdau Johannpeter

Thank you very much for your participation. Thank you for your questions. Should you have any questions or if we were not able to address any of them, our IR team is available. And I would like to invite you for our conference call on May 5 to discuss the results for the first quarter of 2015.

Operator

Gerdau's conference call is concluded. Thank you for your participation and have a nice afternoon.

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