

## Q3 2018 Earnings Call

### Company Participants

- Ricardo Lewin, CFO and IR Officer

### Other Participants

- Augusto Akihito Ensiki, Latin America Analyst
- Bruno Amorim, Equity Analyst
- Joshua Milberg, Equity Analyst
- Lucas Marquiori, Research Analyst
- Teresa Clare Barger, Co

### Presentation

#### Operator

Good afternoon, ladies and gentlemen. At this time, we would like to welcome everyone to Rumo's Third Quarter of 2018 Results Conference Call. Today, the conference call will be conducted by Mr. Ricardo Lewin, Chief Financial and Investor Relations Officer.

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

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

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

Now, I'll turn the conference over to Mr. Ricardo Lewin. You may begin your presentation.

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

Good afternoon, everyone. And thank you for attending the call for Rumo's 2018 results.

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Let's begin our presentation from Slide #2. Our transportation volumes grew by 15% in this Third Quarter '18 versus Third Quarter '17. In the first five months of 2018, we see a significant contribution from grains, fertilizers, pulp and containers.

In the Third Quarter '18, the record soybean crop extended the grain export period mitigating lower corn production in a few states. Port loading volume declined due to unfavorable sugar export scenario.

Moving to the next slide. Let's review yield and EBITDA performance. Volume and yield performance, together with cost discipline increased EBITDA to BRL 953 million in the quarter, up 19% year-over-year. Once again, we evidenced our ability to increase volumes while maintaining cost efficiency. This quarter, fuel consumption decreased 4.5% in liter per GTK versus the Third Quarter '17 and fixed costs were diluted.

As a result, Rumo's EBITDA margin reached 51% in the Third Quarter '18, up 2percentile points versus the Third Quarter '17.

Moving to the next slide. We can see the performance breakdown of our business units. The North Operation posted another quarter of consistent results, reaching 60% EBITDA margin. High capacity allowed us to mitigate a higher demand for transportation of corn originated in the state of Mato Grosso.

In addition, other cargo, such as pulp, fertilizer and containers also showed solid performance.

Moving to the next slide. We see Rumo's market share at the Port of Santos. In the Third Quarter '18, Rumo's market share of grains transported to the Port of Santos went up 6.6percentile points. Beside higher generated capacity, which enabled Rumo's Third Quarter volume to grow by 13.9% in the quarter, volume from other logistic sources decreased, demonstrating our competitiveness.

In the first nine months of 2018, the company's market share reached 49.5%, 1.2percentile points higher than the same period last year.

Moving to the next slide. We will discuss South Operation's results. South Operation's volumes in the quarter were similar to those of the Third Quarter '17. The record soybean crop allowed exports to extend to the second half mitigating the impact of corn crop failure in the state of Paraná. However, consolidated results were impacted by an unfavorable sugar export scenario and a client -- usual client shutdown.

The decrease in EBITDA and its margin occurred because in the Third Quarter '17, the result was affected by the recognition of tax credit. However, in the 9 first (sic) (first 9) months of '18, result posted 15.3% EBITDA growth and 0.6percentile points margin expansion.

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On the next slide, we look at grains transported by our railway to the Ports of Paranaguá and São Francisco do Sul.

In the Third Quarter '18, the South Operation's market share was just 5.2 percentile points in the grain transportation to the Port of Paranaguá and São Francisco do Sul. This, again, reflects higher capacity, which enabled a 10% increase in Rumo's transported volume as well as our overall competitiveness since we saw a slowdown in the whole market during this period.

In the first nine months of 2018, we gained 5.8 percentile points market share, while volume grew by 26%.

Moving to the next slide. Let's review our Container Operation's result. Our Container Operation has started to see positive results. In the Third Quarter '18, volume grew by 20% year-over-year and for the first time, this operation posted positive EBITDA. There is still a lot of work to be done. But we are on the right track to grow with profitability.

Now let's take a look at the company's consolidated indebtedness position and consolidated financial results. With the increase of last 12 months EBITDA and reduced net debt, we decreased indebtedness to 2.3x net debt-to-EBITDA this quarter. This is the lowest level since the inception of our investment plan.

Thus we are in optimal position for true cost of debt reduction and financing our investments.

In this quarter, our financial results significantly improved, posting a net expense of BRL 258 million in the Third Quarter '18. The advance in the prepayment process and initiatives to reduce the average cost of debt contributed to the results.

Moving to the next slide. We look at cash flow. It's worth pointing out that this quarter, for the first time, we reached BRL 222 million of cash generation before funding and amortization.

In nine months '18, we can see a cash generation breakeven, reversing the cash consumption in the 6 first (sic) (first 6) months '18.

Moving to the next slide, we present the most relevant operating and financial performance indicators. This quarter, our operating ratio improved 3% versus the Third Quarter '17, reflecting higher yields and reduced fixed and variable unit cost.

In the Third Quarter '18, better energy efficiency drove the 4.5% reduction in diesel consumption as measured in liters per GTK versus the Third Quarter '17, mainly evidencing the gain from renovation of our locomotive fleet and a better mix of products transported.

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When we look at the railway safety indexes, we saw a 2% decrease in rail accidents and personal accidents. It's worth mentioning that referring to the personal safety index, Rumo already achieved the safety goal set by international railway back. The cycle time of railcars improved in the North operation, mainly due to higher efficiency at terminals operated by the company.

Moving to the next slide. We discuss our most recent market projections.

Agroconsult again revised its projections for the 2017, 2018 soybean crop, indicating a 4% increase versus 2016, '17 crop season, both in Brazil production and in the state of Mato Grosso.

For the 2017, 2018 corn crop, Agroconsult foresees an 18% growth in Brazilian production and an 11% drop at Mato Grosso production.

For 2019, preliminary estimates indicate another record soybean crop with 1% growth in Brazil and 2% in the state of Mato Grosso.

In addition, a solid corn crop growth is foreseen, 18% in Brazil and 9% in the state of Mato Grosso.

Now moving to the next slide, our guidance for 2018. Our guidance for the year remains the same, reaffirming our already disclosed projections.

Here I finish our presentation. And remain at your disposal for any clarifications. Thank you very much.

## Questions And Answers

### Operator

(Operator Instructions) Our first question comes from Bruno Amorim, Goldman Sachs.

#### Q - Bruno Amorim {BIO 21628005 <GO>}

Congratulations on the results. So I have a question on yields. You have reported an average increase of 3% yields. Diesel prices were up by 18% year-on-year as you have reported. And I understand diesel is an important component of price.

So just wanted to understand if you could please shed some light on the reason why yield is not going up even further, maybe mix explains that trend. So any color in that sense would be helpful.

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

Bruno, this is Ricardo. Thank you for participating in the call and making question. Bruno, the main factors for the increase of the yield are basically, you're right, one is fuel and the other is a best mix of products, okay. So we had high (inaudible) products in this quarter and -- but basically (inaudible) is also important factor, not only fuels.

### **Q - Bruno Amorim** {BIO 21628005 <GO>}

Okay. And it would also be great if you could give us some color on an update on the potential renew of the take-or-pay contracts with the main customers? Anything in that sense would be interesting as well.

### **Operator**

Our next question comes from Teresa Barger, Cartica Management.

### **Q - Teresa Clare Barger** {BIO 16027598 <GO>}

Congratulations on a great quarter. I was just wondering, Ricardo, could you give us some more color on any updates on the Nobres truck terminal and also (inaudible) and (inaudible) projects in south?

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

Teresa, first, it's an honor to have you in the call. Well as you know, we will be very soon entering a new cycle of the company that we call the group cycle. And 1 project that we intend to do is the expansion to (inaudible).

The first phase of this expansion will be a terminal, not necessarily in Nobres but close to (inaudible) and it will be a truck terminal. We are still studying this terminal. It's not already decided the location and when it will start.

But for sure, we will give more color on that in our next call because it's still premature without the approval of the lease extension to talk about -- sorry, they call it a concession to talk about the extension, But most probably, in the next call, we'll be giving you more color on that.

### **Operator**

Our next question comes from Josh Milberg, Morgan Stanley.

### **Q - Joshua Milberg**

Two questions on my side. The first was -- I think this was asked before. But the first was, if you could just update us on the status of the negotiations with the grain trading companies.

Then also related to that, Lewin, if you could just comment on the issue of the different contract structures that you're contemplating. I think sometime back, you talked about the possibility of a take-or-pay that might have a shorter duration and higher penalty and

then, maybe also a second structure in selling a premium payment. That's my first question.

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

Josh, thank you, you gave a very good question. I think everybody is curious about that. But the negotiation with the trading are going well. We have several contracts already closed. But I cannot give much more color or much more detail on that because we still have several contracts that are under discussion.

What I can give you some details is that, you're right, there are some changes in the way that we are signing the contracts and, as you know, due to the change in the commercial scenario. As you know, tradings that are our main clients has been under pressure, it's squeezed between the take-or-pay contracts and the farmers and the truckers -- truck drivers. So what's changing due to this change in the scenario in the chain -- commercial chain is that we still have a relevant amount of take-or-pay contracts.

Second thing that this contract will be shorter than the ones that we are using. So they will not be two years anymore. But will be 1-year contracts. As we are reducing the term of the contracts, on the other hand, we are increasing the penalties -- the take-or-pay penalties in case of nonperformance. So there will be the minimum of 70% of penalty.

There are other benefits in this contract. I will give you 1 example here, is that the flow of cargo in this -- during the year will be much better, much more uniform than it was in the past.

What's important here, I would like to report and I always report in the meeting that I have with sell side and with our investors is that these changes are not a consequence of the doubt of our clients regarding of which model is more competitive. We are cheaper, we are much more competitive and safe than the other models. But this reflects -- this change reflects the situation of our clients that are squeezed between the take-or-pay -- long take-or-pay contacts and the farmers.

So this is the reason. It's alignment between the clients and the railway in the sense. So hopefully, I answered your question. And I think this is the first question, that's right? You have another one.

### **Q - Joshua Milberg**

Yes. One more, Lewin. And that was very helpful. My second one is if you could comment a little bit on how you're seeing November and December from a volume standpoint.

We had understood that all of the volumes on take-or-pay contracts could be already transported by the end of November, perhaps giving customers a little more flexibility in terms of what they do with either shipping volumes in December or kind of deferring until next year maybe awaiting better pricing. Any color you could give there would be great.

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

Josh we have the guidance. What I can tell you right now is that we are very optimistic about the guidance that we provided. So I think most of you have seen our website volumes. So very soon, we will be giving volumes of October.

The only thing that I reinforce is something that we wrote in the report that -- remember that last year, the harvest was record, the corn harvest. But -- so the volumes were very high last year. So one thing that I'd just say is that don't expect to have a double-digit growth comparing the 2 quarters. But we're relatively sure that will be in the guidance.

### **Q - Joshua Milberg**

Lewin, very understood. You have difficult comps coming into the Fourth Quarter. But can you say a little bit about what you think that today's kind of commodity price level means for the interest of grain trading companies and farmers to kind of go ahead and ship volumes on a more anticipated basis.

Do you think that the pricing is at a level where it makes sense for the grain trading companies to do as much volume as it can? Or could you see them holding some volume until next year?

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

Let me answer. I took a bit longer to answer. So Josh. The point here is that there is a specific situation this year that the war -- the commercial war between China and the U.S.. And there is a huge corn storage in the U.S.

So it's not very clear still what will happen between in these last months between China and the U.S. that can affect the price. So it's not very clear for us to confirm anything regarding the price of commodity and how this can affect us on that.

### **Operator**

Our next question comes from Bruno Amorim, Goldman Sachs.

### **Q - Bruno Amorim** {BIO 21628005 <GO>}

So I have a question on your market share. As you said, your unit costs are coming down, you're gaining market share, which makes a lot of sense. I'd just like to better understand to what extent this could continue to be the case and for how long.

And in that sense, that would be -- that would be great if we could have from you an indication on what's your market share currently. Out of all the grains that are transported from Mato Grosso to the Port of Santos, for instance, how much -- how much market share do you have in this route, any indication you could give us in that sense?

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

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Bruno, you have been following the company and you see that we have been increasing CapEx in the last two years. So while we increased our capacity, it's a good way to increase market share. So obviously, in the long run, we are fighting to gain market share, both in the South and in Mato Grosso. And this will be more a consequence that increase of our capacity and all the investments that we are doing.

These are direct? Yes. We expect increase. How much? This is not part of our guidance. But we do expect to increase our market share. And this is the consequence of our investment that we are doing. Sorry, I don't know if I lost -- you asked about market share, did you ask something else?

**Q - Bruno Amorim** {BIO 21628005 <GO>}

Yes, yes. So I've asked, in this route, Mato Grosso to the Port of Santos, how much is your market share there? Out of all the grains that go from Mato Grosso to the Port of Santos, how much is currently transported by Rumo as opposed to trucks?

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

Bruno, let me tell about the market share of ports, that go from Mato Grosso to Santos. In 2017, that we have already closed something around 50%. So you can see that there is still a lot of room for growth and this is our most important route.

**Operator**

(Operator Instructions) Our next question comes from Lucas Marquiori, Banco Safra.

**Q - Lucas Marquiori** {BIO 17907247 <GO>}

Ricardo, you mentioned it quickly on an earlier question regarding the Malha Paulista concession renewal. So -- I mean, could you give us an update on that? I mean, how are we today? What should we expect going forward? What are the next steps on the renewing process? It would be nice to have a sight on that.

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

Lucas. Well all of you know we did well, I know that. I always say the same thing regarding these questions is that I'm always optimistic that this is resolved by the end of this year.

The point here, Lucas, is that the process has been now two years after having discussed with ANTT. ANTT approved the postponement of the concession. And in September, it was sent to TCU. From then, from this last thing we know that TCU is analyzing the process. They have been talking to some investors that we know about the amount of information that they have, it's a huge amount of information. They need time to analyze all the material that was sent to them, all the studies.

And so formally, TCU has no time to approve that. Although we still have -- doubtless to have this solved soon. As it is in the hands of TCU, we -- it's difficult to make any kind of projection at this stage, almost at the end of the year, when this would be approved.



## Operator

Our next question comes from Augusto Ensiki, HSBC.

### Q - Augusto Akihito Ensiki {BIO 15988025 <GO>}

Two for me. Firstly, on the fertilizer, I mean, it's kind of picking up pretty nice. I was wondering, when it gets to -- where would the normalized run rate be like? How much volume can it reach? And by when will you expect to reach that?

Then secondly, on -- sorry, I lost the question here -- sorry, first question on the fertilizer and then I'll come back with the second question.

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

Okay. Well regarding fertilizers, the operation has been evolving very well. So in the first five months of operation, we have done something around 260,000 tons of fertilizers. What I promised in the past and I reinforce that, I said in the first 12 months, we will be doing 1 million tons of fertilizer.

What's important to say that this first months, we increased our volumes. In July and August, we did something around 100,000 tons of fertilizers and this is what to expect for the next month. So we will reach the 1 million in 12 months. In the long term, what we always said is that we can do something around 3 million to 4 million tons of fertilizers or fertilizer transportation.

### Q - Augusto Akihito Ensiki {BIO 15988025 <GO>}

On an annual basis?

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

Annual basis, that's right.

### Q - Augusto Akihito Ensiki {BIO 15988025 <GO>}

Okay. Perfect. Then secondly, on the financials. So this quarter came down significantly. Is this kind of a normal of what we can expect going forward for financials? Or is there more room for financials to come down?

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

Part of this is a result of the liability management that we have done and also CDI has been going down. So you have these 2 factors in the results. Also you have the hedging account. So you know that 100% of our 2 bonds are hedged.

So you have some noises that for some months, depending on the CDI curve, this can go up and down. We don't have control on that. So there is a small part that can go up and down without our control. But our intention is to keep working in the part of liability

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management and reducing the cost of our debt. So the part that depends on us is expected to still going to go down.

## Operator

(Operator Instructions) That does conclude the question-and-answer session for investors and analysts. Now I'd like to turn the floor over to Mr. Ricardo Lewin.

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

Thank you very much for participating in this call. This is the last call of 2018. So I expect to see you and talk to you next year. Thank you very much.

## Operator

Rumo's conference call is over. Thank you for waiting. Welcome.

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