NLMK

Transcript: Q1 2014 US GAAP FINANCIAL RESULTS

OLEG BAGRIN, CEO

GRIGORY FEDORISHIN, CFO

SERGEY TAKHIEV, HEAD OF IR

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SERGEY TAKHIEV, HEAD OF IR

Good afternoon everybody. This is Sergey Takhiev from NLMK Investor Relations. Thank you very much for joining us today on our conference call to discuss the results for the first quarter of 2014. We will have a brief presentation from Mr Oleg Bagrin, CEO and Grigoriy Fedorishin, VP for Finance, followed by a Q&A session. And with that I will hand over to Mr Bagrin Q1 2014 US GAAP Results

OLEG BAGRIN, CEO

PAGE 3 covers the situation in the GLOBAL STEEL MARKET

- In Q1 this year global steel output increased by 2.5% year-on-year to 400 million tonnes supported by output growth in China and Europe.
- Industry capacity utilization was 78% improving compared to Q4.
- At the beginning of the quarter restocking rates were high especially in China. Since the beginning of the year finished steel stocks in China increased by 50% by end of February. Now inventories are gradually declining on the back of improving demand.
- Average steel prices in Q1 were stable or slightly down compared to the previous quarter. Steel prices in China decreased by around 3% over the quarter driven by growth in inventories and decline in raw material prices. Average steel prices in Europe and the USA were essentially flat.

PAGE 4 covers the developments in the RUSSIAN DOMESTIC MARKET

- Steel production in Russia in Q1 was slightly up at 17.2 million tons. Steel demand was seasonally soft in the first two months of the year but started to improve in March.
- Rouble devaluation was one of the main factors affecting domestic prices. It discouraged imports and provided an incentive for the local producers to shift sales to external markets where prices were more attractive.
- Throughout the quarter steel prices in ruble terms were catching up gradually to reach export parity. Domestic prices were supported by weaker competition and improving demand.

RAW MATERIALS MARKET is discussed on the next PAGE 5

- In Q1 average iron ore prices declined by 9% over the quarter on the back of increased supply. Chinese buying activity was a mixed bag with iron ore imports growing by 20% but iron ore stocks at Chinese ports growing by 30% at the same time.
- Coking coal prices continued to decline and were on average 12% lower vs. Q4 due to continuing supply and demand imbalance. Today we are seeing certain stabilization in the coking coal market but we expect further weakening in Q3.
- Scrap prices were also slightly lower affected by a seasonally soft demand.

Now let’s talk about NLMK production results shown on PAGE 6.

- In Q1 NLMK crude steel production was 3.9 million tonnes 4% lower than in Q4. Apart from seasonal factors this decline was driven by low production at NLMK Kaluga which started industrial trials of sections and angles and therefore decreased output.
- NLMK Group steelmaking run rate was consistently high at 92%. Capacity utilization of the main production site in Lipetsk was 98%.
- In Q2 steel production is expected to remain stable due to scheduled maintenance of the hot end operations at Lipetsk site.

PAGE 7 shows our SALES GEOGRAPHY

- In Q1 Group sales grew by 8% to 3.9 million tonnes. Sales increased across the board both in Russian and international markets. We also used the window of better demand environment and better prices to sell stocks accumulated in Q4 last year.
- NLMK sales to the Russian market grew by 6% to 1.6 million tons. Domestic sales accounted for 40% of our revenue. Construction and infrastructure was the biggest market for us accounting for 73% of our Russian market sales.
- Sales to the international markets grew by 10% to 2.3 million tons. NLMK increased sales to North America by 12% and to Europe by 11%. A portion of sales to the Asian markets was moved to other regions including Latin America where prices were higher.

NLMK SALES STRUCTURE is further discussed on PAGE 8

- Finished product sales grew by 11% to 2.5 million tonnes. Their share in total sales increased from 62% in Q4 to 64% in Q1 in line with one of our strategic priorities.
- The increase in finished steel sales was mainly driven by higher sales of hot rolled products from Lipetsk site and by 11% sales growth at NLMK Dansteel.

PAGE 9 shows our progress against our STRATEGIC priorities

- NLMK remains focused on improving its operational efficiency. In the 1st quarter we continued to roll out our operational efficiency programs and to deploy NLMK Production System an initiative started in 2013.
- Over the course of the quarter operational efficiency initiatives brought structural savings of $70 million over $244 million delivered last year. Key areas of efficiency improvements were core technology and operational practices energy efficiency supply chain and labour productivity.
- With respect to investments we are on track with our most capital intensive project the construction of a pellet plant at Stoilensky and confirm its launch in 2016.
- In the meanwhile we are achieving good progress raising the mine efficiency with the objective to eventually expand iron ore concentrate production by 1 million tons and to reach 15 million tonnes of annual production.

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Now to conclude my part of the presentation NLMK delivered strong results despite continuing overcapacity in the industry sluggish demand and generally challenging macro backdrop. We remain committed to the strategic objectives announced during our Strategy Day in February this year. As we roll out efficiency programs across all Group divisions we remain fully on track to deliver on those targets.

Grigory Fedorishin, CFO

Thank you, Oleg. Good day everyone.

PAGE 10. KEY HIGHLIGHTS

- NLMK delivered a set of strong results in the seasonally weak first quarter of the year.
- Our revenue went up by 5% q-o-q to $2,638 million driven by a 8% increase in sales volumes.
- Top line growth and lower production costs were behind a double digit growth in EBITDA of $468 million.

- This is the sixth quarter in a raw of profitability expansion that went up from 11% in Q1 last year to nearly 18% in the first three months of this year.
- Operating cash flow jumped by 131% to $436 million by 3 times exceeding investment cash outflow. This lead to a free cash flow hitting $271 million in Q1.
- Net debt dropped by $400 mln to $2.3 billion driven by a positive free cash flow. With increased profitability and reduced debt level the Net debt to EBITDA ratio was reduced to 1.39 from the 1.8 in the previous quarter.

Let me now give you more details on the profitability numbers.

PAGE 11. PROFITABILITY

Please turn to page 11

- In Q1 our EBITDA totaled $468 million, a 14% growth compared to the previous quarter and 47% growth y-o-y.
- The q-o-q increase in EBITDA was attributed to the increase in sales volumes, realization of efficiency programs, supporting pricing environment in our export markets, and local currency depreciation.
- In Q1 Steel segment was the major contributor to the EBITDA growth, accounting for nearly a half of the Group EBITDA driven by increased sales volumes and better export prices.
- Profitability of the Mining segment decreased due to lower iron ore prices. However EBITDA margin of the segment actually grew from 65% to 66% driven by further cost efficiencies.
- Long steel profitability was impacted by a seasonally weaker pricing environment and lower sales volumes. In Q2 we already see a reversal of those trends with both growth in prices and better sales.
- International operations posted $23 mln of EBITDA (against $30 mln the quarter before), mainly impacted by stronger slab feedstock prices.

PAGE 12. CASH FLOW

Let’s turn to page 12, where we discuss the Q1 cash flow

- In Q1 our net operating cash flow grew 3 times q-o-q to $401 million driven by growth in sales and better profitability.
- Working capital remained flat despite a 5% growth in revenue.
- Our total capex was $131 million, a sequential growth of 33% from a seasonally lower 4th quarter base.
- With strong profitability and low level of investments our Free Cash Flow jumped to of $271 million, which is almost 3 times increase q-o-q and y-o-y.

PAGE 13. DEBT LEVERAGE

Please turn to page 13 for the debt leverage discussion

- Net debt declined by 15% q-o-q to $2.3 billion driven by a sizable growth in Free Cash Flow.
- In Q1 gross debt dropped by 7% q-o-q to $3.89 billion as we settled some of our borrowings totaling $149 million.
- The Net debt/EBITDA ratio declined to 1.39 compared to 1.8 at the end of Q4. This ratio decline is in line with our long-term target of 1.0.
- Average maturity period for our loan portfolio decreased to 3.2 years.

PAGE 14. SETTLEMENT OF FINANCIAL LIABILITIES

We will continue the discussion of the debt and liquidity on the page 14.

- The Company has substantial liquidity with almost $1.6 billion in cash and short-term investments and committed undrawn bank lines of about $2.8 billion.
- Our short term debt stands at $1.1 billion.
- The amount is represented by ruble bonds, credit lines including revolver lines for the working capital financing and ECA financing.
- Long term liabilities of $2.7 billion are represented by the Eurobonds and a long term portion of ECA.

PAGE 15. OUTLOOK

Finally let's turn to the outlook.

- In Q2 we anticipate seasonally better conditions in our key markets, including in the local market that enters into high demand season.
- Steelmaking utilization rates are expected to remain above 90% for the Group core assets.
- In Q2 crude steel production will be largely flat totaling 3.9 million t.
- Ongoing realization of operational efficiency programs and somewhat better demand patterns will contribute to further growth in our financial results.

With this, the formal part of the presentation is over and we are ready to answer your questions.

Thank you for your attention.

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