Conference Call Transcript — 1Q14 Results — May 7th, 2014

Operator:

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to América Latina Logística ALL's 1Q14 earnings conference call. Today, with us, we have Alexandre Santoro, CEO, Rodrigo Campos, CFO and IRO, and Pedro Albuquerque, IR Superintendent for ALL.

We would like to inform you that this event is being recorded and all participants will be in a listen-only mode during the Company's presentation. After ALL's remarks are completed, there will be a question and answer session. At that time, further instructions will be given. Should any participant need assistance during this call, please press *0 to reach the operator.

We have simultaneous webcast that may be accessed through ALL's IR website, www.all-logistica.com/ir. The slide presentation may be downloaded from this website. Please, feel free to flip through the slides during the conference call. There will be a replay facility for this call for one week.

Before proceeding, let me mention that forward-looking statements are based on beliefs and assumptions of ALL 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 ALL and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Rodrigo Campos, CFO and IRO for the Company, for a brief explanation of how ALL's figures are presented; and then, Mr. Alexandre Santoro, CEO, who will start the presentation.

Mr. Campos, you may begin the conference.

Rodrigo Campos:

Thank you for holding the conference of ALL. Just before start, I would like to make a brief comment about the numbers we will be releasing in this presentation. As you know, we do not operate concessions in Argentina anymore since June last year. And since then, all the results coming from Argentina are in a separate line called 'results of discontinued operations'.

But as in the 1Q13 we were still operating concessions there, the results, which were released in the 1Q13, were consolidated. So, in the results we are showing now, in the 1Q14 we are comparing with results of the 1Q13 already booked as discontinued operations, in order to have a comparable basis.

Conference Call Transcript — 1Q14 Results — May 7th, 2014

With that, I would like to pass the word to Alexandre Santoro.

Alexandre Santoro:

Thanks, Rodrigo, and good morning, everybody. To start our call, I would like to mention a few important highlights in this 1Q of our company, pointed in slide number four. We reached a consolidated adjusted EBITDA growth of 11.5%, mainly through yield increases in our rail operations and to contributions from Brado Logística. Our rail operation volumes increased 1.2% in this 1Q. Our volume performance in the rail operations was marked by a bad January when compared to last year, in which we benefited from an extraordinary amount of corn volume left from the second corn crop of 2012.

So, we decreased our volumes in January against last year. But during February and March, however, we performed much better and were able to increase volumes near double digits. In addition, agricultural volume was also impacted by a worse mix of products, mainly in the Wide Gauge corridor, contributing to lower asset productivity.

We had a good quarter in terms of industrial volumes as it increased more than 10% in the 1Q, mainly driven by our pulp and paper segment and by Brado's growth. Brado was able to grow in the main corridors that it operates, the Wide Gauge and Paraná corridors, but did not perform so well in Rio Grande and Mercosur corridors.

This way, total volumes grew almost 8% year-over-year in the 1Q. Ritmo Logística did not have a good quarter. The volumes decreased 16% in the 1Q, and the adjusted EBITDA dropped 24.6% to R$4.5 million, pressured by a volume decrease in both Intermodal Business Units and Dedicated Solutions Units.

An important step for us happened in March, when we got the remaining necessary environmental license from IBAMA for our rail stretch duplication project from Campinas to Santos. This is a very important project for us and for the Country as well, as it will structurally increase capacity in our Wide Gauge corridor, the most relevant corridor in terms of agricultural export in Brazil. Our Rondonópolis project, which is also structured in terms of grain exportation, is operating at capacity now and is ready to hold volumes for the peak of the harvest.

Going to the consolidated reserves, we can see on slide number five that the adjusted EBITDA reached R$444 million and 11.5% growth in the 1Q against last year. Our rail operations contributed with 11.3% EBITDA growth and Brado posted an improvement of 41.4% year-over-year in this figure, while Ritmo Logística's EBITDA performance offset a part of it.

Our consolidated net profit was R$7.4 million in the 1Q, lower than the 1Q13. And we had higher financial expenses with increasing interest rates almost 50% and inflation here in Brazil.

Now, I would like to pass to Rodrigo, who will discuss the results of our business units, as well as the financial consolidated highlights. Thank you.

Rodrigo Campos:

Thank you, Santoro. Starting from the rail operations business unit, as Santoro said, volume increased 1.2% year-over-year in the 1Q14, mainly driven by an atypical 1Q13, very strong. We know that the 1Q normally is the weakest quarter in terms of volumes and seasonality in the railroad. And last year, we had a strong 1Q because of high volumes of inventory of corn at the end of the year that pushed volumes on January. But we will talk a little bit more about that when we talk about agricultural commodities.

Our net revenues increased 10%, with a good yield increase, average tariff increase of 8.7%, which basically reflects the inflation and diesel price increase in Brazil, the pass-through of diesel price increase. And in terms of EBITDA, EBITDA increased 11.3%, with an increase also in EBITDA margin from 53.7% to 54.3% in the 1Q14 as compared to the 1Q13.

In page seven, we start to open the agricultural commodities business unit. We see that in agricultural commodities, volume decreased 1.7% and hugely explained by the seasonal effect I mentioned. When we look at the volume per month, we see that in January that is typically the weakest month in the year, it went down 20% as compared with last year. Last year, we had strong volumes of corn in January, as Santoro mentioned. But the volume increased 8% in February as compared with last year and 8% in March, so recovering part of the drop we had in January 2004.

And also we have an additional impact in terms of volumes in agricultural, which is related to the sugar transportation in the State of São Paulo in our Wide Gauge corridor. We increased almost 40% volumes of sugar there. And we know that sugar has a smaller average distance, a lower productivity in terms of rail and port. So, at the end of the day, it reduced average productivity and impact volume growth also.

Going to slide eight, we start to look the results in agricultural commodities. We see that revenue grew almost 10% despite of the 1.7% volume drop, and it is very related with the increase in the average yield, in the average tariff, which reflects inflation and diesel price pass-through to our tariffs. In terms of EBITDA, EBITDA grew 10.2%, with a 0.3% increase in margin from 56.7% to 57%.

When we go to slide nine, we see that we had a good quarter in terms of industrial products business unit. Our volume grew 10%, pushed by intermodal flows, more specifically with wood and paper flows, and with 18% increase in containers measured in RTKs, so a very good growth in wood and paper and containers. And in pure rail products, we increased volumes 1.7% basically because of the construction segment.

When we go to the results of industrial products in slide number ten, we see that net revenues increased 11.2% and average yield was more or less in line with last year, it increased 0.5%.

In terms of our agreements, we passed through inflation in diesel as we did in agricultural, but there was a very important mix effect in the industrial with the increase in the containers, increase in wood and paper flows, and a decrease in volumes transportation, which makes the average yield lower despite of inflation and diesel price pass-through.

In terms of EBITDA, we have a material gain in industrial business unit; we increased almost 17% EBITDA as compared with last year, with an important EBITDA margin increase from 42.2% to 44.3%.

When we go to Brado, in slide 11, we see that volumes in Brado increased 8%, as measured in containers in the 1Q14 as compared with the same quarter of last year. And the average distance grew a lot. Remember that when we measure in RTKs, not only containers but multiplied by the distance, the growth was 18% and was very concentrated in two corridors, which were the corridors we have prepared Brado to grow. We have added rolling stocks for 2004, which were the Wide Gauge corridor, which links Mato Grosso and Santos and on the Paraná State corridor, which concentrates Brado's growth.

In terms of EBITDA, Brado increased more than 40% with a meaningful margin gain from 15% to 21%, so a 6 p.p. increase in Brado's margins, which reflects the increasing average distance, also reflects beginning of Rondonópolis, a good quarter for Brado in the 1Q14.

Going to Ritmo, in slide 12. Ritmo, by the other hand, had a tough quarter. In terms of volumes, volumes dropped 16% in the 1Q as compared to the same period of last year. Part of the volume drop was related to the dedicated operation, and we leave some operations where we were not able to pass through to the tariffs the cost increase we had. So, at the end of the day, we will leave some operations. And intermodal flows, which are the segments we have been growing in a very strong way in the last two years, our volume dropped 20% because of a structural change in an operation of a client. So, we lost this operation. But even considering that, I believe we have a very big opportunity in intermodal operation in Ritmo. So, we should be able to grow even in an environment like that. So, not a good commercial quarter for Ritmo, and Ritmo should start to capture the opportunities they have in intermodal to keep growing at the rate it was growing in the past.

In terms of adjusted EBITDA, EBITDA decreased 25%. Of course, the Company has a fixed cost structure. And with this reduction in volumes, you have an impact in EBITDA higher than the volume drop itself. So, margins went down from 10% to 8%, going down 2% in EBITDA, ending the quarter in R$4.5 million.

Going to the financials, on page 13, we see our consolidated net revenues that we already mentioned, that grew 8.1% in the quarter.

In slide 14, we see that our EBITDA increased 11.5% in a consolidated basis, and our margin increased from 48% to 49%.

In slide 15, we see that our net income decreased to R$7 million from R$34 million. And it is mainly driven by an increase in the interest expenses. You know that our EBITDA increased, operational results increased, but interest rates in Brazil increased 50% as compared to the same period of last year. Also, inflation was higher, so inflation-denominated debt was also impacted by these trends. So, at the end of the day, we had a drop in our net income pushed by interest expenses.

On page 16, we see our capital structure. We see that our net financial debt/adjusted EBITDA increased from 2.2 to 2.48. And usually in the 1Q the deleverage increases, because this is a low-season quarter, so we have less revenues, which has to pay for the same fixed-cost structure. So, of course, it is impacting the cash flow. And by the other hand, you also have more CAPEX, because you are preparing the Company for the crop season. And also, this is the period that you have more time to offer to make the works on the tracks, given the low volumes we have.

So, it naturally intensifies the CAPEX during this period of the year. So, with higher CAPEX, lower operational cash generation, naturally the leverage increases in the 1Q every year.

With that, I would like to pass the word to Santoro to make some additional comments.

Alexandre Santoro:

Thanks, Rodrigo. Just some quick additional comments on the quarter's results and on our expectation for the next quarters. First, we expect to have a better operational condition from the 2Q onwards, as most of the problems at the port have already been solved by the beginning of this year.

We have faced problems in the port since the 2Q13, mainly in TGG and T-XXXIX terminals in the grain segment, as well as difficulties in the rail unloading structures in other segments. The grain terminals are already operating regularly, and investments for the recovery and expansion of terminals are happening in the other segments. Rondonópolis is ready to load the major part of the agricultural commodities volumes that were loaded before at Alto Araguaia terminal. Increasing average transported distance and putting the Company prepared to hold volumes from the harvest peak in the 2Q and 3Q14.

And as you already know, on April 15th, our Board of Directors approved the proposal sent by Rumo aiming to merge the companies. The merger is still conditioned to the approval of ALL shareholders in an Extraordinary Shareholders' Meeting to be held tomorrow here in our headquarters at 4:00 PM São Paulo time, and to the approvals of Brazilian Antitrust Authority, CADE, the National Land Transportation Agency, the ANTT, and also to other precedent conditions.

With this, I conclude our presentation and put ourselves available for clarifying any doubts you may have. Thank you.

Mark Suarez, Euro Pacific Capital:

Hi. Good morning. Just to go back on the rail duplication project you have from Campinas to the Port of Santos, how much rail capacity do you expect to add after this is concluded and what sort of productivity gains do you expect to achieve? If you can give us some more color on sort of what productivity gains you mean, you are talking about longer and heavier trains, sort of speed, velocity of the locomotives. I am wondering what sort of metrics you are looking to achieve here?

Rodrigo Campos:

OK, Mark. When we duplicate Campinas to Santos, we add a lot in terms of capacity, so we increase from a capacity of, in pars of trains, from 15 to 37, so we more than double the capacity from Campinas to Santos.

And also, as you know, today the train has to cross and this is the tracks where you have more density of trains. So, average speed was very low. After the duplication, the train goes and comes back straight to the port, so a lot of gain in terms of transit time. So, of course, the potential increase in terms of volumes is huge. We will be able to haul much more sugar, also much more grains than we haul today, after the duplication.

In terms of productivity, it will depend a lot on the kind of route you are. On the sugar that is a shorter-distance route, the impact will be very important because this segment represents almost all the extension of those routes. So, the transit time would be reduced by half or better than that.

In terms of the longer routes that go to Mato Grosso, it will depend on the month, it will depend on the port, but it can be reduced 15%, 20% in terms of the transit time.

Mark Suarez:

Got you. And then, just to follow up on that, the sugar volumes have actually trended very strongly in the 1Q. Should we expect maybe the sugar traffic to the terminals to maybe eat up some of that capacity or most of that capacity, including the duplication if and when the merger is approved? Should that be the trend that we should be looking forward to?

Rodrigo Campos:

Could you repeat, Mark? I could not hear you very well.

Mark Suarez:

Just on the sugar volumes that you talked about this quarter. I wonder if and when the merger is approved, obviously that is conditional on a number of factors, but should we expect greater sugar traffic to maybe eat up that new capacity once the duplication is concluded? How should we think about sugar volumes vis-à-vis the rest of the agricultural commodities?

Rodrigo Campos:

Mark, as you said, in order to be concluded, we need to have first the shareholders' meeting approval, which is tomorrow. So, we will see if it is approved or not. And after approving that, we need CADE's approval. In this period, both companies will be managed in a completely separate way. But independently on that, the duplication will completely change the productivity in terms of the railroad in sugar routes, and also will create capacity to increase volumes in sugar and increase a lot also in the grains.

So, with the duplication, we would be able to accommodate all these contracted volumes that today we were not able to attend. So, duplication is important. Of course, it is not only a matter of duplication. We need also the port capacity. Rumo is doing the investments on the port. And today we set the volumes we transported based on the port unloading capacity. But, pacing 12 months ahead, which is the period we are talking here in order to conclude the duplication, probably the port will be operating fully also, and so all the conditions will be there.

Mark Suarez:

Got you. And now, when we talk about the terminals of the Port of Santos, Rumo is, as you mentioned, making some investments right now. Do you expect terminal capacity to maybe increase over the next 12 to 18 months, therefore making the logistical system more efficient as you increase your rail productivity, capacity if you will?

Alexandre Santoro:

Yeah. When we think in terms of this 12 period timeframe, which is our forecast for completing and the duplication to Port of Santos, the plan of Rumo, for sure, is to have the terminal completed there. But to have the exact timeframe of the works on the terminal, on the port, the best thing is to ask Rumo.

Conference Call Transcript — 1Q14 Results — May 7th, 2014

Mark Suarez:

Got you. OK. I will get back in the queue, guys. Thanks.

Kevin Kaznica, Citigroup:

Can you hear me? OK. Just one quick question: was on the 1Q rail investment plan partially related to the shutdown or repair of the Wide Gauge corridor, and are you considering an investment of your plans on annual CAPEX related to that?

Rodrigo Campos:

Stephen, if I hear you well, I understand that you are questioning about the increase in CAPEX in the 1Q14 as compared to 1Q13. Am I right?

Kevin Kaznica:

Yes. We were just wondering if part of that was related to the shutdown or repair of your Wide Gauge corridor, or was that...?

Rodrigo Campos:

Yes. There are two factors here. When you compare with last year, we take advantage of the lower volumes we had in January to increase, to concentrate more the CAPEX in the 1Q, which is good because they depend less on the time between the trains to do the work that I need, so intensify the maintenance and the CAPEX we need for the crop season. This was one thing.

The other thing, you are right, was that we got the environmental licenses, so we started to do the CAPEX there. We mobilized all the teams to start working there since the first day we got our license. So, there was an additional CAPEX related to the duplication of rail track from Campinas to Santos. Remember that today this is a part of contract with Rumo, but due to litigation, the cash flows are free. So, we are doing that by ourselves, because the returns related to the duplication are unquestionable, are very huge. We would not like to delay the CAPEX plan because of the litigation.

Kevin Kaznica:

Understandable. So, also a quick follow-up, are you considering an adjustment of your plans on annual CAPEX, so just like the incremental, an addition overall, or I guess your CAPEX guidance is still holding for the rest of the year?

Rodrigo Campos:

Our guidance for CAPEX is R$800 million. It is been the same. Of course, it does not comprise the duplication, which is something that is inside our agreement with Rumo, and we expect to solve that in some way until then.

Kevin Kaznica:

OK, very helpful. Thank you.

Mark Suarez, Euro Pacific Capital:

Hi, guys. Thanks for taking my call one more time. I just had a follow-up question on the CAPEX here. You mentioned your funding for the rail duplication since you do not want to lose time. That is how I understand it. I am wondering if and when the merger is approved, how is that going to change? Is Rumo going to be taking up the remaining balance of the projected CAPEX, and how are they going to fund it? What are the detailed funding plans, if you will, if you have any at this point?

Rodrigo Campos:

Mark, I really cannot anticipate anything like that at this point, because, first, it must be approved tomorrow by the shareholders. After that, both companies will keep being managed in a separate way. So, until you have CADE's approval, we cannot consolidate anything and we do not do that. So, it is hard to answer that right now. So, we do not have this visibility. At the end of the day, what I can tell you is that we will do the CAPEX independently of what will be the outcome of all the decisions.

Mark Suarez:

OK. And just one last thing, on the potential merger here. Assuming that everything goes according to plan and CADE shows approval, what do you think the turnaround time for the two government agencies as to either approve or reject the merger? Are we talking about a matter of days, weeks, or months? I am just trying to get a timing on as to when potentially we could see this merger come to fruition.

Rodrigo Campos:

Yeah. I believe the biggest timeframe naturally comes from CADE, which has a legal timeframe of 330 days to decide, to approve or not approve, to have a final decision. Of course, this is the maximum and it could be the decision of CADE could come in a much shorter time, but the maximum timeframe is these 330 days.

Mark Suarez:

OK. So, it would not be out of the realm of possibility this could only come into fruition by next year, or do you think that that is just too conservative and maybe we could see, again, assuming everything comes into play, that this could be a 3Q event?

Rodrigo Campos:

I believe that once the deal is approved, of course the best thing to do is to provide CADE all those information and help CADE analyze as fast as possible, because, of course, it is good for everybody. And for sure, CADE also will want to have the decision as fast as possible. So, of course, the idea is to accelerate that, to provide all information in order to accelerate that. But, it is difficult to anticipate. It can take 330 days. It can take three months, two months. It is hard to tell.

Mark Suarez:

Right, OK. That is all I have for now. Thanks again for your time.

Alexandre Falcão, HSBC:

Hi. Good morning, everyone. Actually, my question is regarding 2Q and 3Q, where we are probably going to see a lot more sugar volumes kicking in. I just wanted to pick your brains on in terms of where the volumes allocation are going to be between sugar and grains on the 2Q and 3Q.

And if you guys could explore a little bit in terms of growth of volumes from now until the end of the year, is it feasible to assume a 10% increase in volumes even with very concerning data from the industrial front that we are seeing in the 1Q14? Thank you.

Rodrigo Campos:

Thank you, Alexandre. In terms of volume on sugar, what we have been doing is to haul based on port unloading capacity, so we will keep doing that. Of course, as compared with last year, probably we will have a meaningful growth, but it is hard to anticipate what the capacity will be, at least from this point. So, we will keep doing the same in the volumes of sugar. We will follow the same thing.

And in terms of industrial volumes, I believe we have been growing in the last quarters, and even considering lower industrial activity, we keep seeing good source of growth from the new projects in the wood and paper segment, and also from Brado. So, we should sustain the growth in industries products.

Yeah. The 10% growth you mentioned in the consolidated basis, you know that we do not give annual guidance. But we prepare ourselves every year to grow high-single digits, low-double digits. But, of course, the growth depends on several things. And we do not give annual guidance, more a long-term guidance. But, it makes sense when we look to long-term targets.

Alexandre Falcão:

OK. Thank you.

Operator:

Since there are no questions, I will turn over to Mr. Alexandre de Santoro for final considerations. Mr. Alexandre de Santoro, you may give your final considerations.

Alexandre Santoro:

Well, thank you, everybody. Have a great day. We will keep in touch to talk about the results of the shareholders' meeting tomorrow. Thank you, everybody.

Operator:

Thank you. This concludes today's ALL's earnings conference call. You may disconnect your lines at this time.