# MMK Group

FY 2019 FINANCIAL RESULTS CONFERENCE CALL
EDITED TRANSCRIPT

## MMK Group's speakers

Andrey Eremin, CFO

Mariya Nikulina, Director for financial resources

Veronika Kryachko, Head of Investor Relations

## Participants asking questions

1. Andrew Jones – WOOD

## Presentation

**Veronika Kryachko**

Good day, ladies and gentlemen. My name is Veronika Kryachko. And on behalf of MMK Group, I would like to welcome you to our conference call on Q4 and 12 months of 2019 IFRS financial results. I would like to introduce the MMK team that is presenting today: Andrey Eremin, Chief Financial Officer, Mariya Nikulina, Director for Financial Resources. We will start our call with update on key financial results and market overview presented by Andrey Eremin. Please, sir, go ahead.

**Andrey Eremin**

Good day, dear ladies and gentlemen. We are pleased to welcome you today. Thank you for joining us, for the presentation of MMK Group financial results for Q4 and 12 months of 2019. Let's begin with slide 4. In Q4 the Company's performance was under pressure from significant price correction on global steel market, as well as seasonal weakening of business activity in the Company's main sales market. MMK Group's revenue declined by 14.3% from the previous quarter and amounted to USD 1,722 million. EBITDA was down 36.2% quarter-on-quarter (q-o-q) to USD 335 million, while EBITDA margin declined by 6.6 p.p. to 19.5%. Despite the decline in profit, free cash flow amounted to USD 272 million in Q4.

Compared to our results for 2019, I'd like to note that several factors had the negative impact on EBITDA. These were low production volumes due to a new reconstruction phase of Mill 2500 and decline in global prices for metal products and a significant price increase for iron ore materials. As a result, EBITDA decreased by 25.7% year-on-year (y-o-y) to USD 1,797 million. The decline was partially offset by an increase in sales of HVA products, including sales of thick plate Mill 5000. The decline in free cash flow by 14.9% for full year 2019 to USD 882 million, was tight to a decrease in profitability amid high volatility in global prices.

In Q4, we saw further decline in global prices for metal products, which reached the lowest level seen over the last several years. As a result, average price for HRC for the quarter on the FOB Black Sea basis declined by 16% to USD 404 per tonne. Iron ore prices also declined from their peak in mid 2019. This price adjustment came against the backdrop of negative price dynamics for metal products and the growth of export shipments of iron ore from Australia. Platts index IODEX Fe62% declined by 12% to USD 89 per tonne in Q4 2019.

The reduction in spot purchases of coking coal from China intensified price competition among coal companies. As a result, global benchmarks for coking coal prices saw negative trends in Q4.

The improved productivity of MMK's blast furnace allowed pig iron output to increase by 1.7% in Q4 2019 to 2.6 million tonnes. At the same time, steel output decreased by 3.9% due to seasonal decline in demand. Overall for 2019, pig iron output increased by 1.6% y-o-y, due to reduction in maintenance work at the Company's blast furnace facilities. The decline in steel output by 1.6% y-o-y was caused by decreased demand for steel, as well as construction works at hot-rolling mill 2500. In Q4 capacity utilization of high-margin production units remained at a high level.

MMK Group's finished product sales amounted to 2.78 million tonnes in Q4 2019, a decrease of 4% from the previous quarter. This was due to seasonal weakening in business activity and the significant decline in prices on the global steel market.

The sales share of high value-added (HVA) products remained at a high level, making up 46.6% of total sales at MMK Group. This was despite a decline in sales in Q4 2019 amid weaker demand from the construction industry and more complex production mix at Mill 5000.

Over the year, the Company increased its sales of HVA products by 1.9 p.p. to a total sales volume of 48.4%. This was made possible by record shipments of thick plate Mill 5000.

The share of sales to the domestic market decreased to 82% in Q4 2019, as a result of a seasonal slowdown in business activity.

Overall for 2019, the Company increased its share of sales to domestic market to 85%, which had a positive impact on the Company's financial results.

The sales structure on the domestic market by industry was effected by seasonal factors.

In Q4 2019, MMK Group reallocated its export sales to the Asian market where the margins are higher. As a result, this market accounted for 20% of international market sales.

MMK Group's revenue declined by 14.3% q-o-q to USD 1,722 million. The key factors in this decline were a significant correction in the global steel prices and a seasonal slowdown in business activity.

MMK Group's cost of sales amounted to USD 1,323 million in Q4. The decrease of 6.6% q-o-q was due to lower sales volumes and the correction in prices for basic raw materials.

Blast furnace raw materials made up a greater share in the structure of material costs, due to an increase in pig iron production in Q4 2019. At the same time, there was a significant reduction in the share of metal scrap due to lower capacity utilization of electric-arc furnaces amid lower steel output.

As a result, the slab cash cost decreased by 9.6% to USD 283 per tonne. The key factors for this decline were lower prices for iron ore and coal concentrate, as well as a decrease in the share of pellets in the blast furnace charge, and metal scrap in the steel production process.

As a result of negative market factors, profitability indicators decreased in Q4 and FY 2019 as a whole. EBITDA of the Russian steel segment amounted to USD 327 million, down 36.9% q-o-q.

EBITDA of the coal segment amounted to USD 10 million, a decrease of 28.6% q-o-q amid a negative correction in prices for coal concentrate.

By the end of 2019, EBITDA of the Russian steel segment amounted to USD 1,744 million, down 23.6% y-o-y. The difficult economic situation in Turkey put pressure on the performance of the steel segment in that country. EBITDA of the coal segment for 2019 declined due to a 12.9% decrease in the coal concentrate sales. This was tied to reconstruction of the beneficiation plant, as well as to lower market prices.

MMK Group continues to consistently implement its investment programme in line with the Company's strategy up to 2025. CAPEX for 2019 amounted to USD 833 million, down 3.1% y-o-y. The key events in 2019 were the launch of a new sinter plant No. 5 and reconstruction of roughing train at hot-rolling Mill 2500.

The new sinter plant allowed to increase our output of sinter by 1 million tonnes, thereby, reducing the consumption of more expensive materials such as pellets. The new plant also significantly improved the Company's environmental performance.

Among the major projects planned for this year I would like to highlight the construction of new coke battery complex and the final reconstruction stage at Mill 2500.

NWC in Q4 amounted to USD 953 million, which is the lowest level on record since the Company went public in 2007. The significant decrease was tied to the acceleration of the turnover of settlements with customers - a decrease in accounts receivable and an increase in advance payments from customers. As a result, NWC to revenue ratio at the end of the year amounted to 13.8%.

Regarding MMK Group's debt burden, I would like to note that despite our Eurobond placement in 2019 we continue to have one of the lowest debt burdens among all global steel producers.

At the end of 2019, the Company had 1.1 billion in cash and deposits on its accounts, which fully covers MMK Group's total debt of USD 870 million. Therefore, the net debt / EBITDA ratio as of 31 December 2019 was negative.

Free cash flow (FCF) for Q4 amounted to USD 272 million, down 5.9%. The main negative factor was a decrease in EBITDA by 36.2%. However, the effective maintenance of working capital allowed the Company to significantly reduce the impact of EBITDA decline.

The stable generation of positive free cash flow and a sustainable financial position allowed the Company to pay dividends on a regular basis.

In November 2019, the Company's Board of Directors approved a new dividend policy that formalised the payment of dividends equal to 100% of FCF.

On 4 February 2020, the Board of Directors recommended that the Annual General Meeting of Shareholders approved the payment of dividends for Q4 2019, which equals to 100% of FCF for the Q4 2019.

To conclude, I will focus on the outlook for Q1 2020.

The Company expects metal production to decline in Q1 2020 due to the maintenance of blast furnace and converter facilities. Production will also be affected by the suspension of operations at hot-rolling Mill 2500 due to its planned reconstruction in March (suspension will last 110 days).

Capital expenditure in Q1 2020 is expected to remain unchanged from Q4 2019, which is fully in line with the current investment programme as part of the Company’s strategy.

The Company’s performance will be supported by the favourable price environment on the domestic market and price stabilisation for key raw materials.

The Company’s performance should be further supported by measures to increase operational efficiency and high capacity utilization of high-margin production units.

This is the end of my presentation, thank you for your attention, we are now ready to answer your questions.

## Questions and Answers

### 1. Andrew Jones - Wood

**Andrew Jones:** Are you still talking about studying USD 900 million CAPEX for the full 2020?

**Andrey Eremin:** Speaking about the guidance on CAPEX plan for the full 2020. We actually expect CAPEX to be approximately USD 900 mln for this year, based on the fact that this year CAPEX was a bit lower than we expected. So, there is a possibility that it will be a bit bigger next year, but we’re talking of maximum of plus USD 50 mln.

**Andrew Jones:** Any guidance on specific volumes of working capital in Q1 2020?

**Andrey Eremin:** Talking about working capital, in Q4 we actually saw significant relief in working capital, mainly due to relief in accounts receivable. So actually in the last days of December we received abnormal, advantage from few of our customers, which affected FCF for Q4. In Q1 2020 we actually expect prices to go up and working capital to be higher than Q4, so it will have impact on free cash flow for Q1 2020.

**Andrew Jones:** Any guidance on production volumes?

**Andrey Eremin:** So, in Q1 2020 we expect reduction in the volumes, just because of repairment works for the blast furnace and the converter. In Q2 2020 we’ll see reduction in volumes due to reconstruction of hot-rolling Mill 2500 which will lasts for 110 days. Comparing to Q4 2019, we will see reduction in our volumes by 70–100 thousand tonnes. For the whole year 2020 we will maintain the volumes, so we expect high volumes in Q3–Q4 to compensate the reduction in Q1–Q2 because of repairment works.

**Andrew Jones:** Can you give some guidance to cost of your iron ore and coal contracts? What sort of dynamics can we expect in terms of costs and in terms of volumes for Q1?

**Andrey Eremin:** We saw a reduction in the coking coal price in Q3–Q4 2019 by 16%. We’ll have the same price reduction in January 2020. Starting from February, we we’ll have price reduction by 2% for the next 5 months. And expect this price to maintain up to the end of the year. Talking about iron ore price, they fluctuate with index based with time lag of 2 months.

Ladies and Gentlemen, this is Veronika Kryachko and thank you very much for your time today. If you have any questions, please feel free to contact us any time. With this, we would like to close the call and wish you all a very pleasant evening. Good bye.

***