

01 OCT 2024

Fitch Affirms Gerdau S.A. at 'BBB'; Outlook Stable

Fitch Ratings - New York - 01 Oct 2024: Fitch Ratings has affirmed Gerdau S.A.'s (Gerdau) Long-Term Foreign and Local Currency Issuer Default Ratings (IDRs) at 'BBB'. Fitch has also affirmed Gerdau's National Scale Ratings at 'AAA (bra)', senior unsecured notes, and the senior unsecured notes issued by its related or subsidiary companies at 'BBB'. The Rating Outlook remains Stable.

Gerdau's rating affirmation is indicative of the sustained robustness of the company's market position, capital structure, extended maturity schedule, and liquidity profile. The company's geographic diversification and the adaptable operating framework of its electric arc furnace steel production enable Gerdau to respond expeditiously to evolving market conditions.

Gerdau's ratings are not constrained by Brazil's 'BB+' Country Ceiling because of its ability to service debt with cash flow generated by its U.S. subsidiaries and/or the cash and marketable securities it holds outside of Brazil.

Key Rating Drivers

Strong Business Position: Gerdau is a prominent producer of long steel in the Americas, maintaining an industrial presence across seven countries. The company's diversified asset portfolio mitigates the impact of significant downturns in primary markets, such as Brazil and the U.S., thereby conferring a degree of stability to its cash flow. In 2023, Gerdau's EBITDA composition was as follows: North America accounted for 50%, Brazil for 25%, South America (excluding Brazil) for 12%, and Specialty Steel for 13%.

Low Leverage: Gerdau's commitment to maintaining a strong capital structure is a core rating consideration. Fitch expects the company's gross and net debt/EBITDA ratio to reach 1.2x and 0.5x in 2024, and gross debt to be slightly above Gerdau's BRL12.0 billion long-term target. The expected average gross and net leverage metrics between 2024 and 2026 are 1.1x and 0.5x. Gerdau's financial policy also includes keeping an average maturity term beyond six years and net leverage below 1.5x.

Flexible Operations: Gerdau's production structure consists of 75% electric arc furnaces and 25% integrated blast furnaces with two iron ore mines, enhancing raw material self-sufficiency. Despite rising domestic demand, increased Chinese steel imports (up 29% in 1H24) and ineffective tariffs keep Brazilian steel prices low, with no near-term recovery expected by Fitch. Gerdau aims to cut costs by BRL1.5 billion by 2025 compared to 2023, including BRL1 billion from Brazil through streamlined maintenance and operational leverage, and BRL500 million from North America and Specialty Steel through productivity improvements. Fitch expects a 5% reduction in cost of goods sold by 2025.

FCF Generation: Fitch forecasts Gerdau's EBITDA to drop to BRL10.8 billion in 2024 and then rise to

BRL10.9 billion in 2025. Gerdau is halfway through a BRL11.9 billion investment program (2021-2026) to optimize assets and boost steel capacity by 1.4 million tons. Capital intensity rose to 6% of revenue (2021-2023) and is projected by Fitch to reach nearly 9% through 2026. About 63% of the investment targets Brazil, focusing on sustainable mining, rolling mills, and forestry expansions, with additional investments in North America and Specialty Steel. FCF margin is expected at 1% (2024-2026).

North American Cash Flow: Gerdau's ratings are not constrained by a country ceiling. Fitch estimates Gerda's EBITDA from operations in the U.S. can comfortably cover its consolidated hard-currency interest expense by more than 6x over the next 12 months; therefore, per Fitch's "Non-Financial Corporates Exceeding the Country Ceiling Rating Criteria," its applicable country ceiling is that of the US (AAA).

Derivation Summary

Gerdau's diversified operational footprint, significant operating cash flows from its assets abroad, mainly in the U.S., and flexible business model that allows it to better withstand economic and commodity cycles, are all key competitive advantages. Gerdau has also met creditors' demands proactively by selling assets twice in the last seven years, for total considerations of BRL7.4 billion, and raising equity three times with most of the proceeds reallocated to repay debt in the last 15 years.

Gerdau's vertical integration as a dominant competitor in the scrap market and downstream multiproduct distribution network compares with Companhia Siderurgica Nacional's (CSN; BB/Stable) and Usinas Siderurgicas de Minas Gerais S.A.'s (Usiminas; BB/Stable) integrated business profile. CSN and Usiminas are highly exposed to the local steel industry in Brazil, particularly to the flat steel sector, and have large iron ore exports.

Among the three Brazilian steel producers, Gerdau has consistently maintained the strongest balance sheet, made efforts to improve its capital structure through assets sales or equity issuances, and kept the most manageable debt amortization schedule. Gerdau's Fitch adjusted gross debt (BRL10.9 billion at YE 2023) is higher than Usiminas's (BRL5.9 billion), but lower than CSN's (BRL52.1 billion). Gerdau's gross and net leverage of 0.8x and 0.4x, at YE 2023, and Usiminas's 4.0x and -0.1x are lower than CSN's at 4.4x and 3.2x.

Unlike the operating profile of blast furnace led North American peer's U.S. Steel (BB/RWP) or Cleveland-Cliffs (BB-/Stable), Gerdau's operation is more similar to Nucor (A-/Stable), Steel Dynamics (BBB+/Stable), and, Commercial Metals Company (BB+/Positive), with Electric Arc Furnace facilities, scrap collection markets presence, long steel predominance and U.S. operations. Gerdau has a larger global production capacity (15.6 million tonnes of crude steel), but lower in the U.S. than that of Steel Dynamics (14 million tonnes) and Commercial Metals (10 million tonnes), as well as smaller capacity than Nucor (29 million tonnes).

Gerdau has obtained lower profitability in 2023 with EBITDA/tonne of USD240 than Commercial Metals (USD300 in North America), Steel Dynamics (USD285/tonne) or Nucor (USD 320/tonne). However, Gerdau has posted the second highest last three-year average EBITDA margin of the group with 24.9%, behind that of Nucor (25.9%) but higher than those of Steel Dynamics (23.3%) and Commercial Metals

(15.1%).

Gerdau is more geographically diversified across the Americas compared with Commercial Metals U.S. and Poland operations or Steel Dynamics' and Nucor's sole North American focus. Gerdau's leverage metrics (last three-year average gross and net leverage of 0.7x and 0.4x) compare similarly to those of Commercial Metals (1.0x and 0.5x), Steel Dynamics (0.7x and 0.3x) and Nucor (0.7x and 0.2x).

Key Assumptions

- Brazil's domestic steel volumes fall by 1% in 2024, grow by 2% in 2025 and by 6% in 2026;
- Brazilian export steel volumes fall by 10% in 2024, and by 3% in 2025 and in 2026;
- North America steel volumes increase by 2% in 2024, by 1% in 2025 and 1% in 2026;
- South America steel volumes fall by 10% in 2024, increase by 4% in 2025 and by 3% in 2026;
- Specialty steel volumes grow by 5% in 2024, by 4% in 2025 and by 3% in 2026;
- Combined EBITDA/tonne reaches USD 190 in 2024, USD 186 in 2025 and USD 181 in 2026;
- Capex at BRL6.0 billion in 2024, in 2025 and in 2026;
- Dividends at BRL1.7 billion in 2024, BRL1.7 billion in 2025 and BRL1.9 billion in 2026;
- An exchange rate of BRL5.4/USD1.00 at YE 2024, and BRL5.3/USD1.00 in average foreign exchange rate for the remainder of the forecast horizon.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

- Further geographic diversification in low risk operating environments;
- Larger contribution to cash flows from higher value-added products;
- Sustained adjusted total debt/EBITDA below 1.5x and/or adjusted net debt/EBITDA below 0.5x.

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

- Sustained adjusted total debt/EBITDA above 2.5x and/or adjusted net debt/EBITDA above 1.5x;
- Persistent negative FCF;
- EBITDA margins below 12% on a sustained basis.

Liquidity and Debt Structure

Boosted Liquidity: Gerdau consistently has kept a conservative financial strategy resulting in the

company terming out its debt and holding enough cash to cover upcoming maturities. The company had BRL6.6 billion of cash and marketable securities as of June 30, 2024. Gerdau's cash holdings are sufficient to cover amortizations until 2027. Its debt profile has an average term of 7.2 years.

Approximately 61% of Gerdau's cash was held in US dollars as of June 2024. In addition to the cash it holds, Gerdau has a USD875 million global credit revolving facility till 2027, none of which has been used as of June 30, 2024.

Furthermore, a favorable tax dispute ruling allowed Gerdau to add cash availability of BRL1.77 billion in previously held judicial tax provisions. These provisions were related to the exclusion of ICMS (state VAT) from the calculation basis for PIS and Cofins (Social Integration Program and Contribution for Social Security Financing). Moreover, Gerdau will file a request with the Brazilian Federal Revenue Service to obtain a tax credit arising from overpayment or incorrect payment of BRL786 million.

Gerdau has strong access to local and international debt markets, as well as Brazilian and international banks. Gerdau's debt consists of cross-border issuances (65%), local Brazilian debentures (18%) and working capital lines (17%). Approximately 65% of the company's debt is US dollar denominated.

Issuer Profile

Gerdau S.A. is a leading manufacturer of long steel in the Americas and has a strong presence in special steel in the U.S. and Brazil. It also produces flat steel and has iron ore operations in Brazil, and a strong presence in the scrap market.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

MACROECONOMIC ASSUMPTIONS AND SECTOR FORECASTS

[Click here](#) to access Fitch's latest quarterly Global Corporates Macro and Sector Forecasts data file which aggregates key data points used in our credit analysis. Fitch's macroeconomic forecasts, commodity price assumptions, default rate forecasts, sector key performance indicators and sector-level forecasts are among the data items included.

ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

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Rating Actions

ENTITY/DEBT	RATING	RECOVERY	PRIOR
Gerdau Trade Inc.			
• senior unsecured	LT BBB	Affirmed	BBB
Gerdau S.A.	LT IDR BBB	Affirmed	BBB
	LC LT IDR BBB	Affirmed	BBB
	Natl LT AAA(bra)	Affirmed	AAA(bra)
• senior	LT BBB	Affirmed	BBB

ENTITY/DEBT	RATING	RECOVERY	PRIOR
unsecured			
GUSAP III LP			
• senior unsecured ^{LT}	BBB	Affirmed	BBB

RATINGS KEY OUTLOOK WATCH

POSITIVE	⊕	◇
NEGATIVE	⊖	◇
EVOLVING	◊	◆
STABLE	⊙	

Applicable Criteria

[Corporate Rating Criteria \(pub.03 Nov 2023\) \(including rating assumption sensitivity\)](#)

[Corporate Recovery Ratings and Instrument Ratings Criteria \(pub.02 Aug 2024\) \(including rating assumption sensitivity\)](#)

[National Scale Rating Criteria \(pub.22 Dec 2020\)](#)

[Sector Navigators – Addendum to the Corporate Rating Criteria \(pub.21 Jun 2024\)](#)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 [\(1\)](#)

Additional Disclosures

[Solicitation Status](#)

Endorsement Status

Gerda S.A. EU Endorsed, UK Endorsed

Gerda Trade Inc. EU Endorsed, UK Endorsed

GUSAP III LP EU Endorsed, UK Endorsed

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