

GIS 1Q21 EARNINGS CONFERENCE CALL
April 26, 2021 @ 10am CT

Melanie Carpenter: Ok, ladies and gentlemen, we're going to get started. Let me say good day and welcome all of you to GIS' first quarter 2021 conference call.

Joining us today is GIS' Chief Operating Officer, Mr. Jorge Rada, GIS' Chief Financial Officer, Mr. Saúl Castañeda, and GIS' Investor Relations Manager, Mr. David Sandoval. Please be advised that this call is for investors and analysts only.

During the call, they will be discussing GIS' performance as per the earnings release that we issued on Thursday. If you did not receive the report, it is available on their website at gis.com.mx in the Investor Relations section and we encourage you to follow along with the on-screen presentation.

All lines are on mute to prevent any background noise, there is going to be a question and answer session after the speakers' opening remarks, and I will give you instructions at that time so you can ask a question.

Let me just remind you that forward-looking statements may be made during this call. Those are based on information that is currently available and is subject to change due to a variety of factors. For more details and a complete disclaimer, please refer to the earnings release. Also, all figures that are going to be discussed today are in US dollars, unless otherwise noted.

It is now my pleasure to introduce the GIS' team, and we are going to begin with Mr. Saúl Castañeda, the CFO to begin the conference call, so please Saúl...

Saúl Castañeda: Thank you very much Melanie, and thank you all for joining us today.
On behalf of GIS, we hope that you and your families are in good health.
First quarter results proved a solid trend of sustainable and profitable growth across all GIS business units, strengthening the recovery seen during the second half of 2020.

Our consolidated EBITDA was 42 million, a 35% increase year over year with a strong 17% margin. This operating performance allows us to reach our third consecutive quarter of EBITDA growth.

Higher volumes, a better mix, and important cost savings through our operational efficiency initiatives, offset most of the broad upswing in commodity prices.

Regarding sales performance, Draxton continues recovering volumes across all regions where it has operations. In the first quarter of 2021, Draxton sales rose 18% year-over-year.

Vitromex attained its highest sales level for a quarter since 1Q17, due to the dynamic remodeling sector in Mexico, successful product launches and better mix.

Cinsa top line grew 43% year-over year, measured in Mexican pesos, achieving the highest first-quarter sales in its history, mainly driven by significant growth on exports and e-commerce channel.

On a consolidated basis, GIS' revenue was the highest since second quarter 2018, this level validates the dynamism in all regions where we operate. For the upcoming quarters we remain optimistic about the pace of the consolidated top line.

Regarding Debt, we should highlight there are no relevant maturities until 2023 and our debt average life is 4 years, as a result of the refinancing strategy carried out during 2019, thus we are benefiting from our financial flexibility to evaluate strategic alternatives to increase shareholder value.

GIS maintained its solid financial position, with a Net Debt-to-EBITDA ratio of 1.6 times, which is even lower than last quarter's ratio. We continue to expect that by the end of the second quarter of the year it will be below 1.4 times.

I will now pass the presentation over to Jorge Rada.

Jorge Rada:

Thank you Saúl and good morning to everyone. I hope you and your families are staying safe and are in good health.

In the first quarter of the year, we continued to see revenue growth and margin expansion in our three business units. Improvement across regions where GIS operates was highly influenced by economic recovery, government stimuli and vaccination rollout. We have been able to capitalize on this recovery due to our flexibility to serve higher demand of our products and improving profitability through efficiency programs in all plants.

During the first quarter of the year, China's economy continued to recover from the pandemic. The world's second largest economy grew more than 18% year-over-year, setting a new record for the country. This growth supports 2021 GDP forecast of nearly 12% increase over the fourth quarter of 2019.

Even though the pandemic continued to be top of mind of the US government, during the first quarter of 2021, the economic recovery gained speed, supported by the stimulus programs which increase consumer disposable income, also the low interest rates, and the optimism generated by the steady vaccination rollout. The US economy has almost returned to pre-COVID levels during the first quarter.

Europe's economic rebound was slowed down by a new pandemic wave and lockdowns in several European countries. We expect a gradual recovery throughout 2021 coming back to pre-pandemic levels by the end of the year.

Mexico's growth forecast for 2021 has been revised upward, due to a positive impact on demand, fueled by US performance during the quarter, Analysts expect that Mexico might return to Pre-Covid levels by the first half of 2022.

During the quarter, the economic rebound seen around the world has led to a significant increase in commodities' prices; however, at GIS, due to successful negotiations with our suppliers, higher volumes and efficiency programs implemented across all our business units, we were able to offset this impact.

The Purchasing Managers Index shows how economic activity is accelerating, mainly in the US and Europe. This is a positive outlook for GIS and the regions in which we operate.

I will now turn to the automotive industry, in North America, sales continued to improve with a 4% year-over-year increase. The industry is expected to recover from the semiconductors shortage in the coming quarters, and OEMs have announced that they will reduce normal summer shutdowns in order to increase the levels of inventory.

Even though production and vehicle sales continue to recover at a slower pace than in other regions, some governments in Europe have offered incentives and stimulus packages to promote electric vehicle sales. Volumes in Europe continue to benefit from the export of vehicles to different countries, a trend that has been seen since the fourth quarter of 2020.

In China, we saw a 70% increase in vehicle production year-over-year, and a 76% increase in sales since last year's first quarter volumes were hardly hit by the lockdowns at the start of the pandemic in China. The strong demand for vehicles this year was mainly due to a positive economic outlook, government subsidies, and optimal control of the pandemic.

Moving on to Draxton's performance, during the first quarter, our global foundry volume increased 12% year-over-year, due to the recovery in the main markets where we operate and the ramp-up of recently launched programs. For North America the growth was 9% as demand in the US spiked, and it was 14% for our units in Europe and Asia, mainly driven by the Chinese market.

We recorded global sales of 175 million dollars, an 18% increase year-over-year, due to higher volumes and also indexation of scrap iron prices, which continued their upward trend from last year.

The global semiconductor shortage continues, and is affecting the automotive industry, among others. So far, we've only been affected by a 2% production loss across the three regions where we operate, and we are expecting general industry recovery during the year, as the regular summer shutdowns will be shortened.

EBITDA closed at 35 million dollars, 8% higher than in the first quarter of 2020, for a 20% EBITDA-margin. The majority of the one-time metal lag generated by the indexation formulas of our prices based on scrap iron indices was offset thanks to the higher volume, negotiations with suppliers and the efficiency and

productivity improvement programs we have been implementing since before the pandemic. As scrap iron prices stabilize in the next few months, we expect no further major impacts from indexation.

During the first quarter of 2021, Draxton won new contracts for 30 thousand tons, most of them in the brakes system, which confirms our highly compatible portfolio with Hybrid and Electric vehicles. With this, our products under development have increased to 300, which considering the natural phase out of some existing programs will represent a 10% sales increase vs pre-pandemic levels.

We are expecting growth in Mexico in the next coming years due to the USMCA. We will be prepared to take advantage of new opportunities, especially in braking components, continuing to launch products fully compatible with Electric vehicles.

Moving on to Vitromex. Revenue rose 21% year-over-year, attaining the highest level of sales for a quarter since the first quarter of 2017.

Vitromex's team has been working on consolidating the Operations System through which the business was able to reduce production costs by 5%, as well as improving the "Sales and Operations Planning" process, which allowed the business to capture incremental volumes.

Efficient management of Working Capital generated 119 million pesos in cash flow in the first quarter of 2021.

Our implemented strategies resulted in an EBITDA of 128 million pesos, and a 13% EBITDA margin, which is the highest margin over the last 10 years.

In Mexico, we continue to see an extraordinary level of demand, which we were able to capitalize on during the quarter thanks to our better market position. This was derived from the new strategies focusing on proximity to clients and to improving our service levels.

We have received the first orders from key customers in the US, and in South America the opening of markets has allowed us to win new customers.

Regarding Cinsa, the business set a sales record for a first quarter with total sales of 480 million pesos, and it continues with a steady upward trend.

Sales growth was mainly driven by exports, which grew five times for the US and two times for other countries. We also saw an important recovery on two of our main channels, traditional and modern, and we achieved exponential growth in the e-commerce channel.

Higher volumes, a better product mix and prices aligned with each segment, as well as efficiency measures across plants, enabled Cinsa to offset the majority of the price increase of cold rolled steel, and thus we reached an EBITDA margin of 10% during the quarter.

This concludes my remarks for today. Thank you for your attention.

Melanie, please begin the Q&A session...

Melanie Carpenter: Thank you. At this time, we're going to open the floor for your questions. So first, we are going to take the questions from the conference call and then we will take questions from the chat.

If you would like to ask a question via Webinar, please press the little hand icon, once your line is opened, a popup window will appear to confirm if you'd like to activate your audio, click on it and please we ask you to mention your name and affiliation. If you are connected via phone, please press the star key, followed by nine. Once your phone line is opened, press the star key, followed by six to begin speaking, also please just say your name and affiliation before you ask your question.

If you're connected via the Webcast there is a "Question mark" button, we ask you to click on that and type your question into the box that appears and click "Send".

We're just going to pause a moment so that people can enter their questions.

Again, if you see, on the webinar there's a little hand icon if you could press on that. Then, that will enable you to ask a question. We're just going to pause another moment...

Saúl Castañeda: Melanie, I think we have our first one from **Alejandro Azar**.

Melanie Carpenter: Alejandro, can you enable your audio, please?

Alejandro Azar: Yes. Hi, good morning. Good morning Melanie, Saúl, Jorge. Thank you for taking my questions and congratulations on the results.

First, on Draxton. I was having problems with the zoom, I don't know if you commented on the semiconductor shortage, I understand that the OEMs have announced that they are going to use the summer shutdowns but what are you seeing? Did you see any troubles in the first quarter? Are you seeing something in April? Because there is too much noise around the industry, about plants shutdowns and your results are really strong so I just want to understand if you are seeing something for the second quarter or maybe the third.

That will be my first one on Draxton and the second one on Draxton would be, with your incremental volumes, with your incremental contracts, how is your mix by component going to change? Are you estimating that your percentage of sales from brakes are going to grow, or what are you seeing on that front?

Jorge Rada: Yes. Thank you Alejandro, nice to talk to you.

The first question. It's a little bit difficult to predict at this moment what is going to happen in the next months, however, I can tell you that in the first quarter, we were not hardly hit yet.

We are seeing that still the problem exists and we have read a lot of articles and a lot of experts are talking about it, that maybe we'll continue for the rest of the year.

The impact is not going to be tremendous as our sources are telling us, we think that it's going to be between 2%-3% of the total output worldwide. So, it sounds a little bit too much noise in the industry but volumes don't seem to be affected by more than 3%.

The customers also, the OEMs are privileging or focusing on not stopping the products that are highly sold in the market, more preferred by the customers and fortunately Draxton is

participating in the high volume platforms, especially in the US, where we are more dedicated to SUVs and pickup trucks. That is another reason why we might not be affected as much as other platforms or other suppliers that are focusing on other kinds of vehicles; this is what we have seen today.

We are following up almost on a daily basis what is happening in the industry and we continue to see that the situation will continue for the rest of the year, but as I said at the beginning, the impact seems to be no more than 2%-3% of the total output globally.

The second question was about...

Alejandro Azar: If the breakdown of your sales is going to change drastically.

Jorge Rada: Not drastically but definitely we have a trend that started a few years ago, in which we are selling or gaining a lot of market share on the brakes components.

At the moment, we are more or less about 50% of our global output related to breaks and this is going to continue growing probably to 60% in the next years.

At the moment, Draxton's portfolio is very close to 80% compatible with hybrid and electric vehicles, that's why we are very optimistic that if we continue with this kind of trend and activities, commercially we will be a strong participant in the electrification of the industry.

Alejandro Azar: Jorge, one more question or two more on Draxton. Are you currently manufacturing EV components or are you in the phase of designing them? Do you already have a contract to manufacture a differential case...

Jorge Rada: Sure. For example, in Europe, we are producing differential cases for two electric platforms through a Tier 1 customer. We are casting them and we are machining them. We have implemented a team that is fully dedicated to differential cases signed in machining, we are trying to be the leader in the market for this kind of components for the electrification.

In addition to that, we are already producing other components for electric vehicles that are also part of the power train that is

called the stator carrier. The stator is part of the motor, actually the electric motor, and we are producing already some components in Europe. Remember that the electrification is going faster in Europe, that's why I mentioned more Europe than North America. That's the way it is, if we want to focus more on electrification, it will start in China and then continue together with Europe and at the end, it will come to the US, and we expect that when this trend reaches the US, we will also be taking advantage of this trend. But definitely we are participating, not only in brakes, but also in other components.

I can tell you that also for the heavy trucks, we recently were awarded a program that is going to be for a truck and it's related to the protection of the batteries and this is made of iron. There is a lot of weight that is going to be in one truck, so this is another area of opportunity that we are exploring, diversifying also for heavy trucks in electric power trains for trucks so definitely we are taking advantage of this electrification trend and gaining a lot of new contracts and we are fully prepared to take advantage of it.

Alejandro Azar: Thank you, and one more, if I may Jorge, on Draxton. Out of your total operations, is there a percentage where you don't pass the cost of metal to the client? I remember you had some clients in Europe or in China, where you didn't do the pass-through.

Jorge Rada: That is a small percentage of customers in China only, where the prices are set with a reference price and then you continue for several years. But all the new programs, when you get the new product or even the replacement of existing one, you have the possibility to adjust the prices to the new levels of the market so almost 90% or more than 80% of the volume in Draxton is... no, more than 90 because China is only 10% of the total output of Draxton and only a portion of China is not fully hedged or indexed, so it's a very small portion

Alejandro Azar: Excellent, Jorge. Thank you very much, and just one in Vitromex, you mentioned the key customers in the US. Is there any way you can give us some color on what are you targeting in terms of sales when you when you bring in those customers only from the US.

Jorge Rada: You mean in terms of...

Alejandro Azar: Export sales in Vitromex

Jorge Rada: Yes. What we are targeting... in the past, we were selling several million square meters a year. Our target this year is going to be much more modest, we are trying to reach levels of one to two million square meters per year. In the long term, we are seeing or targeting the US market as a main market for us, that's why the whole organization in Vitromex is committed to regain the market share that we used to have in the US and we are implementing a new strategy where we are developing new customers, customers that are being very successful in the market and we are developing new products for them. It takes time because these customers are asking us for new designs that we are validating with them, once we get the validation, we will start the ramp up and we would like to see this ramp up start in the second half of this year.

Alejandro Azar: Perfect. Thank you Jorge and again, congratulations on the results.

Jorge Rada: Thank you, Alejandro. Nice talking to you.

Melanie Carpenter: Next we're going to take a question from the webinar. We have a question from **Carlos Alcaraz** from Apache Analysis and he is asking:

First, due to the shortage of semiconductors and its effect on the automotive industry, do you consider that it will significantly affect the obtaining of new contracts during the rest of the year?

Second, given the good first quarter cash flow results will the target level of leverage remain 1.4 times, or has that been adjusted?

Jorge Rada: You want to talk about the leverage first, Saúl?

Saúl Castañeda: Sure, let me answer that, Jorge. Thank you for the question, it is a good one. We should remind that in this formula, measured at the second quarter of 2021, we are excluding the loss at EBITDA level of around 10 million dollars, so we are going to have a great number of EBITDA last twelve months from third quarter 2020 to second quarter 21.

On the other hand, this target of 1.4 has already considered the cash flow performance of first quarter 2021 that was excellent and it is important to remind also that in April, we had a dividend

payment of around \$32 million dollars. This 1.4 target is also including that so it's our best number, so far, including the dividend and the cash flow projected.

I don't know if you want to take the other part, Jorge.

Jorge Rada: Sure, regarding the semiconductor shortage, we are not seeing any impact on new programs.

What we are seeing is just a small on releases or forecasts on existing programs that are already in production, but we haven't seen any kind of delay on decision making from our customers on new programs.

I think I understood the question was related to new programs. If I didn't understand it correctly, please correct me.

Saúl Castañeda: I understood like you, it was mainly thinking about obtaining new contracts, Jorge.

Jorge Rada: We haven't seen any kind of impact and actually, we are very active this year on commercial negotiation with customers and we expect a very good year in terms of new programs negotiation with customers.

Melanie Carpenter: Excellent, so I just want to remind everyone, since we have the gentlemen here, we want to make sure that everyone who wants to ask a question has the opportunity to do so, if you are connected via the webinar, there's a hand icon, if you're via telephone we just ask you to press star, followed by nine that will alert us that you want to ask a question.

I will just pause one more moment. Okay, it appears we have a follow up from **Alejandro Azar**.

Alejandro Azar: Hello again guys. Just one more question, more on the strategic front. With your new balance sheet, how should we think about Draxton? You mentioned growing on EVs, growing on the caliper bracket front... are you seeing a consolidation in the upcoming years? Maybe you're looking out to vertical integrating towards brake discs?

Jorge Rada:

Very good question Alejandro. Well, with the industry that is a relatively mature, I'm talking about the foundry industry actually, related to the products we make.

At the moment, we don't have any firm or any opportunity available that we are pursuing but definitely this kind of industries, we know it from the history, normally go through a consolidation phase or trend.

I would say that based on all the skills that we have developed in the last years to integrate companies that we have acquired in the past five years and growing also organically by adding machining and additional lines like in Evercast, we are very well prepared to participate in the consolidation of this industry.

Definitely, this is one of the strategic lines that we are following. At the moment, I can tell you there is nothing on hand. Definitely, in terms of investments, one of the strategies is to continue growing on machining and machining requires additional capacity. Not many of the iron foundries have been able to add successfully machining operations, we think that by machining our products, we are going to be adding more value to the customers and we continue to grow and gain more loyalty from the customers, because once they give you the machining, the contract is going to stay there for longer times.

As I said before, we have developed a complete team dedicated to machining worldwide from Europe, from Spain, we are supporting all the regions in terms of technology for machining so that's another trend that we are following.

Also, we are expanding operations in several places, we are improving our efficiency in the plants and in Mexico, for example, with marginal investments, we are going to be able to absorb higher demand and eventually we might be in the need to add additional foundry capacity. Once we have decided that in the future, we will announce it properly and in time, but we see that, with the USMCA, most probably, there will be a need to add capacity Mexico.

Alejandro Azar:

Great, Jorge. Thank you again and nice talking to you also.

Jorge Rada:

Thank you, Alejandro

Melanie Carpenter: Ladies and gentlemen, it doesn't appear that we have any more questions so I'll turn it back to management for some closing remarks.

Saúl Castañeda: Thank you Melanie and thank you once again for your interest in GIS. Please don't hesitate to contact us if you have further questions and we hope you stay healthy and safe. Have a nice day.

Jorge Rada: Thank you very much.

Melanie Carpenter: Thank you everyone That concludes the event and we'll see you next quarter.

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