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RASSINICPO.MX - Q4 2015 RASSINI SAB de CV Earnings Call

EVENT DATE/TIME: FEBRUARY 24, 2016 / 3:00PM GMT



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PRESENTATION

Operator

Good morning and welcome to Rassini's Earnings Conference Call for Fourth Quarter and Full Year of 2015. At this time, all participants are in a listen-only mode. Following prepared remarks, there will be a question-and-answer session. As a reminder, this conference is being recorded for replay purposes.

Please note that the accompanying presentation for today's conference call is available for download on the Company's website at rassini.com. Alternatively, you can e-mail Rassini at rassini.com and a member of the Rassini Investor Relations team will send you a copy of the presentation deck as soon as possible.

With that, I will now turn the call over to Francisco Freyre, Assistant Vice President of Investor Relations and Finance for Rassini. Please go ahead, sir.

Francisco Freyre - *Rassini SAB de CV - Assistant VP of IR & Finance*

Thank you, operator. Good morning and thank you for joining us today. With me on the call is Juan Pablo Sanchez, our CFO. At Rassini, we are pleased to deliver another strong year in 2015, during which we made substantial progress in many areas and achieved record sales, EBITDA and net income.

Please refer to slide 2 of the presentation. For the year, sales increased by 8.4% to MXN12,897 million and EBITDA grew 36.5% to MXN2,141 million. Net income before taxes, extraordinary income and minority interest increased 38.7% year-over-year to MXN1,154 million. The fourth quarter was particularly strong with sales increase of 12%, 31% EBITDA growth, and 77% increase in net income before taxes, extraordinary income and minority interest over the fourth quarter of 2014.

Consolidated net income for 2015 reached MXN884 million. This represents an increase of MXN20 million over the MXN864 million reported in 2014. However it should be noted that, as we have mentioned, in 2014, Rassini received an extraordinary non-recurring income for the sale of



certain royalty rights, and excluding that one-time gain, the increase in net income year-over-year would have been 46%, which we consider to be more representative of the earning power of the Company.

Our continued emphasis on quality and technological innovation coupled with the strong demand across the industry allowed us to gain market share within our primary market, NAFTA. We gained share not only within existing markets but in a new market for us, the North American heavy truck suspension market. We took a major step towards meeting this growing demand when we completed MXN378 million investment in our Puebla, Mexico brake plant. The expanded facility came online in April of 2015 and has helped us to maintain flexibility and to balance our product mix.

Our commitment to quality was demonstrated last August when we received Daimler Trucks North America's coveted 2014 Masters of Quality Award in our first year as a supplier for this truck manufacturer. And in September, rating agencies recognized our progress in entering new markets, growing sales and controlling costs as Moody's upgraded Rassini's corporate credit rating from Ba3 to Ba2 and Fitch rating revised Rassini's outlook from stable to positive.

We continue to benefit from ongoing growth in the North American automotive industry, which is linked to the positive macro-economic factors as shown on the slide 4 of the presentation; higher housing starts, lower unemployment rates and decreased fuel costs, as well as attractive financing conditions to buy vehicles.

On slide 5, the seasonally adjusted annualized rate of US light vehicle sales grew throughout 2015 reaching 17.5 million units during January of 2016. Production of light vehicles in North America reached 17.5 million units in 2015 and December inventories closed at a level of 61 days' supply, the same level as against last year and close to the industry ideal of 60 days' supply.

As we have noted in the past, IHS forecasts that total production in North America is estimated to reach 18.2 million units in 2016, an increase of 4% compared to 2015. Their outlook for outlying years has been tempered somewhat and they are now back to forecasting 1% growth in 2017 as well as 2018. Underlying conditions include pent-up demand, aging of the car fleet, an accessible lending environment, healthy inventory levels in the industry, low gas prices, unemployment and continued, albeit modest, economic growth remain favorable and we are encouraged by this outlook.

Operating conditions within the Brazilian market remains challenging, but we have taken several measures to control cost and align operations with the local environment. We continue throughout the year to strengthen our relationship with OEMs as an essential preferred business partner and we believe the market presents us with a strong foundation for growth in 2016 and beyond.

Moving on to our financial highlights and results on slide 7, we reported excellent financial performance in 2015, extending the five-year trend in which compounded annual growth rate of sales has been 11% and of EBITDA has been 15%. As seen on slide 8, sales in our main market, NAFTA, remains robust. NAFTA now accounts for 89% of sales, with Brazil representing 11% and NAFTA also contributes essentially all of our EBITDA with Brazil contributing only 3%.

Slide 9 shows that within NAFTA, sales in our suspension division rose 22%, while sales in our brakes division rose 20% contributing to an overall 21% sales growth in our NAFTA business. EBITDA in this region grew by 55% for the year.

Macroeconomic factors in Brazil including low consumer confidence and higher cost for electricity, gas, labor and sales taxes greatly affected our business there. Our program of action has minimized the impact and we continue to adjust our cost structure and the scale of our business to reflect conditions there.

As shown on slide 10, we reported consolidated net income of MXN1,154 million before taxes, extraordinary income and minority interest, 39% increase over last year. Net income increased 2% to MXN884 million from MXN864 million in 2014 and earnings per share was MXN2.76. I would like to reiterate that excluding the extraordinary income during 2014, net income would have increased by 46%.



Slide 11 details consolidated cash flow. We noted previously that EBITDA increased by 37% from MXN1,568 million in 2014 to MXN2,141 million in 2015. Net operating cash flow more than doubled, growing 103% to MXN2,362 million in 2015, reflecting improved operations and working capital management.

As part of our commitment to deliver increasing value to our shareholders, we made a dividend payment in July of MXN250 million and we concluded the year with a substantial cash balance of MXN1,223 million, which is almost 45% higher compared with 2014. As our operations deliver increased cash flow, we are using these resources to pay down debt and invest in our operations.

As shown on slide 12, our consolidated debt balance has increased (sic - see press release, "declined") to \$154.5 million as of December 31, 2015 from \$201 million at the end of the same period in 2014. In US dollar terms, our cash balance as of December 2015 is \$71 million and our net debt is \$83 million.

Our improved financial position is reflected in our improved level of ratios as seen on slide 13. As of December 31, 2015, net debt to EBITDA was 0.7 times, while the interest coverage ratio was 7.5 times EBITDA to net interest expense.

Our 2016 outlook remains positive as we continue to see strong demand and progress in new markets such as in North American Heavy Commercial Trucks. With our commitment to quality and to reinforcing our partnership with top manufacturers, we believe we are well positioned to deliver additional value to shareholders now and into the future.

With that, Juan Pablo and I would be happy to open up the call for questions. Operator?

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions) Nicolas Prado, Newfoundland Capital.

Luis Adaime - Newfoundland Capital - Analyst

This is actually Luis Adaime from Newfoundland. Couple of questions. First, for your improvement in working capital, especially on the receivable side, to what do you attribute that? And was that due to any specific program or effort at the Company or was it specific to one client? Where is the working capital improvement coming from?

And two, you're generating a lot of cash, you've delevered. Where do you see usage of cash going forward? And maybe an idea for the investment plan for 2016?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

Okay. Regarding your first question, we improved over working capital as you said in the line of working in accounts receivables. Since several years ago, the Company, the way to finance the working capital needs of the Company is through factoring of account receivables. During the last year, we improved these kind of programs and that was reflected mainly in the last quarter of 2015. And this is one -- we can say that this one event and we will have our working capital stable in the future. Obviously, these facility depends on the volume and the accounts receivables generation.

Second, based on the generation of cash flow that you mentioned, the Company's strategy is to have these cash generation in order to look for potential growth for the company. This can be organic growth or look for other options. The Board of Directors of the Company review this very frequently and at appropriate time, if a decision is made, we will inform properly to the investors.



Luis Adaime - Newfoundland Capital - Analyst

Would you -- let's say, there are no opportunity for acquisitions, for M&A, would you go on that cash, what's the limit to the accumulation of cash would you say for the Company?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

The Company we try to keep at least a balance of MXN35 million to MXN40 million as cash balance and the other part would be used for, let's say, as I mentioned, for potential growth or maybe depending on decision of The Board of Directors and the stockholders decision, maybe it could be some potential dividend like we made in the last year. But that is decision that will be reviewed and analyzed and defined in the future by the proper level of authority of the Company.

Luis Adaime - Newfoundland Capital - Analyst

Okay. And, any idea for the investment plan in dollars, CapEx in dollars for 2016?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

Yes. At this point in time, as we have mentioned in the past, we have mainly maintenance CapEx. This maintenance CapEx represents around 3% to sales. However, we are exploring additional business for the Company that in the future could trigger that we make some additional investments. But this depend on the contracts that we have in hand. The Company has followed the policy to carry out CapEx investment for growth only if we have on hand the contracts with the customers.

Luis Adaime - Newfoundland Capital - Analyst

And just one final question on the heavy truck suspension business. What's the potential there in terms of volumes or extra sales for the Company in 2016? How much sales do you expect from this business in 2016 and where do you think the potential is?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

For 2016, we are expecting sales around \$20 million, \$25 million and the potential is that we are trying to get a market share in this kind of market of 25%. That would represent maybe sales in the future around [\$50 million to \$60 million] per year.

Operator

Mauricio Santos, GBM.

Mauricio Santos - GBM - Analyst

I was wondering could you touch on the volume performance in 2015. The thing is that, if I use the average FX throughout the year, it seems that there is little growth in sales in US dollar terms. So I was wondering -- I would like to get some details on the volumes side.



Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

Okay. Regarding the volume, we see the NAFTA suspension business show an increase in volume of 6% compare 2015 against 2014. Then we have an increase in volume of, as I mentioned, 6%. In the case of Brazil, you know that the situation in Brazil is very complicate. We have a reduction of 38% as we have mentioned in the past. And in the case of the brake business, we have an increase. If we talk about tones, we have an increase of almost 4%.

Then the volume, it's okay, is above the average of the industry in all of our business except for Brazil. The point that you have to take into consideration is the matter of the steel pass-through agreements that we have with customers. As we have explained in the past, we received the support of all of our customers regarding the price of the raw material.

Raw material is the most important, let's say, material that we use in the production of our products and the agreements that we have means that if there is a decrease in the price of the raw material, we have to adjust the selling price. And if we compare 2014 to 2015, there was a reduction in the cost of the steel by \$140 per ton and that was reflected in the line of raw material in the cost and also in the line of sales.

Operator

Valentin Mendoza, Banorte.

Valentin Mendoza - *Banorte - Analyst*

Congratulations on the result. I have a couple of questions. The first one is, as far as I understand, Rassini has been investing during 2015 in research and development. Should we expect this 2% compared to sales that in the past used to be the investment of the Company in this field to grow in the future? Looking forward, to improve the product line, both of breaks business and suspensions?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

The answer is yes. As you know, the name of the game in this industry is invest in technology and innovation. That represents for the Company improvements in the process engineering, in the product engineering and with that, we are able to get additional business, increase our market share in all the lines and also increase our profitability. Then the answer is yes, we will be investing in this kind of things in the future in order to improve our products and improve the service quality et cetera to our customers.

Valentin Mendoza - *Banorte - Analyst*

Okay. And as a percentage of -- in terms of the sales, would you say, as I mentioned, it used to be 2%. Would you see that this percentage will increase?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

Yes, we would say that we will be in the range of 3% to 4% to sales.

Valentin Mendoza - *Banorte - Analyst*

Okay. Thank you very much. And also, could you please give us some color on the -- you already mentioned 6% year-on-year growth on the NAFTA suspension volume growth. However, during the last quarter of the year, the growth was larger than that. Would you please elaborate a little bit further on what happened, that was related to light vehicles or heavy trucks? What was the main driver for this volume growth in the last quarter in NAFTA suspension?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

We can say that this growth was according with a trend of the automotive industry. As you know, the last year, there was a significant improvement in the line of light trucks and that was the result -- that was reflected in the last quarter of 2015 and based on orders from our customers, we are looking, we are seeing this first quarter of 2016 in the same mode as the last quarter of 2015.

Valentin Mendoza - *Banorte - Analyst*

Thank you very much, Juan Pablo. A couple of questions if I may. The next one is, do you expect the negative EBITDA that Brazilian operation had in the last quarter to continue in the first half of 2016?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

No, we don't foresee that in the future. The last quarter of 2015, as you have read in the news, was a terrible quarter for the Brazilian economy. There was a lot of stops by the customers in the productions et cetera, et cetera that reduced substantially the volume.

Of the structure, we will say that we have made the adjustment in the structure to run the business according with the expected volume by the, (inaudible). That is one of the authorities that deliver projections in Brazil. Then we see that was an extraordinary quarter, the fourth quarter, because the deeper recession in Brazil.

We are looking very closely over operations in Brazil in order to adjust the structure as soon as possible and considering any change in the trend of the industry. As you said, last quarter was terrible. However, we end the full year of the Brazilian operation with positive EBITDA that was around 4% to 5% to sales and that is the most important thing that we are keeping our operation [about] breakeven.

Valentin Mendoza - *Banorte - Analyst*

Thank you very much, Juan Pablo. And finally, would you give us some color what do you foresee for revenues growth in this year as well as for the EBITDA margin in 2016?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

In that, talking about margins, we don't see any major change of that. Regarding volume, as Francisco mentioned during the explanation, we are seeing a growth in the industry of 4% for the year 2016. And we are expecting an increase in our volume, talking about tones, of around 5% to 8%. Then, with that, you can easily factorize in your model, the expected sales and EBITDA.

Operator

Hector Vazquez, GBM.

Hector Vazquez - *GBM - Analyst*

Congratulations for the results. My question has just been answered. I was going to answer it to last year, about the guidance of 2016. Thank you very much.

Operator

Jose Vazquez, GBM.

Jose Vazquez - GBM - Analyst

In your press release, you mentioned that given the efficiency that you have achieved and the lower cost in steel, you have reached a new breakeven point for both suspensions and [for air and break]. So if you could explain a little more on that to see how has been the trend on cost and what would we expect for the year?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

As we have mentioned in the past, we have a breakeven point in our operations that we can be profitable if we run the business with 30% to 35% optimization of the facilities. And that, we have keep that and we have keep that because the improvements in the productivities, in the process, et cetera, et cetera. And then, that's our goal and that's why we have kept from several years ago. Regarding the guidance, the only thing that I want to mention is the same thing that we are expecting our growth above the growth presented by the industry or forecasted by AHS.

Operator

Jean Bruny, BBVA.

Jean Bruny - BBVA - Analyst

Most of my question have been answered so far. I just have one doubt and it's regarding the tax rate you've paid in the last quarter. I think it was about 60%. Just if you can break it down or explain why it was [wide during] this quarter and what do we expect to pay in tax rate in 2016?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

The point is that, during the last quarter of 2015, we have an increase in the line of deferred taxes that is a non-cash item. The effect there is that we amortize tax losses that we have and we have to do that because we were very profitable in our operations in North America. And for the future, as you calculate the effective tax rate that we have in last four quarter, we are talking about 27% to 30% on the income before taxes and we think that, that would be the rate that we have in the coming months and years.

Operator

(Operator Instructions) Guillermo Diego, Santander.

Guillermo Diego - Santander - Analyst

Just a couple of questions. What's the EBITDA breakdown and what's the run rate of depreciation? We saw high grade, from 2% versus fixed asset to almost 4%. So what would be the expectation going forward for the run rate of depreciation? And maybe the second one, you already mentioned, the tax rate and the taxes, but how much is left right from the fiscal, from the tax bank consolidation. So, we're expecting that 27% to 30% tax rate and how much rate from the tax consolidation bank.

Just confirming, you are expecting the next year CapEx around \$25 million, right. And the next one for free cash flow generation and the working capital, the thing that you make on factoring, how much from the MXN520 million were on this factoring strategy and on which the factoring rate that you get from this place?



Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

Sorry, we didn't hear you very clearly your questions. Could you repeat, please?

Guillermo Diego - *Santander - Analyst*

Yes, sure. If you want, the first one is on the EBITDA breakdown. What would be the expected depreciation run rate because we saw (multiple speakers) from [2% to 4%]?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

In that, we have two effects. The first effect is that in April we finished the expansion of the foundry plan for the break business that we mentioned in the past that we were investing in order to supply business on hand from our customers that we will be supplying during 2016 and 2017, et cetera, et cetera. That was part of the increase in the depreciation line.

The second is, as you mentioned, we have 4% depreciation to sales. This is an increase of 1% is related first to this thing that I already mentioned, the expansion of foundry, the foundry facility in Puebla. And the second one is also because this is a mathematical effect because of the reduction of the sales price because of the (inaudible) that I already explained. Also the sales is reduced because of that and that makes [that the percent] has increased. That's a mathematical effect also.

Guillermo Diego - *Santander - Analyst*

Okay. Second question was on taxes, we saw [MXN140 million]. But also we saw MXN240 million on cash taxes, right. So you already said you're expecting 27% to 30% tax rate, but how much is left from the tax consolidation bank. How much should we expect from here to 2018 in terms of [USD millions or Mexican Pesos]?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

In that, we have, let's say -- it depends on the volumes, et cetera, et cetera, how much we will be using. We can say that in this program we are using around 75% to 80%. That means if there is an increase in the accounts receivables, we can increase this facility using the product we have available.

Guillermo Diego - *Santander - Analyst*

All right. And just reviewing CapEx expected for the next year, our maintenance CapEx should be around \$25 million, right?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

Where do you get that number, sorry? The maintenance CapEx, yes, the answer is we will keep the same level that we have in the past. We don't see any major changes if we talk about maintenance CapEx.

Guillermo Diego - Santander - Analyst

Okay. And the last one is just on working capital, on the accounts receivable that you already mentioned, we saw a drop in days right from [41 to 34 or 50]. How much of that change in working capital, accounts receivable, MXN520 million, were obtained under the factoring study that you mentioned?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

We can say that we get around \$10 million is the amount.

Guillermo Diego - Santander - Analyst

Okay. And what was the factoring rate, the cost that you got on those \$10 million?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

The cost that we have is LIBOR plus 2.5.

Operator

(Operator Instructions) Munehiro Nakagawa, Daiwa.

Munehiro Nakagawa - Daiwa - Analyst

Firstly, could you give us new contract you've got during last year?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

Yes, we are in -- the contracts that we get during the year mainly was the heavy trucks contract that we mentioned during the presentation. Also we get a business for Mercedes-Benz, that also is mentioned in the report that we present. Those are the contracts, the main contracts that we have. But as I mentioned, we are also working to get additional business and probably in the near future we will inform to all the investors in the proper way the business that we will be getting.

Munehiro Nakagawa - Daiwa - Analyst

Okay, great. And the second question is performance of your brake business, and it seems your revenue of brake business in NAFTA was down in US dollar terms in the fourth quarter. Could you give us a color what's behind the weakness?

Juan Pablo Sanchez - Rassini SAB de CV - CFO

It's -- the brake business is reflecting the situation of the automotive industry. In the case of the brake business, we have in the full year we have an increase in the volume sales of 3% if we talk about tons. If we talk about pieces, you will see a decrease, but the rationale on that is that we sell more pieces for light trucks than for cars. In the case of the brake business, we sell breaks for cars and light trucks. That means that we are selling products with higher weight, that's why we have this increase in tons terms. However in pieces we see an decrease because in the past we were selling more for cars than the light trucks.

Munehiro Nakagawa - *Daiwa - Analyst*

Okay. Great. And about your guidance for this year, you mentioned you expect your volume to grow by 5% to 7%, is that right?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

Yes, that's right.

Munehiro Nakagawa - *Daiwa - Analyst*

So this means, as steel price has been coming down over the past year, your revenue growth will be weaker than this 5% to 8%, probably flat?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

It will depend on the assumption that you take into consideration for the price of the steel. We are seeing a decrease in the prices of the commodities like the steel, but that will depend if the steel price reduction is in a size that kind of set the volume increase, maybe you will see that but with a growth that we are seeing of 5% to 8% volume, we see that we will be positive in the line of sales.

Munehiro Nakagawa - *Daiwa - Analyst*

Okay. Assuming the steel price to remain at the current level?

Juan Pablo Sanchez - *Rassini SAB de CV - CFO*

Yes.

Operator

And it appears that there are no further questions. At this time, Mr. Freyre, I'd like to turn the conference back to you for any additional remarks.

Francisco Freyre - *Rassini SAB de CV - Assistant VP of IR & Finance*

Thank you so much, operator. I want to thank everybody for joining us today. And we look forward to updating you again with the results of the first quarter of 2016. In the meantime, please don't hesitate to contact us with any questions you might have.

Operator

And that does conclude today's conference. Thank you for your participation.



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