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PRESENTATION

Operator

Good morning and welcome to GCC's First Quarter Earnings Call for 2021. Before we begin, I would like to remind you that this call is being recorded and all participants will be in listen-only mode. Please also note a slide presentation will accompany GCC's earnings results webcast. The link is available on the company's website at gcc.com, within the Investor Relations section. There will be an opportunity for you to ask questions at the end of today's presentation.

I will now turn over the call to Ricardo Martinez, Head of Investor Relations. Ricardo?

Ricardo Martínez

Thank you, operator. Good morning everyone and thank you for joining our earnings call. With me on today's call are Enrique Escalante, our Chief Executive Officer and Luis Carlos Arias, GCC's Chief Financial Officer.

As a reminder before we begin, today's discussion contains forward-looking statements about the Company's future business and financial performance. These are based on management's current expectations and are subject to risks and uncertainties. You can find more information about risks, uncertainties and other factors that could affect our operating results in our most recent filings with the Mexican Stock Exchange. It is important to note that these statements include expectations and assumptions related to the impact of the COVID-19 pandemic. As seen on slide 2, our forward-looking statement provides information on risk factors including COVID-19 that could affect our financial results. In particular, there is significant uncertainty about the duration and contemplated impact of the pandemic. This means GCC's results could change at any time, and the impact of COVID-19 on the Company's business results and outlook is a best estimate based on information available as of today. Let me now turn the call over to Enrique.

Enrique Escalante

Thank you, Ricardo, and good morning everyone. Let me open today´s call by emphasizing that GCC had another favorable quarter, highlighting the fact that our backlog and the overall market trends are encouraging in both countries. It is reassuring to see the economy emerging from tough and uncertain times into brighter months ahead. GCC´s results reflect a positive momentum in our industry and show early signs that we are entering into a new phase of the industry´s cycle with a stronger demand for most of our products.

At GCC we always prefer to have a positive, objective and future-oriented perspective; therefore, we are turning the page from COVID-19-related challenges to focus our efforts in producing and supplying the pent-up demand that lies ahead. We will neither drop our guard in our health and safety protocols nor leave behind all the lessons learned during the hardest times of the pandemic. We gained a great amount of knowledge – financially, operationally, and with our teammates. We learned that no matter how well GCC is running, there is always room for improvement, for innovation and to adapt. You never know how strong a company is, until you're truly tested. GCC is stepping into the 2021 construction season even stronger.

Let me now briefly discuss our key highlights from our performance this quarter as well as market conditions. Luis Carlos will follow with GCC's results and financial position. He will then turn the call back to me for comments regarding full-year guidance and closing remarks. Finally, we will take your questions.

Turning to slide 4. Given the seasonality of our business, GCC´s first quarter volumes are not a strong indicator of the Company's full-year shipments. Historically first quarter volumes represent less than 20% of the total. If we compare the last two years' cement and ready-mix first quarter volumes against third quarter volumes, there is a one to three ratio. Yet our full year backlog remains encouraging in every sector where we operate. It is important to mention that during the first quarter 2020 COVID economic effects were not present yet and shipments were strong. Nonetheless, we are very pleased with the results delivered during this first quarter, in which we increased EBITDA, Free Cash Flow and EBITDA margin.

Consolidated sales were only impacted by tough comps in oil well cement volumes, although overall performance and market conditions were much better than we originally expected.

Turning to slide 5, to comment on U.S. operations and market trends. We experienced challenging weather conditions in the markets where we participate coupled with gas and electricity outages in Texas. Nevertheless, construction cement volumes increased 6% while total cement volumes declined 8% due to oil well cement comparison.

We are bidding new projects and shipping at strong levels across GCC´s markets presence. Several U.S. competitors suffered from cement shortages, coupled with some markets gains above expectations, so we are taking advantage of our spare capacity to supplement this increased demand. Therefore, we will fire up all of Chihuahua's cement plant kilns to produce and export construction and oil well cement. We are able to supply the additional demand thanks to our connected system of cement plants with terminals, one of our main competitive advantages. In response to the expected and stronger demand in this construction season, every kiln at GCC will be up and running to produce cement. This hasn't happened since about fifteen years.

On slide 6, regarding U.S. segments, I would like to comment:

- **Infrastructure**. Projects are running at a steady pace and several more are in the pipeline. Considering recent news, this market has an upside in the short and mid-term. In respect to the latest economic stimulus package, we welcome the federal government's efforts to support the U.S. recovery. Currently we have limited information on the specifics of the infrastructure bill for roads and bridges. But from what is known, it might allocate an incremental funding of 30% to 50% over Fast Act levels. In our opinion, this could extend the cement cycle and have a significant impact in cement consumption in the coming years. By our estimates, an infra bill increase in actual cement demand would take at least 12 to 18 months after the proposal is fully approved.Besides the additional and steady funding that this bill could generate, the construction industry would benefit indirectly. The bill could:

  - Reduce uncertainty while injecting money where it is needed.
  - Support consumer confidence by distributing unemployment checks,
  - Boost infrastructure spending with aid to state and local governments

- **Residential.** The pandemic has resulted in a home buying surge with a race for residences with more home-office space and yards. A limited housing supply, favorable demographics and low interest rates are supporting positive trends. Recent research shows that the annual housing supply and demand imbalance will not be rectified before 2022. Given the Fed´s comments to keep interest rates low for an extended period, the residential outlook remains strong in the mid-term.

- **Non-residential and commercial sector. -** As we have previously stated, this sector showed mixed demand again this quarter. There were projects which were favored by the pandemic while others were put on hold. On the positive side, the U.S. economy recovery and government's stimulus funds will support this market as well. For example, small business grants can protect against real estate vacancies. Other grants that are part of the stimulus package could unlock projects that were halted.

Moving to slide 8, on oil well cement demand in the Permian Basin. In spite of an increase in oil prices, some of our competitors are exiting the West Texas market to reallocate their production to supply the temporary shortage of construction cement in the Texas triangle. The aforementioned is a result of an equipment failure at a competitor cement plant as well as the effects of the deep freeze in mid-February. Therefore, we foresee an opportunity to increase market share in this segment which will be captured by Odessa and Chihuahua cement plants.

The price increase of US$8 per short ton came into effect in all of our markets starting in January with a few markets sliding into April. As a result, cement prices increased 3% against the first quarter of last year. We did not experience any significant pushback given the tight supply and the high utilization levels in the cement industry. We do not expect that this issue will be resolved in the short term, so the price environment and dynamics will remain favorable in the markets where we operate.

It is important to note, this price increase only applies to current GCC's committed volumes to customers. Any additional volumes or any new customer agreement, will be subject to different pricing depending on market conditions at the time.

All in all, U.S. performance and backlog remains positive and encouraging. Projects are starting sooner and we're seeing some customers request more cement. In the foreseeable future, our cement business looks promising across the board. For practical purposes, our system is sold out.

Turning to our Mexico operations on slide 9. The state of Chihuahua continues a V-shaped recovery. Sales in Mexico's division increased by almost 8% in the first quarter, mainly driven by continued demand from industrial warehouse construction, mining & self-construction projects as well as the reactivation of several public works projects in the city of Juarez. 2021 began with momentum and a strong demand for cement and ready mix. Once again, we leveraged our Construred state-wide retail store network to supply a solid demand of bagged cement. At the same time, our strategically located ready mix operations were able to better serve our customers against competitors. Despite being impacted by the deep freeze event in February as well, cement volumes rose 6%, and ready-mix volumes increased 8% in the quarter.

Economic fundamentals in the State of Chihuahua are primarily driven by private investment. Growth is strongly tied to the U.S. economy and its recovery, as well as the state of Chihuahua is an important part of the manufacturing supply chain. We are satisfied with the results achieved in this region in terms of both volumes and prices. Market trends remain positive.

Let me now turn the call over to Luis Carlos to discuss the quarter's financial results, then I will return for comments regarding our full-year guidance and closing remarks.

Luis Carlos Arias

Thank you, Enrique, and good morning, everyone. Turning to slide 11. As noted in our quarterly financial statements released yesterday, for the first quarter, consolidated net sales decreased by 2%. During Q1, we saw a sharp increase in construction cement volumes in both countries and ready mix in Mexico. These gains were offset by a hard comparison in oil well cement and a decline of 33% in U.S. ready-mix volumes - which translates to only 7,000m^3 less.

On slide 12, cost of sales as a percentage of revenues decreased 2.2 points to 74.4% in the quarter, mainly reflecting favorable production expenses and better prices in both countries, as well as the continuation of the cost and expense reduction plan. SG&A expenses as a percentage of sales decreased 0.7 percentage points in the quarter to 11.3%. This was mainly due the continuation of the cost and expense reduction plan as well.

As a result, as we illustrate on slide 13, EBITDA increased 9% in the quarter while the EBITDA margin was 27.7%. This is an increase of 2.7 percentage points. We are highly focused on continuing to increase profitability on a yearly basis. This year will be challenging because our results will have to compensate for US$14 million of cost and expenses that were saved last year. As a reminder, in 2020 we deployed and successfully executed a comprehensive plan to reduce cost and expenses which totaled US$24 million. This year, we expect to maintain US$10 million in savings as we believe we've found the sweet spot between short- and long-term profitability without compromise to our operations, employees' safety or taking unnecessary risks.

Turning to slide 14, net financial expenses totaled US$5 million due to a positive foreign exchange effect on GCC´s cash position during the first quarter in 2020, partially offset by lower debt balance and lower interest rates on the variable portion of GCC´s debt. As a result, earnings per share and consolidated net income decreased 7% to US$15 million so far in 2021.

Moving to our cash generation on slide 15, free cash flow was US$18 million in the first quarter 2021, compared to US$11 million in 2020. This translates into a free cash flow conversion rate around 36% in the first quarter. This was mainly driven by increased EBITDA generation after operating leases, decreased working capital requirements and maintenance CapEx, as well as lower cash taxes and interest expenses. I would like to point out GCC's improvement in controlling payables, receivables, and inventories. Based on the last twelve months of sales, as of year-end, we reduced days in net working capital from 59 to 47 - a total reduction of 12 days.

Turning to our balance sheet, we ended the quarter with US$557 million in cash and equivalents. Our net debt to EBITDA ratio dropped to 0.22x at the end of March. Thus, we continue to be in an advantageous and solid financial position, having one of the healthiest balance sheets in our industry.

The rating agencies are recognizing our operating performance and solid financial results by raising our credit rating to triple B minus with a stable outlook. I am pleased to highlight that GCC has reached investment grade rating for the first time in history. The rating upgrade came from both agencies - Fitch and S&P Global Ratings.

With that, I will now hand the call to Enrique to discuss the guidance for the year ahead and to share his closing remarks.

Enrique Escalante

Turning to slide 17. Consistent with what we have said, we have a professional team fully dedicated and actively looking for growth opportunities both organic or inorganic. The latter mainly focused on cement plants that could be plugged into our system, while increasing presence in existing markets and/or expanding to adjacent markets where synergies can be generated. On this matter, I want to reiterate that we will maintain our prudent capital allocation strategy, growing in an orderly manner. We are focused on generating value while we invest strategically in our business. As stated before, if we do not find an appropriate asset that fits into our strict criteria, we will pay down debt to save on interest expenses.

I would like to take this opportunity to discuss our guidance for this year. We're expecting the positive momentum to continue as the underlying trends of GCC's business remain very solid, coupled by the temporary market supply shortage already discussed. Fortunately, our short-term visibility has improved substantially. While confirmed and projected COVID deceases are declining, U.S. government stimulus measures are boosting the economic recovery, and the vaccine rollouts have been a game changer in the U.S. Therefore, in the U.S. we expect GCC's cement volumes to increase 2% to 4% year-over-year. In the ready-mix business, some remarkable projects that concluded last year led us to record volumes and created a high base comparison. Thus, we expect volumes to decline between 10% to 13%, returning to historical levels while its base business remains stable.

In terms of prices, in light of the announcements we've already made, we anticipate a price increase in the 4% to 5% range in cement and ready mix.

In Mexico, we expect market dynamics to remain solid in the Chihuahua region, fueled by the strong correlation with the U.S. economy and its recovery. For 2021, we expect GCC's cement volumes to increase 2% to 4% and ready-mix volumes 3% to 5%, with price increases in the 2% to 3% range for cement and ready mix.

Regarding profitability, we expect 2021 EBITDA to increase between 4% to 9% year over year. We approximate our capital expenditures at US$75 million, with US$60 million allocated to maintenance expenses and US$15 million from last year which were carried over to the current year. As a result, Free Cash Flow conversion rate is going to reach above 60% and a net debt to EBITDA ratio would be negative

As a last comment, our official corporate name has changed from Grupo Cementos de Chihuahua to GCC. This new name unifies our brand in multiple countries, mirrors the stock ticker and reflects how the market best refer to us. It is cohesive with our recently renewed 2025 vision: *to be the best cement company in North America with the proper balance of people, profit and the planet.*

The best is yet to come and GCC is prepared for it.

With that, this concludes our prepared remarks. Let's now turn to your questions. Operator, please go ahead.

Operator

We will now be conducting a question-and-answer session. Our first question comes from the line of Adrian Huerta of JPMorgan. Please proceed with your questions.

Adrian Huerta

Hi, everyone. Thank you for taking my questions. First on margins. If we look at the implied EBITDA margin from the guidance that you have on volumes and prices, it seems like you're calling for margins to be flat and we saw margins already up almost three percentage points in the first quarter. If you can just shed some more color on what you see on margins.

The second question is just on working capital. We saw large improvements last year. How sustainable are those? In the conversion rate of free cash flow of more than 60%, are you expecting an investment on working capital, or working capital investments to go down a little bit?

Enrique Escalante

Thank you for your question, I'll refer it to Luis Carlos for the answer.

Luis Carlos Arias

Hi, Adrian.

From the EBITDA margin, as you may recall last year we had US$24 million of savings on cost and expense. As I said in my remarks, US$10 million is being replicated for this year. We'll have to absorb US$14 million of cost of those reductions that are not going to be replicated this year. That's the main reason.

In your second question, what we have done in terms of working capital optimization, we truly believe that it's sustainable for the long run. If you see our balance sheet, we are managing much better in the side of the payables. That's the main explanation on the optimization, and we are controlling very well the accounts receivable in both U.S. and Mexico.

You asked a third question, Adrian, or just those two?

Adrian Huerta

Thank you so much. Appreciate it.

Luis Carlos Arias

Thank you, Adrian.

Operator

Thank you. Our next questions come from the line of Nikolaj Lippmann with Morgan Stanley. Please proceed with your questions.

Nikolaj Lippman

Thank you very much for taking my questions. A couple of questions.

2021 looks like you're going to have very different trends between—you have strong housing, weak commercial. Can you address a little bit how you're seeing the infrastructure market in the different states or operating areas where you are operating, in the U.S. in particular? And also what kind of pricing trends you're seeing in these different operating areas in your official pricing increases, those kinds of things? That's sort of the first or second question if you will.

Then finally, if you can provide more insight into the oil well cement, the West Texan plant, how should we think about the recovery and what is happening there in terms of pricing? Thank you very much.

Enrique Escalante

Nikolaj, this is Enrique. Thank you very much for your questions.

If I understood your first question correctly, in terms of market segments in the U.S., I think that we're seeing—I mean basically in all of our regions, I mean, good projects across segments. Housing remains very strong in every market where we're participating.

As we mentioned, the commercial side, it's really a little bit weaker in the Central New Mexico area because last year there were several large projects there, that are not repeating. We're also seeing on the ready-mix side, in the Dakotas and Iowa, a little bit less of windmill projects.

However, I can say that there are still some more in the pipeline and in the bidding process. Those two segments may probably feel a little bit less of a decrease that is definitely being compensated by more infrastructure projects. That remains very strong in the field of bidding in several of our regions.

In terms of pricing, as I said, the price is being very well accepted mostly in every market. There's a little bit more of a pushback at the beginning of the year in the river region where we access with our Rapid City cement plant into the Minnesota markets, but I think that now the market's being more conscious that cement may be in short supply, it is getting more and more traction. We don't see any additional pushback. On the other hand, I think that if inflation continues to be as strong as we're seeing, there may be even an opportunity for a second price increase in specific markets, but that's still a little bit early in the year.

In terms of foreign world cement, we're being benefited by both. I mean, the recovery of the industry in the Permian Basin, as we have been saying, it's not going to be a very fast recovery, but it's indeed increasing faster than what we expected at the end of last year.

When you combine that with the fact that two cement competitors that were shipping oil well cement to the area announced that they are taking back those shipments to Central Texas and North Central Texas, well, that's given us a better opportunity to basically to have a sold-out plant in Odessa. If you remember, the plant was running with just one kiln basically all last year. Now, the plant is running with two kilns and it's going to be supplemented by kiln number two in Chihuahua that is firing up on May 1.

A very different outlook for us compared to last year, which as you know was the segment in which we suffered the most during the pandemic and the oil well cement crisis.

Nikolaj Lippman

Thank you very much. Congratulations, guys.

Enrique Escalante

Thank you, Nikolaj.

Operator

Our next questions come from the line of Alberto Valero with UBS. Please proceed with your questions.

Alberto Valerio

Thank you for taking my questions. Hi, Enrique and Luis Carlos.

Two quick ones on my side, a follow-up of Adrian's questions on guidance. You mentioned in your presentation that the first quarter is below the 20% of consolidated results for the year. And what we have here is that the past five years, the first quarter was close to 14% of the consolidated results on additional (phon) line. My question is, are you guys conservative on the guidance, or are you expecting some deceleration during the year?

My second one is about the M&A aspect. We know that there are two public assets for sale, one from Heidelberg in California and the other one from LafargeHolcim in Brazil. I suspect that Brazil is not an interest to you guys, but I would like to hear your thoughts about the California assets. And congrats on the results.

Enrique Escalante

Thank you for the questions, Alberto. Luis Carlos is going to take question number one and then I will comment on the M&A question.

Luis Carlos Arias

Thanks, Alberto.

We feel very comfortable with the guidance that we issued. And yes, we've had a very strong 1Q with very good increase in EBITDA margin. Never the less, it's going to be a long year and, as Enrique explained, we have a very good backlog. We feel very comfortable again on the cost and expense side. There's still nine more months of the year; so we feel comfortable with the guidance that we issued.

Enrique Escalante

Thank you. On the M&A question, Alberto, even though growth, as we've mentioned, is our top one priority. We don't find the California assets on the market as an attractive proposition for GCC. We think they are basically detached from our current network, and our strategy calls for, I mean, trying to find answers that can create synergies by the connectivity on our network. Those assets in California are not attractive from that perspective, so we have to pass on this opportunity.

Alberto Valerio

Okay. Very clear. Thank you very much.

Operator

Thank you. Our next question comes from the line of Froylan Mendez with JPMorgan. Please proceed with your questions.

Froylan Mendez

Hello, guys. Thank you so much for taking my question, and congrats on the strong results.

Enrique, could you just break down on your guidance for the U.S. on volumes? How much is embedded from growth in oil well and how much is from construction cement?

Secondly, we have seen a strong decline year-on-year in ready-mix volumes. The past two quarters, you did have enough to show up in the third quarter of last year. Was there supposed to be an impact on the size of your ready-mix operations given the asset swap? Thank you so much.

Enrique Escalante

Thank you, Froylan. I will take the second question first and then we'll see if Ricardo and Luis Carlos have those percentage growth for those sectors of oil well cement and the construction separated. I'm not sure we have them at this moment, but let me comment on the ready-mix side first.

We had a very, very strong year on ready-mix in the U.S. last year. Actually, it was a record year and basically fueled by very specific projects in the Dakotas and Iowa and Minnesota, of course. I mean, I have mentioned several times, several projects. I think five simultaneous projects of a windmill farms, which has, even though we have a lot of experience in that segment, in that area, we never saw so much activity. We don't think that's going to be obviously sustainable to keep doing so many projects simultaneously. That's one of the main reasons why ready-mix wasn't part of the planning.

The other important one is in the El Paso-Las Cruses region where we also had very significant projects like the runway, the Biggs Airforce Base, that I have been commenting on, which was a massive concrete project that obviously last year was very active at this time of the year. Those two segments are the ones that are making the difference.

As I mentioned in my remarks, we're basically returning to normal levels for those markets. It is not like the markets are suffering a big decrease. It's more a comparison with a very high base. The market seems robust and prices are also recognizing that demand level. The asset swap that we did with the Fort Smith plants in Arkansas and Oklahoma, for the ones that we acquired in Iowa and South Dakota, don't have any implication on this volume decrease. On the contrary, we think that we're going to be benefiting from that swap because of what we explained last year, which is volumes are similar, and, of course, now we have integrated those plants into our cement supply, so that's just a plus for us.

Luis Carlos, I don't know if you have any comments on the margins and the markets.

Luis Carlos Arias

Yes, Enrique. Hi, Froylan.

On the breakdown on the increase in volumes in the U.S., we have both increases in normal construction cement and oil well cement; and actually, oil well cement is increasing on a double-digit basis. But, yes, the growth comes from both construction and oil well.

Froylan Mendez

Okay. Very clear. Thank you so much, guys, and congrats again.

Enrique Escalante

Thank you, Froylan.

Operator

Our next questions come from the line of Alejandro Azar with GBM. Please proceed with your questions.

Alejandro Azar

Thank you. Good morning, Enrique, Luis Carlos, and Ricardo. I have three questions.

The first one is just to clarify on the oil well cement, right now you have three kilns working, right? Two in Odessa and one in Chihuahua. Also, if you could comment more on the competitive landscape in Texas you previously were mentioning. Is that in both types of cement: grey cement and oil well cement?

My second one is if you can remind us what's the percentage around your whole U.S operations that is yet to increase prices. I don't know if that happened in April, or it's going to happen in May, if you can give us more color on that front also, please.

Enrique Escalante

Thank you, Alejandro.

On the oil well cement first, yes, we have three kilns that are going to be supplying the Permian Basin. The two of the Odessa plant are already working. As I mentioned, the plant is working since several months with the two kilns. The one in Chihuahua, kiln number two, is going to start producing oil well cement now on May 1st. Those are the plans so that the rest of the year, we will have three kilns shipping oil well cement to the Permian Basin. If necessary, we could also produce oil well cement in the Tijeras plant in New Mexico. Although what we're seeing so far is that our plant may be also sold out for the year. Very, very promising view here.

In terms of the price increases, some of the customers in some of the regions the pricing was effected April 1 instead of January 1, like the majority of the cement. I don't have a breakdown here for you, Alejandro, in terms of what percentage of the customers or the volume. We will have to call you back with that information.

Alejandro Azar

Thank you, Enrique. And just one, if I may, one more. On capital allocation, several years ago, you mentioned about maybe expanding capacity in Chihuahua to provide the U.S. with imports. With your current capacity utilization, do you think that announcement might be really close?

Enrique Escalante

Good question, because as I mentioned also on my remarks today is that we have a couple of teams working both on M&A and on internal growth and expansion projects. Yes, we mentioned in the past the possibility of building a new kiln in the Chihuahua plant.

Now, given that the majority of the growth in the coming years, we're seeing it in North America, in the U.S. market, we're also reconsidering, and we also mentioned it before, the possibility of expanding and modernizing the capacity of the Odessa cement plant. Since it's ultimately part of our network, we could use that cement not only on oil well markets, but also on construction cement throughout our network. The two projects are under a very strict scrutiny in terms of what creates better long-term value for the Company. Most likely, yes, by the end of this year, we should have a decision of where to expand definitely. Our priority, I must say, is to find an M&A opportunity; but absent of that, it's very likely that we will proceed with an expansion.

Alejandro Azar

Excellent, Enrique, and now that you mentioned the Odessa back again, that new kiln, if it were to happen, it would have the same flexibility of the ones that we have today in terms of oil well cement and grey cement?

Enrique Escalante

Exactly, Alejandro. That's what I meant by saying that it will be obviously used through the connectivity of the whole network that we have where we can shift construction cement from that new kiln into our aviation market.

Alejandro Azar

Great. Thank you, Enrique, and congrats on the results.

Enrique Escalante

Thank you.

Operator

Thank you. There are no further questions at this time. I would like to turn the call back over to Management for any closing comments.

Ricardo Martínez

Once again thank you to everyone for your interest in GCC and for joining us today, we appreciate your questions this morning and look forward to talking with you again in the months ahead. This concludes our conference call. But our team is, of course, available for any follow up questions you may have. Goodbye and stay safe.

Operator

Thank you for your participation. This does conclude today's teleconference. You may disconnect your lines at this time. Have a great day.