

**Transcript of
Cementos Pacasmayo
First Quarter 2020 Earnings Conference Call
April 30, 2020**

Participants

Claudia Bustamante - Investor Relations Manager
Humberto Nadal - Chief Executive Officer
Manuel Ferreyros - Chief Financial Officer

Analysts

Andres Soto - Santander
Luis Pardo - Compass Group
Francisco Cerez - Scotiabank
Anoka Vivice - Remak Insurance

Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Cementos Pacasmayo's First Quarter 2020 Earnings Conference Call. At this time, all participants are in a listen-only mode. Please note that this call is being recorded. At the conclusion of our prepared remarks, we will conduct a question-and-answer session.

I would now like to introduce your host for today's call, Ms. Claudia Bustamante, Investor Relations Manager. Ms. Bustamante, you may begin.

Claudia Bustamante - Investor Relations Manager

Thank you. Joining me on the call today is Mr. Humberto Nadal, our Chief Executive Officer, and Mr. Manuel Ferreyros, our Chief Financial Officer. Mr. Nadal will [audio drops] strategic outlook. Mr. Ferreyros will then follow with additional commentary on our financial results. We'll then turn the call over to your questions.

Please note that this call will include certain forward-looking statements. These statements relate to expectations, beliefs, projections, trends and other matters that are not historical facts and are therefore subject to risks and uncertainties that might affect future events or results. Descriptions of these risks are set forth in the company's regulatory filings.

With that, I'd now like to turn the call over to Mr. Humberto Nadal.

Humberto Nadal - Chief Executive Officer

Thank you, Claudia. Welcome, everyone, to today's conference call.

We know that this is an extraordinary moment for everyone, and our hearts go really out to those affected by the new coronavirus. After a record start of the year with revenues growing close to 15% in January and February, everything came to a sudden stop when the Peruvian government, as most others around the world, declared a state of emergency starting March 16, 2020, intended to last two weeks at first and then extended it various times. The quarantine, as we speak, is currently set to end May 10, 2020 when a gradual return to activities, probably by sector, is expected.

Our priorities right now are, first and foremost, the health and safety of our employees and their families, and secondly, the financial wellbeing of the company. Although our operations are basically closed on the production side, our team has continued working from home to not only help all the safety measures and protocols in place to begin production as soon as legally possible, but also working towards the future. Although uncertain of the details, we are certain that we'll never be the same at least in the foreseeable future.

We have presented our operational resource plan to restart production with the safety of our employees as always as our top priority. We have used this opportunity to jump start some initiatives. We have already been considering such as more extensive work from home arrangement. We have been pleasantly surprised with the results, encouraging us to continue this working method per legal requirements as we believe it will bring about higher productivity levels, good wellbeing and a work-home balance for our employees.

On the financial side, we have made very significant budget adjustments to our organization, making it as lean as possible for its restart. We have also taken some sort of loans as a precautionary measure to ensure our liquidity during the most difficult times. We have always been very conservative on the financial side, and we believe this will pay off now.

I would also like to mention that we launched a voluntary initiative to take the quarantine time as vacation period for those that were not critical workers and to take the time off now. The vast majority of the company took it. Over 80% of our workers voluntarily agreed to this initiative. Besides the positive financial applications of this initiative, it clearly demonstrates the commitment of our employees and the alignment with the company's overall wellbeing.

Managing in these difficult times means more than ever taking care of each other and our families is a top priority. As we said, we're rolling out the HealthCheck mobile app to stay connected. This application will help us understand how the different infectious areas are impacting our daily lives and our own state of health in order to provide the necessary support and help manage the risk of the new coronavirus. The application allows us to see in real time how the virus is impacting our company and our family as well as the health and wellbeing of everyone. It also gives us the ability to manage our company's current operations.

Finally, I want to emphasize, that we remain focused on our long-term goals and are absolutely convinced that the cement industry in our country will come back. There's great potential for our industry even in the medium term, as we believe the government should prioritize investment in infrastructure to boost the economy. Our company is more ready than ever to capitalize on this potential and to try to make the best out of this situation adapting to a new reality.

I will now turn the discussion over to Manuel to go into more detail in our financial performance. Manuel?

Manuel Ferreyros - Chief Financial Officer

Thank you, Humberto. Good morning, everyone, and I hope all of you and your families are staying safe and healthy.

First quarter 2020 revenues were PEN 299.3 million, 4.4% lower than the same period of last year, mainly due to a halt in production and [indiscernible] after the government declared a state of emergency to prevent the spread of the new coronavirus. Gross profit decreased 17.9% in the first quarter of 2020 compared to the first quarter of 2019, mainly due to lower sales as well as higher costs derived from the sudden stop in regular production. However, as Humberto mentioned, revenues were performing outstandingly well during the first two months of the year, with growth of 14.4% compared to the same period 2019. Consolidated EBITDA reached PEN 72.3 million

in the first quarter of 2020, 22.8% lower than the same period of last year, mainly due to decreased sales and higher costs mentioned above.

Turning to operating expenses, administrative expenses for the first quarter 2020 remain in line with the first quarter 2019. Selling expenses in the first quarter of 2020 increased 31.7% compared to the first quarter 2019, mainly due to increased advertising and promotion during the first two months of the year as well as an increase in the provision for doubtful collection.

Moving on to the different segments. Cement, concrete and precast sales increased 4.3% during the first quarter of 2020 compared to the same period of 2019, mainly due to the halt in production. However, during the first two months of the year, sales of cement, concrete and block increased 14.7%, mainly due to the increased sales of cement and concrete for a construction-related project and self-construction. Gross margins decreased 5.9 percentage points in the first quarter of 2020 when compared to the same period of last year, mainly due to lower sales and the costs derived from the sudden stop in production.

Sales of cement decreased 9% in the first quarter of 2020 compared to the first quarter 2019, mainly due to the stop in production. However, during the first two months of the year, sales of cement increased 9.9% compared to the same period of the previous year, mainly due to the increase of demand in the northern of Peru, particularly from the construction spending on the self-construction segment. Gross margin decreased 5.6 percentage points, mainly due to lower sales and increased costs related to the halt of operations.

Concrete sales continued to perform extremely well this quarter, achieving an 18% growth despite the halt in sales since March 16th, mainly due to increased demand from small and medium-sized companies as well as other construction-related projects. Gross margin increased 0.8 percentage points this quarter compared to the same period of last year, mainly due to dilution of fixed costs and derived from higher sales.

Precast sales also increased 77.8% in the first quarter 2020 compared to the same period of last year, mainly due to high demand from construction-related projects. Gross margin increased 0.4 percentage points, mainly due to higher sales despite higher costs related to the halt in operations.

Quicklime sales decreased 5.5% compared to the first quarter of 2019, mainly due to increased demand. Gross margin increased 4.3 percentage points in the first quarter 2020 compared to the same period 2019.

Profit for the first period decreased 64.5 in the first quarter of 2019, primarily due to decreased revenues and higher costs from the halt in operations mentioned above.

Operator

Manuel's line has disconnected. Please standby. Manuel has rejoined.

Manuel Ferreyros - Chief Financial Officer

To summarize, despite our very strong start for the year, the quarter already showed the effect of the new coronavirus. As Humberto mentioned, we are focusing on maintaining the financial health of the company, adjusting all costs and at the same time preparing ourselves to restart operations as soon as legally possible and embrace the new reality.

I'll now turn back the call to Humberto for closing remarks.

Humberto Nadal - Chief Executive Officer

Thank you, Manuel. These are indeed unprecedented times. We are forced to think of new and innovative ways to function, both as individuals and in our business. We are more than ready for the challenge and we will continue to work hard to generate long-term value for our shareholders.

Can we now please, operator, open the call for questions?

Operator

[Operator instructions]. We'll take our first question from Andres Soto at Santander.

Q: Good morning, Humberto, Manuel, Claudia. I hope you and your families are doing well these days. I understand there is a plan to gradually reopen the Peruvian economy over the next few months, which includes construction as one of the sectors that should normalize first, especially for large-scale infrastructure projects. Could you please help us quantify the potential demand that we could see from these projects this year and how much of this could start showing up in your 2Q results? That would be my first question.

My second question is related to margin performance in Q1. I imagine this was not only due to lower capacity utilization but also increased transportation costs from the Piura to the Pacasmayo plant. Could you please help us break down these effects? I'm trying just to quantify the sensitivity of your EBITDA margin to lower volumes. Thank you.

Humberto Nadal - Chief Executive Officer

Hello, Andres. This is Humberto. Thank you for your question and I hope everybody is doing well in your home and your family. I'm going to take the first question and I will let Manuel take the second one.

At this point, it's not really clear what will happen starting Monday. I have seen many different plans as to how the government intends to open the economy. But, I will say that most of them include cement as an industry that will go in the first chunk of industries opening because indeed we are strategic to mines and everything. But, I think initially we're going to be focused fundamentally to service infrastructure. In our case, we're talking about the airport. In our case we're talking about the airport in Chiclayo which we have already been at work in the past and quite a few other projects that are going on.

When you talk about specific volumes, it's hard to tell because first of all you have to bear in mind that 65% of our sales goes to self-construction. That's going to take, I think, a little bit longer to restart, even though we have submitted protocols for all our hardware stores and even the construction sites. But, we have to wait and see what the government does. So, we are reopening at the beginning for the 25% to 30% of the market and it's all going to depend on how ready the building companies are to pick up the rhythm in the current future. So, you know me, I'm very conscious about predicting volumes, so at this point it's very hard to project until we actually open and see what are the construction companies' output [ph].

Manuel?

Manuel Ferreyros - Chief Financial Officer

Yes, related to how much could have been the EBITDA without cost of transportation, the clinker from Piura to Pacasmayo, it could have gone up to around 25.2% EBITDA margin. And [indiscernible] EBITDA margin, excluding the [indiscernible], could have been a little bit higher than 30%.

Q: Perfect. Thank you.

Operator

[Operator instructions]. We'll go next to Luis Pardo at Compass Group.

Q: Hi. Thanks for the call, and I hope you're all doing well. I understand there's a high level of uncertainty, as Humberto mentioned, but it is important to point that in all phases of the recovery, construction is mentioned. You have 95% market share so whether it's concrete demand or whatever it is, if something gets built in Northern Peru it is likely you would be involved. Am I correct?

Humberto Nadal - Chief Executive Officer

Yes, the answer is absolutely yes. I mean we have a very high market share like you mentioned and we are more than ready to start serving every single client. But I was trying to be cautious about it. The reason at which these projects are going to pick up and it has to do—you have to realize that construction companies have to redeploy the workers to the [indiscernible] or the case of airport in Chiclayo and so forth.

And also, I think the big push that's going to determine how fast we're going to come back is not only construction but it's self [ph] construction. If you see what's going on in Colombia, what's going on in the US, and what's going on in Spain, construction is one of the leading areas for the recovery for many reasons. One, because it's high in labor, it's a nice employment which is very important for countries. Point number two, construction sites are in the open and there's quite a significant social distance between workers if everyone is doing whatever they're supposed to be doing.

So, I think the protocols we have submitted to the government authorities are pretty clear that this is a segment that is very important for the recovery and we believe that the health risks are significantly low. So, yes, I'm very optimistic that we're going to be one of the ones with the fastest recovery, but as much as I'm optimistic, I mean I really cannot put color or a specific number to that at this point.

Q: That I completely understand, and I agree with. It would be difficult to do. The other question is for Manuel. With the cash that you have on hand, let's say Peru goes into a massive disaster and doesn't reopen, how much could you stand without operating with the cash you have today?

Manuel Ferreyros - Chief Financial Officer

In the worst case scenario, if nothing opens and we stay with total payroll and all the costs and etc., we have enough cash for the whole year.

Q: So with the cash that you have today, even if you don't sell one more bag of cement, you have cash until December?

Manuel Ferreyros - Chief Financial Officer

That's right. Yes.

Humberto Nadal - Chief Executive Officer

That's correct.

Q: Excellent. That's all. Thank you, guys, and I appreciate the time and hope you are all well.

Humberto Nadal - Chief Executive Officer

Same for you, Luis.

Operator

We'll go next to Francisco Cerez [ph] at Scotiabank.

Q: Hi, good morning, gentlemen. Thank you for the call. I hope you and your loved ones are doing fantastically well. It's great to hear you.

My question relates with import [indiscernible] prices. It seems that the overall production costs of clinker have declined due to energy prices. Is it fair to say that you will be seeking more volumes to rather than better prices once you can restart your operations? Thank you.

Manuel Ferreyros - Chief Financial Officer

Francisco, the costs of the clinker are going down because of costs of raw materials, some raw materials like coal are going down. Yes, we expect a lower cost in the future despite we have a stock of [indiscernible] in Piura for the Piura plant. So, we will restart the Piura plant in we expect three or four months. But the Pacasmayo plant, we'll start producing clinker immediately after the halt stops.

Q: Okay. And then on your overall pricing strategy, do you think that you will be limiting your potential price increases going forward and you will be [background noise] the highest possible volumes to the market rather than wishing [ph] for better prices?

Humberto Nadal - Chief Executive Officer

As we said at the beginning of our—first of all I should start by saying I hope you and your family are doing well. We have started January and February with a very strong increase in revenues, gross of 15%. One of the reasons for that wasn't only good volumes but also I think the price is at a good level. So, I think that good level should probably remain for the rest of the year because it's in a good territory.

Q: Okay. Perfect. Thank you. And lastly if I may, any concerns in any of your raw materials in terms of prolonged disruption? For instance, what about the [indiscernible] that you use [indiscernible] demand?

Humberto Nadal - Chief Executive Officer

Ever since we have the Nina [ph] phenomenon three or four years ago, we were very conservative in terms of stocks. I think Manuel mentioned, in terms of clinker, in terms of slack, in terms of [indiscernible], we have over six to eight months of supply in all of them so we are—that is if anything, probably from a cash [background noise] perspective, as Manuel mentioned, we are deferring the starting of some of our kilns maybe intending to optimize the working capital between cash and inventories. But, we are at ease with all our stocks.

Q: It makes perfect sense. Thanks again and thank you once again for the call. Take good care of yourself.

Humberto Nadal - Chief Executive Officer

Take good care. Thank you.

Operator

With no other questions holding, I'll turn the conference back to Mr. Nadal for any additional or closing comments.

Humberto Nadal - Chief Executive Officer

Thank you, operator. Thank you, all. These are indeed totally unprecedented but extremely difficult times. We remain optimistic. We remain committed to our employees, committed to our shareholders, committed to our communities, and mostly committed to our country. I'm convinced that some months from now hopefully we'll look back into this and focus on the lessons learned and not focus in what we lost, but in what we gained.

But, I'm absolutely convinced that the future is bright for us. If anything, we have suffered a small derail from that but we will come stronger, we will come wiser, and we will come more together as a country in the future. Thank you very much, all, and my best wishes everybody stays home with their loved ones. Thank you very much.

Operator

Ladies and gentlemen, that will conclude today's conference. Actually, we have a few other questions holding, gentlemen, if you would like to take them.

Humberto Nadal - Chief Executive Officer

Sure, go ahead.

Operator

Okay. We will take Anoka Vivice [ph] with Remak Insurance [ph].

Q: Hi, Humberto. Hi, Manuel, and Claudia. Thanks for taking my question. I just want to—I don't know if you can be more specific when you say that you have enough cash in your balance sheet for the rest of the year, even though in a worst case scenario production is off. And maybe you can give me some color regarding your [indiscernible] facilities in a scenario would you have to recognize your debt.

Humberto Nadal - Chief Executive Officer

Sure, let me take the question. I think Manuel was very clear. He said let's foresee a scenario, which I think is highly, highly improbable because I think we will be producing [indiscernible] in which if there's no production, in which there's no collection of our accounts receivable and we make no more extra budget cuts which we have already done, in that case, we have plenty cash on hand to survive the rest of the year. As you may understand, we're only May 1st tomorrow. So, if we see that the next two or three weeks that this is going to be a scenario, of course we will take additional measures so that cash in hand would last us significantly more than to the end of the year. I think that's more than enough color.

And also, you have to bear in mind that I mean all of our financing [indiscernible] have taken over the last six weeks is in a very long-term even though we have some bonds coming up in 2023 that are 13 [ph] and 9 years going forward. So, I think financially we are absolutely nothing to worry, no concern.

One more thing also, I mean we have a substantial stock of raw materials in terms of clinker [indiscernible] raw materials needed. So I was saying to one of our colleagues before, at some point we also want to make wise decisions in terms of how we turn that inventory to maximize the cash position.

I think that's more than enough color, and that should give you more than enough peace of mind from a financial and a cash management point of view we're in a fantastic position.

Q: Okay, thank you.

Operator

And that was our last question. So, today that will conclude the conference. We thank you for your participation. You may disconnect your phone line at this time and have a great day.