genial | Equity Research

GERDAU

4Q23 Review: A quarter to forget...

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Company

GGBR4 BZ Equity
Neutral

Price: R$ 21.40 (20-Feb-2024)
Target Price 12M: R$ 24.50

Main takeaways:

(i) Price suffering from macroeconomic factors; **(ii)** Sales volume also impacted, with Brazil surprising positively and North America BD with a reduction; **(iii)** Revenue shrinking, below estimate due to South America BD, with the mark-to-market for Argentina's currency devaluation affecting the result to a greater extent than we expected. Other business divisions reported revenues in line with projections; **(iv)** Consolidated costs increasing q/q, with Brazil's BD COGS/t coming in a little lower than we expected; **(v)** EBITDA in double-digit contraction, totally in line with our estimate; **(vi)** Net income in free fall due to anemic operations; **(vii)** Dividend distribution announced at R$0.10/share (-61.5% vs. Genial Est.), much lower than last quarter and what we had expected, even though we had already considered a reduction; **(viii)** We see the company with a **24E dividend yield of 6%**; **(ix)** We comment at the end of the report on the **points which**, in our opinion, **could bring upsides/downsides** in the coming months; **(x)** Trading at a **24E EV/EBITDA** of **4.1x** (in line with the historical average), we continue with a **NEUTRAL rating** and a **12M Target Price** of **R$24.50**, setting up an **upside of +14.49%**.

Gerdau released its 4Q23 results yesterday, February 20, after the market closed. The figures reported were very similar to those anticipated in our results preview (Gerdau: 4Q23 Preview), showing a quarter with **weakened performance across all business divisions**.

Table 1. Shipments Summary (4Q23 vs. Genial Est.)

(Thousand Tonnes - kt)	Reported	Genial Est.					
Summary (Shipments)	**4Q23**	**3Q23E**	**% R/E**	**3Q23**	**% q/q**	**4Q22**	**% y/y**
Brazil BD	1.269	1.175	**8,0%**	1.260	**0,7%**	1.150	**10,3%**
North America BD	885	870	**1,7%**	943	**-6,1%**	887	**-0,2%**
South America BD	243	259	**-6,3%**	290	**-16,1%**	290	**-16,2%**
Special Steel BD	339	324	**4,6%**	345	**-1,8%**	401	**-15,6%**

Source: Gerdau, Genial Investimentos

Table 2. Income Statement Summary (4Q23 vs. Genial Est.)

(R$ millions)	Reported	Genial Est.					
Income Statement	**4Q23**	**3Q23E**	**% R/E**	**3Q23**	**% q/q**	**4Q22**	**% y/y**
Net Revenue	14.716	16.614	**-5,3%**	17.063	**-13,8%**	17.964	**-18,1%**
Adjusted EBITDA	2.039	3.158	**1,3%**	3.349	**-39,1%**	3.630	**-43,8%**
Net Income	587	1.633	**-36,2%**	1.592	**-63,1%**	1.219	**-51,8%**

Source: Gerdau, Genial Investimentos

Revenue was **slightly below** our estimate, with a better-than-expected cost at Brazil BD, resulting in an **adjusted EBITDA perfectly in line**, consolidating a **reduction of -39% q/q** and **43% y/y**. **Net income** came in worse than our estimates (recovery of receivables/provisions and proportional result of affiliated companies), with a **retraction of -63% q/q** and **-51% y/y**.

CAPEX showed an acceleration to R$2bn (+36% q/q), fully in line with our bias towards higher levels of investment spending for 4Q23, already reported since October in all our reports on Gerdau. **Cash flow generation** (FCFE) **was close to what we expected**, if we remove from the account the R$474mn of CAPEX that has no cash flow effect. It is worth remembering that **Gerdau did not manage to stay within the guidance of R$5bn**, as we had expected (ahead of consensus), reaching a **total CAPEX of R$5.7bn** (-2% vs. Genial Est.).

Valuation and rating. Brazil's domestic market is struggling with rising imports of crude steel, mainly surplus production from China, with the penetration rate reaching 25.2% in December, as reported by Aço Brasil (IABr). Brazilian steelmakers are being forced to reduce domestic prices in order to compete on a national level, while also opting to redirect products with a lower quality mix in larger volumes than usual to the foreign market.

Looking at North America, high interest rates and a temporary economic slowdown in the consumption of durable goods and in the progress of non-residential construction work are affecting demand for steel. A few weeks ago, the Federal Reserve kept interest rates between 5.25% and 5.50%, which can be considered a high level compared to the historical average of monetary contractionary cycles in the US. In our view, the US economy seems to be largely driven by services rather than consumption of goods, which should result in a reduction in steel consumption y/y in 2024.

Although we have a considerable degree of confidence in this trend, we believe that the market has already priced in a double-digit contraction in the unit's EBITDA. We should remember that Gerdau's shares have fallen ~20% over the last 6M, with the consensus seeming very negative for the performance of North America BD in relation to the years 2024 and 2025 (perhaps too bearish...).

For us, there is still a forecast of a sustained reduction in volumes throughout 2024, together with the difficulty of sustaining high levels of metal spreads (which are well above average). The FED directors' current views emphasize the intention to keep rates high until inflation data suggests gentle progress towards the 2% target, which contradicts consensus forecasts for interest rate cuts during the course of 1H24. For these rate cuts to materialize, factors such as **(i)** beneficial inflation data, **(ii**) a loosening of payroll conditions and **(iii)** a reduction in economic activity in the services sector. All of these factors need to come into play, which doesn't seem likely, given the recent PPI and CPI indicators.

Contrary to the majority belief that prevailed until the last FOMC meeting, the possibility of a rate cut in March has reduced dramatically in recent weeks. Therefore, our forecast, established since the end of last year, is that interest rate cuts will not begin until at least June. This prolongs the period of high interest rates, which is disadvantageous for Gerdau. As we described in our preview report, which is attached below (Gerdau: 4Q23 Preview), we believe that in 2024 Gerdau will be squeezed from both sides.

we like the company's investment thesis, since the re-encounter of **bearish steel cycles** within more than one business unit **seems to cause less damage** to the result **today** than it did to the company before 2021 (there has been a notable change in profitability at Gerdau over the past 5 years). However, even identifying that this pressure on 24E EBITDA (R$10.4bn vs. R$13.5bn 2023) has already been priced in, we **don't see catalysts for the stock to rise in the short term**. We stress that even in the face of lower interest rates in the US in 2H24, there will still be a **delay** before the reduction takes effect in the real economy. Knowing the **short-term mentality of most of the institutional investors** we spoke to, we prefer to wait for a more opportune moment to change the company's rating. Trading at an **EV/EBITDA 24E** of **4.1x** (in line with the historical average), we continue to recommend a **NEUTRAL rating**, with a **12M Target Price of R$24.50**, setting up an **upside of +14.49%**.

Straight to the point...

Brazil: volume surprises positively, but price comes in below estimates. Despite the very weak scenario for domestic steelmakers, Gerdau managed to maintain a sales pace that we find interesting in 4Q23, with sequential stability (+0.7% q/q) that sounds more like a victory at this point. Total sales reached 1,269Kt (+8% vs. Genial Est.), marking growth of +10.3% y/y. This increase was mainly driven by the redirection of volume to other South American countries, with shipments reaching 305Kt (+38% t/t) to foreign markets (FM).

Despite this, the growing prevalence of Chinese steel in the Brazilian domestic market triggered price competition, leading to a drop in Brazil's BD realization to ~R$4,755/t (-7.6% vs. Genial Est.), a considerable reduction of -9.7% q/q, more than expected, also considering that the sales mix to the foreign market was lower value-added (despite the higher volume).

North America: weak seasonality combined with higher interest rates. Unlike Brazil, the business unit saw a sequential reduction in sales due to seasonal weakness and high interest rates in the US, totally in line with what we estimated in our preview report. Closing 4Q23 with a volume of 885kt (+1.7% vs. Genial Est.), configuring a drop of -6.1% q/q, we see a slowdown in the US economy reflected in lower demand for durable goods and a reduction in the pace of work in the non-residential construction segment.

On the price side, realization stood at R$6,697/t (-1.5% vs. Genial Est.), basically stable compared to last quarter, but with a reduction of -8.2% y/y, given a tighter market than in 2022, with more competitive price conditions.

South America: strong currency devaluation in Argentine operations. At first glance, South America's BD result shows a horrible performance in 4Q23. However, as we said in our preview report, we were expecting a mark-to-market in relation to the forced currency devaluation promoted by Javier Milei's current management in an attempt to reduce the gap between Argentina's official exchange rate and the so-called "Blue Chip Swap" (unofficial market exchange rate).

Therefore, the sharp drop seen in the unit's EBITDA (-73% q/q) was mainly due to a one-off, non-operational exchange rate effect. Even so, the macro turbulence in Argentina itself, which accounts for 30% of the business unit's operations, meant that volume was also reported as falling, reaching 243Kt (-6.3% vs. Genial Est.), a reduction of -16.1% q/q and 16.2% y/y.

Special Steel: **Lower volume in the US, partially offset by a recovery in Brazil**. As we pointed out some time ago, 4Q23 would be more challenging for the unit due to the United Auto Workers (UAW) strike, which ended in November and hit harder in the last quarter of the year, reducing the pace of orders from automakers to steel mills in the US. The 4Qs are already showing the effects of weakened seasonality, with the automakers' drive to rebuild inventories slowing down. This already not very encouraging dynamic was compounded by the more difficult situation regarding higher interest rates and the serious situation of the UAW.

However, in Brazil we're seeing the opposite trend, with an increase in demand for automobiles already seen in 4Q23, through the best December recorded in the last 4 years. We have a more favorable base scenario for 2024, in both light and heavy vehicles, with the end of the “hangover” experienced by the segment in relation to the anticipation of purchases of Euro 5 models in relation to the launch of Euro 6. However, just as we predicted, the improvement in Brazil did not compensate for the difficulty faced in the USA, with sales volume reaching 339Kt (+4.6% vs. Genial Est.), down -1.8% q/q and -15.6% y/y, despite being slightly above expectations.

4Q23 Review: In detail!

Price suffering from macroeconomic challenge. There was a drop in prices at the main operating units, with a sharper price decline (-9.7% q/q; -20.5% y/y) at Brazil BD to R$4,755/t (-7.6% vs. Genial Est.). We believe that this regression was influenced by two main reasons: **(i)** the adverse impact of robust exports from China on the domestic market, with greater competitiveness for market share and tighter commercial conditions. **(ii)** Faced with a domestic market without much appetite, coupled with weaker seasonality for civil construction, we analyze that there was a greater redirection of cheaper steel to the foreign market (FM), which although it helped volume, brought it down the realized price of the business division in Brazil.

Looking at the dynamics in North America BD, we observed that the business unit had a stable realized price q/q, in line with our estimate. Even with an appreciation of the average USD/BRL exchange rate vs. 3Q23, the price was recorded at R$6,697/t (-1.5% vs. Genial Est.), with a very slight sequential correction of -0.3% q/q, but an amplification of this downward movement on an annual basis (-8.2% y/y), reflecting more unfavorable conditions regarding competition within a tighter market, due to higher interest rates now vs. 1 year ago.

In other business units, South America BD was squeezed due to the Argentine macroeconomic scenario. As we mentioned, a policy of currency devaluation was forced by the economic team of the current president Javier Milei's administration, in order to bring the official exchange rate closer to the "Blue Chip Swap". This situation led to negative impacts for the Argentina segment, resulting in a realized price for South America of R$1,342/t (-71.4% vs. Genial Est.).

Although we were careful to reflect the mark-to-market within the realized price, estimating a reduction of -13% q/q, we still ended up underestimating the damage this situation did to the unit as a whole, considering that Argentina represents ~30% of the operation. The reduction ended up being -75.2% q/q and -75.1% y/y. It is worth mentioning that this effect should be one-off.

As for Special Steel, we saw a drop in the realized price of -5.1% q/q and -6.7% y/y to R$7,611 (-5.0% vs. Genial Est.). Although the automotive sector in Brazil has shown improvements, competition with Chinese steel is still hurting prices in the segment, in addition to a complicated demand scenario in 4Q23 for price pass-through in the US in relation to automakers, considering the UAW strike.

Volume also impacted: Brazil improves, USA worsens. Brazil BD, despite still facing challenges due to the entry of Chinese steel into the domestic market, still managed to achieve sequential stability, with +0.7% q/q in volume to reach 1,269kt (+8% vs. Genial Est.), with an increase of +10.3% y/y. We believe that this is, in a way, the only positive highlight of the result, since we know how much the market in Brazil is deteriorating.

North America BD showed a declining volume to 885Kt (+1.7% vs. Genial Est.), marking a drop of -6.1% q/q and -0.2% y/y, suffering on a sequential basis due to weak seasonality and high interest rates in the US. South America BD also saw a drop in volume, this time more significantly, by -16.1% q/q and -16.2% y/y, reaching 243kt (-6.3% vs. Genial Est.), still a little lower than we expected. The completely apathetic performance of the business division can be explained by the greater slowdown in volumes in units with lower profitability (Dominican Republic, Colombia, Panama, and Costa Rica), as well as macroeconomic turbulence in Argentina.

For Special Steel, there was also a sequential drop in volume (to a lesser extent), to 339Kt (+4.6% vs. Genial Est.), marking a reduction of -1.8% q/q and -16.2% y/y, reflecting a slowdown in the American macro scenario, due to the continued high level of interest rates (FED rate 5.25%-5.50%), a weaker quarter in relation to the seasonal rebuilding of automakers' inventories, and to top it all off, a strike by the United Auto Workers (UAW) union. On the other hand, shipments grew slightly in Brazil as a result of the loosening monetary policy on the SELIC rate, which was cut 5 times by -0.5p.p. each.

It's worth mentioning the reduction in taxes on light vehicles (IPI, PIS and COFINS) that took place in 2H23, which helped push demand upwards, as can be seen in the ANFAVEA data. Our vision for 2024 is more promising, with growth in the segment for both light and heavy vehicles, with the potential "return to buying" behavior of companies that need to renew their fleet after the market anticipated the entry of Euro 6 models, acquiring a larger volume of Euro 5 in 2022, culminating in very weak sales volumes in 2023.

Revenue down, missing estimates just by a bit. We saw a significant drop in net revenue across all of the company's business units, as we had anticipated. Consolidated revenue narrowed to R$14.7mn (-5.3% vs. Genial Est.), shrinking -13.8% q/q and -18.1% y/y, consolidating a figure slightly below our already pessimistic estimate. We believe that the reason for this lies mainly in the dynamics found in South America BD, with the other business units coming in very much in line with our projections.

It's worth mentioning that the South America division faced the biggest drop in revenues (proportional and nominal), reaching R$326mn (-73.2% vs. Genial Est.), going back a high double digit (-79.2% q/q; -79.1% y/y), mainly due to the mark-to-market of assets in Argentina, a challenging scenario that we've already mentioned in this report. Meanwhile, the Brazil unit registered R$6.0bn (-0.2% vs. Genial Est.), down -9.1% q/q and -12.3% y/y. ON North America reached R$5.9bn (+0.2% vs. Genial Est.), down -6.4% q/q and -8.4% y/y. Finally, the Special Steel division reported revenues of R$2.5bn (-0.7% vs. Genial Est.), down -6.9% q/q and -21.2% y/y.

Table 3. Net Revenue Gerdau (4Q23 vs. Genial Est.)

	4Q23	4Q23E		3Q23		4Q22	
(R$ millions)	**Reported**	**Genial Est.**	**% R/E**	**Reported**	**% q/q**	**Reported**	**% y/y**
Net Revenue	**14.716**	**15.536**	**-5,3%**	**17.063**	**-13,8%**	**17.964**	**-18,1%**
Brazil BD	6.034	6.046	-0,2%	6.635	-9,1%	6.877	-12,3%
North America BD	5.927	5.918	0,2%	6.332	-6,4%	6.472	-8,4%
South America BD	326	1.217	-73,2%	1.566	-79,2%	1.561	-79,1%
Special Steel BD	2.580	2.598	-0,7%	2.771	-6,9%	3.274	-21,2%
Eliminations	(151)	(243)	-37,9%	(242)	-37,5%	(219)	-31,1%

Source: Gerdau, Genial Investimentos

Brazil BD COGS/t lower than forecast, although consolidated increased q/q. Despite the consolidated cost rising sequentially, COGS/t showed a reduction at Brazil BD and an increase at North America BD. Brazil BD reported a COGS/t of R$4,513/t (-9.7% vs. Genial Est.) down -5% q/q and -17.3% y/y, feeling the downward trend of metallurgical coal. Our outlook was for a slight increase, despite greater efficiency in the use of coke and the delay to the spot curve. We were positively surprised by better-than-expected cost efficiency at Brazil BD, as higher shipment volumes (+8% vs. Genial Est.) supported fixed cost dilution capacity.

At North America BD, COGS/t was R$5,557/t (-2.1% vs. Genial Est.), a sequential increase of +4.4% q/q, reflecting the tighter supply of ferrous scrap in the US, as we commented in our preview report. In Special Steel, the increase in COGS/t of +1.3% q/q to R$6,882/t was attributable to the increase in fixed costs, given the low volume of shipments, and the high costs of scrap.

EBITDA in double-digit decline. Even with revenues slightly lower than we expected, due to the much lower than desired dynamics seen at South America, as Brazil's BD COGS/t came in slightly cooler than our estimates, this meant that reported EBITDA was exactly in line with our projections. Gerdau reported an adjusted EBITDA of R$2.0bn (+1.3% vs. Genial Est.), a reduction of -39.1% q/q and -43.8% y/y. According to our projection, there was a margin compression to 13.9% (-5.7p.p q/q; -6.3p.p y/y).

As mentioned, the main negative highlight was South America BD, which reported R$135mn (-25.9% vs. Genial Est.), down -73.1% q/q and -61.8% y/y. Brazil BD recorded a contraction of -41.0% q/q and -32.4% y/y, reaching an EBITDA of R$512m (+14.3% vs. Genial Est.). Although the performance wasn't clear enough for us to call it a positive highlight, we still think it was above our projections due to the higher volume of shipments and COGS/t being cooler than we expected (due to the greater capacity to dilute fixed costs). North America BD was in line with our estimate and posted Adjusted EBITDA of R$1.1bn (+1.5% vs. Genial Est.), down -27% q/q and -37.8% y/y.

Table 4. EBITDA Gerdau (4Q23 vs. Genial Est.)

(R$ millions)	4Q23 Reported	4Q23E Genial Est.	% R/E	3Q23 Reported	% q/q	4Q22 Reported	% y/y
Adjusted EBITDA	**2.039**	**2.012**	**1,3%**	**3.349**	**-39,1%**	**3.630**	**-43,8%**
Brazil BD	512	448	14,3%	868	-41,0%	757	-32,4%
North America BD	1.135	1.118	1,5%	1.555	-27,0%	1.824	-37,8%
South America BD	135	182	-25,9%	502	-73,1%	354	-61,8%
Special Steel BD	340	282	20,5%	475	-28,5%	525	-35,2%
Eliminations	(83)	(19)	341,5%	(51)	63,7%	170	-148,8%

Source: Gerdau, Genial Investimentos

Net profit in free fall due to weakened operation. As a result of a very bad dynamic operation, reported net income was R$587mn (-36.2% vs. Genial Est.), with a downward trajectory of -63.1% q/q and -51.8% y/y. We didn't expect the reduction to exceed the -50% q/q mark, so a large part of the difference to our estimates can be attributed to non-recurring items and the proportional EBITDA of affiliated and jointly controlled companies, since the reported financial result of -R$156mn was also not much different from what we expected.

Table 5. Income Statement Gerdau (4Q23 vs. Genial Est.)

(R$ millions)	4Q23 Reported	4Q23E Genial Est.	% R/E	3Q23 Reported	% q/q	4Q22 Reported	% y/y
Net Revenue	**14.716**	**15.536**	**-5,3%**	**17.063**	**-13,8%**	**17.964**	**-18,1%**
COGS	(13.083)	(13.960)	-6,3%	(14.271)	-8,3%	(15.036)	-13,0%
Adjusted EBITDA	**2.039**	**2.012**	**1,3%**	**3.349**	**-39,1%**	**3.630**	**-43,8%**
EBITDA Margin (%)	13,9%	13,0%	0,9p.p	19,6%	-5,77p.p	20,2%	-6,35p.p
EBIT	**891**	**1.317**	**-32,3%**	**2.384**	**-62,6%**	**2.485**	**-64,1%**
EBIT Margin (%)	6,1%	8,5%	-2,42p.p	14,0%	-7,92p.p	13,8%	-7,78p.p
D&A	(791)	(771)	2,6%	(789)	0,2%	(770)	2,8%
Financial Result	(156)	(216)	-27,7%	(478)	-67,4%	(497)	-68,6%
Net Income	**587**	**920**	**-36,2%**	**1.592**	**-63,1%**	**1.219**	**-51,8%**
Net Margin (%)	4,0%	5,9%	-1,93p.p	9,3%	-5,34p.p	6,8%	-2,8p.p

Source: Gerdau, Genial Investimentos

Our Take on Gerdau

What would be the main upside/downside points? We believe that the sharp drop in EBITDA and margin compression in 4Q23 is nothing new to the market. So, the points that, in our view, will define how the shares prices may behave from now on looking at the business division in Brazil are: **(i)** dynamics in China and potential improvement (or maintenance) of weaker domestic steel consumption vs. the amount of crude steel destined for export; (**ii**) level of protection offered by import tariffs in Brazil vs. dialog between the sector and the Brazilian authorities to recalibrate the tax rate (**iii**) pace of improvement in the automotive market in 2024 and finally, **(iv**) degree of reduction in construction sites in 2024 vs. slowdown in real estate launches (high and medium income) observed in 2023.

In addition, for the US, we point out: **(v)** the level of stabilization of the metal spread in the US (will it reduce, or will it continue to be much higher than the historical average?) and **(vi)** the moment when the FED will begin to reduce interest rates (the probability of it being in March has already fallen a lot, we bet early on June, with a cut of -0.25p.p).

Situation calling for structural change or a combination of factors in favor. Steel from China continues to enter the country and compete with the domestic product, continuing the challenge faced by domestic steelmakers. China's views on real estate activity differ, but it is certain that today the country no longer focuses solely on this market and is seeking activities in other branches that don't demand as much steel (rise in the services PMI, for example), leading it to dispose of its surplus. Blast furnace utilization rates remained above 90% for much of last year and demand in China did not match this crude steel production, which reached ~1Bt in 2023. This combination led to the solution we described above: disposing of the surplus. Looking from November to now (mid-February), average utilization rates at China's main blast furnaces have dropped to ~83%. We believe this was probably the result of a potential cut in government subsidies for steel production coupled with the shutdown of some mills (maintenance + Lunar New Year holiday).

However, Chinese demand still doesn't seem to be enough to improve the situation, and it certainly won't be enough to solve the hindrance suffered by domestic steelmakers in isolation. A combination of factors would help, with **(i)** an increase in the tariff on steel imported into Brazil (we're betting on 17% vs. the 25% demanded by Aço Brasi) and **(ii)** a partial increase in industrial activity in China (we're a little more optimistic than the consensus on this point). Regarding a partial improvement in China's domestic steel consumption, we elaborate more emphatically on how this could help Gerdau and why we are projecting a slight expansion in China's industrial PMI in 2024 vs. 2023, in our preview report. We strongly recommend reading (Gerdau: 4Q23 Preview).

For now, we maintain our neutral bias towards the steel industry. With Chinese exports continuing apace, some action would be needed to counteract them. As mentioned in the paragraph above, one alternative is to increase the tariff on steel imports. The increase in this rate on February 5 (to 14% on average) demonstrates the government's gradual move to try to resolve the impasse, but at a magnitude that is still far from desirable. The truth is that it's a tug-of-war of interests (manufacturing industry lobby + trade relationship with China vs. paralyzed steel mills with suspended work contracts).

The reduction in China's blast furnace utilization rate (from over 90% to 83%) reflects the decrease in supply due to weak demand. However, a structural change is needed to alter the current scenario. Therefore, we don't expect our view of the company to change much in the short term. The next few months will still be made up of difficult days....

Low cash flow generation, but within expectations. Starting from a reported EBITDA suffering a significant drop (-39.1% q/q; -43.8% y/y), in line with our estimate (+1.3% vs. Genial Est.), the reported cash flow (FCFE) was R$1.2bn (+12% vs. Genial Est.), showing a reduction of -42% q/q. We expected CAPEX to be in line with that reported (~R$2bn). However, reported FCFE generation was slightly above our estimate, due to the write-off of a portion equivalent to R$474mn of total CAPEX that has no cash effect, as we mentioned at the beginning of the report. Without this effect, the cash flow would have been fully equivalent to that projected by us.

We were right about CAPEX guidance surplus. In addition, the company exceeded its 2023 annual guidance of R$5bn in CAPEX and reported R$5.7bn, in line with our projection (R$5.8bn Genial Est.). This dynamic has finally consolidated what we have been anticipating for a long time in various reports: CAPEX will be a concern, Gerdau will slip a little in relation to guidance and this will become a moderating factor for investor interest in the company's stock, as can be seen in this report, published by us as recently as October last year (Gerdau Stakeholder Day 2023).

We would also like to point out that Gerdau announced its CAPEX guidance for 2024, which stands at R$6bn. This figure currently fits perfectly within our estimates (R$5.9bn 24E). We will evaluate it throughout the year to see whether or not this target will be exceeded, just as we did with the figure given for 2023 and we got it right in advance.

Disappointing dividends. We had already expected a sequential reduction in dividends, but the retraction was even more intense than our estimate. Even with CAPEX coming in above guidance, but in line with our calculations, dividends fell even more than expected. Gerdau announced a **distribution of R$0.10/share** (-61.5% vs. Genial Est.). As an example, the dividend announced in 3Q23 was R$0.47/share. Along these lines, we are betting on lower dividends for 2024 vs. 2023, and we see Gerdau with a **dividend yield** of **6% 24E**.

A quarter to forget... We appreciate the company's investment thesis and note a less detrimental impact of bearish steel cycles on its results today compared to before 2021 (the mark of the last bullish cycle). We credit this to Gerdau's improved profitability levels over the last 5 years, given the good work the company has done in investing in the right assets, improving the value of the product mix, while divesting assets that did not generate adequate profitability (selloffs of JVs in South America BD are the continuation of this process in 2024). We know, therefore, that the sharp reduction in results in 4Q23 is not related to the company's wrong decisions in any way, but rather to the naturalness of the cyclical steel business. Even so, this is a quarter to forget...

Even though the **operational pressure** reducing **24E EBITDA** to **R$10.4bn** (vs. R$13.5bn 2023) has already been priced into the stock's ~20% drop over the last 6M, we **see no immediate catalysts for the stock to rise**. We have opted to postpone changing the company's rating and continue to suggest a **NEUTRAL** stance, given a **24E EV/EBITDA** of **4.1x** in line with the historical average. Therefore, after the revision made in the last report, the **12M Target Price** in our model is **R$24.50**, proposing an **upside of +14.49%**.

Appendix: Gerdau

Figure 1. Gerdau – Income Statement in R$ Millions (Genial Est. 2023-2028)

Income Statement	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**69.737**	**67.168**	**69.253**	**71.206**	**72.980**	**75.726**
(-) COGS	(58.461)	(59.561)	(59.437)	(60.785)	(62.004)	(62.934)
Gross Profit	**11.276**	**7.607**	**9.816**	**10.421**	**10.976**	**12.792**
(-) Expenses	(2.053)	(1.824)	(1.891)	(1.922)	(1.946)	(1.996)
Adjusted EBITDA	**13.482**	**10.462**	**12.264**	**13.317**	**13.927**	**15.935**
(-) D&A	(2.257)	(3.253)	(3.603)	(3.915)	(4.195)	(4.446)
EBIT	**10.881**	**6.459**	**8.613**	**9.208**	**9.754**	**11.547**
(+/-) Financial Result	(1.420)	(1.258)	(1.364)	(1.358)	(1.317)	(1.552)
(-) Taxes	(1.842)	(925)	(1.113)	(1.233)	(1.292)	(1.540)
Net income	**7.618**	**4.275**	**6.136**	**6.617**	**7.144**	**8.456**
Profitability						
Net margin (%)	10,92%	6,36%	8,86%	9,29%	9,79%	11,17%

Figure 2. Gerdau– Cash Flow in R$ Millions (Genial Est. 2023-2028)

Cash Flow (FCFF)	2023E	2024E	2025E	2026E	2027E	2028E
Net Revenue	**69.737**	**67.168**	**69.253**	**71.206**	**72.980**	**75.726**
(-) COGS	(58.461)	(59.561)	(59.437)	(60.785)	(62.004)	(62.934)
Adjusted EBITDA	**13.482**	**10.462**	**12.264**	**13.317**	**13.927**	**15.935**
EBIT	**10.881**	**6.459**	**8.613**	**9.208**	**9.754**	**11.547**
(-) Taxes	(1.842)	(925)	(1.113)	(1.233)	(1.292)	(1.540)
(+) D&A	2.257	3.253	3.603	3.915	4.195	4.446
(+/-) Δ WK	1.478	262	(294)	(408)	(413)	(290)
(-) Capex	(5.820)	(5.886)	(5.950)	(6.016)	(6.082)	(6.149)
FCFF	**6.953**	**3.162**	**4.859**	**5.466**	**6.161**	**8.014**

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