

# Chief executive officer's letter

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## Dear Shareholder,

In 2018, EVRAZ delivered robust growth amid favourable market conditions and as a result of continuing initiatives to improve efficiency and reduce costs. The Group generated EBITDA of US\$3,777 million during the reporting period, its highest level since 2008, which made it possible to pay dividends of US\$1.6 billion. EVRAZ remained focused on implementing its efficiency improvement programme in the amount of 3% of the cost base, the effect from which totalled US\$340 million in 2018. Shareholders' appreciation of these results is evidenced by the rise in the Group's average market

capitalisation to US\$9.2 billion in 2018, an 197% increase from that in 2017.

Global markets were supportive in 2018, driven mainly by developments in China, where the government finalised its supply-side reform of the steelmaking industry and enacted winter output cuts in a number of provinces. These efforts kept utilisation rates at Chinese steel mills at a level of more than 87% throughout the year. In pursuit of better productivity from existing furnaces, coke and pig iron producers required higher-grade raw materials. Combined with higher



## Financial review

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demand from India and South-East Asia, this led hard coking coal prices to average US\$207 per tonne, higher than had been forecasted. Positive developments on the vanadium market also influenced EVRAZ performance in 2018. China's new rebar standard requiring higher vanadium content in products and its ban on vanadium slag imports, coupled with scarce operating capacity of vanadium producers globally, created a deficit for the metal that drove prices up by 150% year-on-year.

The Group's strategic vision remains unchanged. EVRAZ is a global steel and mining company, leading producer of infrastructure steel products with low-cost production along the value chain. The Group focuses on four key strategic priorities: maintaining a stable dividend payout and proactively managing maturities; expanding the CAPEX programme with selective investments in development projects; continuing to generate efficiency improvements with an annual effect of 3% of the cost base; and developing the product portfolio and customer base across all assets in Russia and North America.

In terms of debt management, EVRAZ ended 2018 with net debt of US\$3,571 million and retains its medium-term debt target at below US\$4 billion. In the longer-term perspective, the Group aims to maintain its net debt / EBITDA ratio at an average level of 2.0x throughout the cycle, taking into account risks of EBITDA fluctuations. EVRAZ also established a new dividend policy in 2018 that envisages paying a minimum of US\$300 million per annum of dividends provided that the net leverage ratio remains below 3.0x. The dividend payout may be higher if the Group's net debt remains close to the stated target and the amount of cash flows generated covers the investment programme needs. Because such conditions were met in 2018, EVRAZ paid dividends of \$1.6 billion with a dividend yield of 17%.

In 2018, EVRAZ took further actions to streamline its operations and divest of non-core assets. In June, the Group announced the disposal of a 15% minority stake in Chinese steel producer Delong Holdings Ltd due to a lack of links with our core operations. EVRAZ also finalised its efforts to exit the Ukrainian market by divesting of EVRAZ DMZ, a decision primarily driven by the limited growth opportunities in the region. The Group's asset optimisation process will allow it to more fully concentrate on developing its core assets.

EVRAZ has tailored its CAPEX allocation programme in a way that it contributes as much as possible to achieving the stated strategic priorities and targets. In 2018, the Group presented an investment programme that envisages annual total CAPEX spending of US\$800-990 million during

2019–22. The expansion is driven by four major development projects, including constructing a flat-casting and rolling facility in Siberia, building a new long rail mill in Colorado, as well as modernising a rail and beam mill and launching a new continuous-casting machine in the Urals.

Safety remains the underpinning of EVRAZ business sustainability. In 2018, the Group maintained its lost time injury frequency rate (LTIFR) at the level of 1.9x, focusing on two major new initiatives: a contractor safety programme and an HSE performance assessment for operations managers. However, despite every effort that was undertaken, EVRAZ was unable to make substantial progress in reducing fatal accidents in 2018: there were a total of 10 fatalities across all Group assets. To achieve a radical change in its safety culture, in 2019, EVRAZ is launching an initiative to engage workers at every level.

In 2018, the Group also devoted special attention to environmental protection, an important aspect of sustainable long-term development. During the reporting period, EVRAZ ZSMK completed the reconstruction of the gas purifying facilities at its sinter plants that, together with other initiatives, has achieved annual reductions in plant emissions of 16 thousand tonnes and in wastewater discharge of 6 million cubic metres. EVRAZ current environmental protection programme includes 23 projects, five of which will be included in the federal presidential ecological programme for 2019–24, driving a reduction in total annual emissions of another 52 thousand tonnes by 2024.

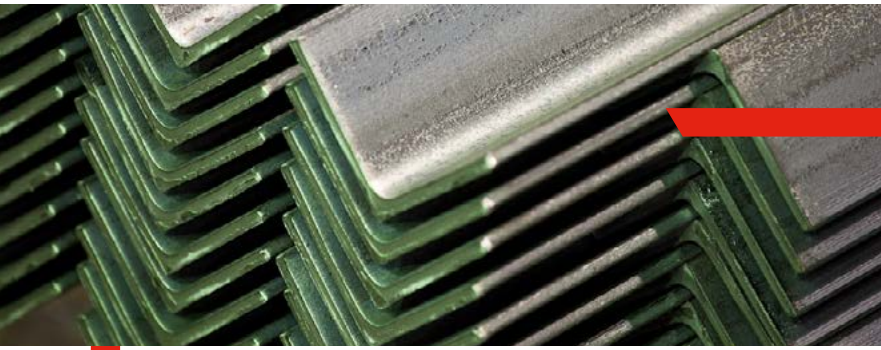
In terms of human capital management, the Group believes that motivated, competent and loyal employees create the foundation for the business. In 2018, EVRAZ implemented several initiatives aimed at developing managerial capabilities and enhancing personnel engagement levels. One key initiative was the newly launched "Top-300 programme", which has been designed as a transformative set of personal training sessions and workshops for shop superintendents and mine directors. The Group also conducted a series of information days at each production site to increase employee awareness of EVRAZ strategy and initiatives and conducted the "We are together" poll to collect feedback in an effort to further improve working conditions. Overall, employee engagement at the Group improved by 1 percentage point to 53% in 2018, while the average engagement figure for the Russian metals and mining industry decreased by 5 percentage points.

To ensure stable development, EVRAZ aims to secure leadership in key markets, namely in long and construction steel products. To achieve these targets, the Group needs

to constantly adapt to evolving customer needs. In 2018, EVRAZ launched a project with a key client, Russian Railways, that included developing new types of rails and extra services. The Group continued to execute its programme to promote the application of beams in construction and increase the available stock of beams. EVRAZ also conducted a set of workshops and meetings with clients at which the Group's senior management team sought to better understand customers' changing needs and most pressing issues in order to create additional value for them.

In 2018, the Group continued to implement EVRAZ Business System (EBS) transformation projects, the overriding goal of which is to engage every employee in the process of continuous improvement and idea generation. These ideas are the major source of new efficiency improvement initiatives and EBS transformations are the projects that create the necessary infrastructure for this process to continue. In 2018, the Group successfully completed 24 EBS transformation projects across its steel and coal assets, and employees generated a total of 17,732 ideas, 5,985 of which were implemented. In overall, EBS has already involved a total of 15,234 people, and its total identified and potential economic effect equalled US\$268 million. EVRAZ aims to reach 100% EBS coverage at all Russian assets by 2021.





## STEEL SEGMENT

The Steel segment remains the core of the EVRAZ business with a unique mix of transportation and construction finished steel products.

In 2018, total output of steel products declined by 5% down to 10.2 million tonnes. Sales of finished steel products in Russia rose to 4.6 million tonnes, up 5% from 4.4 million tonnes in 2017. The segment's EBITDA surged to US\$2,672 million, including a significant effect from the vanadium business. Efficiency improvement initiatives had a total effect of US\$198 million, most of which came from the launch of investment projects, increased domestic sales and savings on steelmaking operations.

One of the most significant events for the Steel segment was the successful launch of blast furnace No. 7 at EVRAZ NTMK. It took only 18 months to complete construction of the project, which had a total CAPEX of US\$204 million. The furnace has an annual pig iron output of 2.6 million tonnes and is considered to be one of the cleanest in Russia, with an increase in air purification of 2.5 times and a reduction in coke consumption of 5 kilogrammes per tonne compared with other operating furnaces.

EVRAZ also launched several successful projects during the reporting period, including: a grinding ball mill at EVRAZ NTMK with CAPEX of US\$17 million, which increased the production of balls to more than 300 thousand tonnes; and the launch of a wheels resurfacing line at EVRAZ NTMK with CAPEX of US\$14 million, which processes premium S-wheels and has a production capacity of 66 thousand wheels.

Looking ahead, one of the Steel segment's key targets is to reach 6.9 million tonnes of finished steel sales to the Russian market by 2023. To achieve this target, EVRAZ is considering several investment projects to enhance the product mix. EVRAZ ZSMK is considering the construction

of an integrated flat casting and rolling facility that will help to enter the flat products market with 2.5 million tonnes of coil a year, including 1.5 million tonnes sold domestically by 2023. The technology entails continuous casting and rolling from steel to coil, eliminating the slab stage, which will significantly lower production costs. Thickness of produced coils will range from 1.2 millimetres to 25 millimetres. Total CAPEX for the project is estimated at US\$490 million.

EVRAZ NTMK is considering a product mix improvement programme that includes investment projects to update the rail and beam mill for US\$215 million and install a new continuous casting machine No. 5 for US\$120 million. Both projects will add capacity to produce more value-added products, including 230 thousand tonnes a year of beams, 50 thousand tonnes a year of sheet piles and 460 thousand tonnes a year of pipe blanks for seamless oil country tubular good (OCTG) production.

In 2019, for these three projects, the Group plans to finalise selection of the general suppliers of equipment, develop project documentation and conduct engineering works. It also plans to complete major construction works for the overhaul of blast furnace No. 6 at EVRAZ NTMK, after which blast furnace No. 5 will shut down in 2020.



## COAL SEGMENT

EVRAZ Coal segment is the leading Russian producer of coking coal.

In 2018, the Group increased coal mining volumes by 0.9 million tonnes to a total of 24.2 million tonnes a year. Coal concentrate production grew by 8% to 14.1 million tonnes. The Coal segment's EBITDA equalled US\$1,218 million for the period, remaining flat compared to 2017. In 2018, the Group also generated US\$70 million from efficiency improvement initiatives.

The increase in mining volumes was driven by ramp up of the Rospadskaya-Koksovaya open-pit project, which added more than 1 million tonnes a year of premium low-vol coal (OS grade). It, combined with focus on internal coal shipments and the disposal of EVRAZ DMZ, led to the improvement of self-sufficiency in coal by 19 percentage points to 69%. In addition to the mining ramp-up, EVRAZ boosted its coal export shipments to 7.7 million tonnes (up 17% year-on-year) through such actions as expansion of its sales geography (up 2.4x times to Europe), increase in the share of long-term agreements with railcar operators to 75% and improvements to the efficiency of operational management for shipments to Russia's Far East.

Looking forward, the key goal of EVRAZ Coal segment is to continue growing coal mining volumes to 28.4 million tonnes a year by 2021. To reach this target, the Group plans to further expand mining of high-vol coal coking coal grades by 4.1 million tonnes. Major effect of 2.5 million tonnes will come from such projects as the development of seam No. 48 at the Uskovskaya mine and seam No. 29 at the Esauskaya mine. EVRAZ also continues to increase the supply of low-vol coal grades through the implementation of its longwall mining project at the Rospadskaya-Koksovaya mine. The project will add 0.9 million tonnes of low-vol coals (K grade) shipped internally, helping to improve coal the Steel segment's self-sufficiency.



## STEEL, NORTH AMERICA SEGMENT

EVRAZ operations in the US and Canada make it a leader in the North American rail and large-diameter pipe market.

Total sales of steel products reached 2.2 million tonnes, up 14% from 1.9 million tonnes in 2017. The segment's EBITDA was US\$14 million, down from US\$58 million in 2017, mainly due to the effect of tariffs and duties on Canadian large-diameter and line pipe sales into the US, as well to production issues at EVRAZ Regina. The operational performance at EVRAZ Pueblo and EVRAZ Portland was strong and the segment's efficiency improvement programme contributed a total of US\$72 million.

In 2018, the major focus was set to achieve the target effect from the two investment projects implemented in 2016-17: EVRAZ Regina's steelmaking upgrade and the construction of the new large-diameter pipe mill No. 5. The targets for monthly slab production, degassing rate and prime yield for large-diameter pipe were achieved in the fourth quarter of 2018 and full capacity should be reached in 2019, supported by solid demand for energy pipe in Canada.

In addition, most of the construction work has been finished for two investment projects focused on electric resistance welded (ERW) and seamless OCTG operations. The first project, a threading line with annual capacity of 110 thousand tonnes at EVRAZ Pueblo, will contribute savings of US\$10 million on third-party services when it reaches full capacity. The second, a heat treatment project with annual capacity of 100 thousand tonnes at EVRAZ Red Deer, will be launched in 2019 to upgrade the OCTG

product mix and streamline the product flows between Canadian operations.

In 2018, the Group initiated the design and engineering work on a new rail mill at EVRAZ Pueblo that is planned to be launched in 2021. The project entails building a brand-new rolling mill with annual capacity of 600 thousand tonnes and will be able to produce rails with a length of 100 metres. Total investments required are estimated at US\$480 million. The project will allow EVRAZ North American operations to maintain technological leadership, reach a 45% market share in North American rails and shift to a higher value product mix in rails.

For 2019, the Group plans to finalise the selection of general suppliers of main equipment, complete equipment and plant engineering and prepare the construction site.



### OUTLOOK FOR 2019

EVRAZ believes that its strong pipeline of existing investment projects, the continued evolution of its efficiency improvement initiatives and its low net leverage levels will help the Group to resist possible market downturns that could potentially squeeze margins, thereby ensuring the business' stable development.

A blue ink signature of Alexander Frolov, written in a cursive style.

**Alexander Frolov**  
Chief Executive Officer