



SECOND QUARTER 2018  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
STELCO HOLDINGS INC.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS OF STELCO HOLDINGS INC.

This Management's Discussion and Analysis (MD&A) is intended to enable a reader to assess Stelco Holdings Inc.'s (Stelco Holdings) results of operations and financial performance for the three and six months ended June 30, 2018 ('Q2 2018' and 'YTD 2018', respectively). Unless the context indicates otherwise, references to the "Company", "Stelco", "we", "us" or "our" refer to Stelco Holdings and its consolidated subsidiaries, as applicable. This MD&A, which has been prepared as of July 31, 2018, should be read in conjunction with our unaudited interim consolidated financial statements and related notes for the three and six months ended June 30, 2018 as well as our MD&A for the period ended December 31, 2017 (2017 MD&A). Our June 30, 2018 unaudited interim consolidated financial statements have been prepared in accordance with International Accounting Standard (IAS) 34, *Interim Financial Reporting* and are presented in millions of Canadian dollars unless otherwise indicated.

These documents, as well as additional information relating to the Company, including our 2017 Annual Information Form for the year ended December 31, 2017 (2017 AIF), have been filed electronically with the Canadian securities regulators through the System for Electronic Document Analysis and Retrieval (SEDAR) and are available through the SEDAR website at [www.sedar.com](http://www.sedar.com).

### FORWARD-LOOKING INFORMATION

Certain information included in this MD&A contains forward-looking information within the meaning of applicable securities laws. This information includes, but is not limited to, statements made in our "*Business Overview*"; "*Strategy*"; "*Review of Balance Sheets*"; "*Capital Resources and Liquidity*"; "*Dividend Policy*"; "*Risk and Uncertainties*" sections of this MD&A and in the "*Risk Factors*" section in the 2017 AIF.

Forward-looking information may relate to our future outlook and anticipated events or results and may include information regarding our financial position, business strategy, growth strategy, budgets, operations, financial results, taxes, dividend policy, plans and objectives of our Company. Particularly, information regarding our expectations of future results, performance, achievements, prospects or opportunities is forward-looking information. In some cases, forward-looking information can be identified by the use of forward-looking terminology such as "plans", "targets", "expects" or "does not expect", "is expected", "an opportunity exists", "budget", "scheduled", "estimates", "outlook", "forecasts", "projection", "prospects", "strategy", "intends", "anticipates", "does not anticipate", "believes", or variations of such words and phrases or state that certain actions, events or results "may", "could", "would", "might", "will", "will be taken", "occur" or "be achieved". In addition, any statements that refer to expectations, intentions, projections or other characterizations of future events or circumstances contain forward-looking information. Statements containing forward-looking information are not historical facts but instead represent management's expectations, estimates and projections regarding future events or circumstances. The forward-looking statements contained herein are presented for the purpose of assisting the holders of our securities and financial analysts in understanding our financial position and results of operations as at and for the periods ended on the dates presented, as well as our financial performance objectives, vision and strategic goals, and may not be appropriate for other purposes.

The forward-looking information includes, among other things: statements relating to the continuation of the strong production performance; the Company's position to grow organically; expectations regarding utilization of excess capacity; expectations regarding upgrades to existing facilities and their effect on revenue and costs; expectations regarding the Company's access to a wider range of markets; expectations regarding the impact of our tax attributes on our future cash flows; expectations concerning the timing and duration of our hot strip mill outage; expectations concerning enhanced shipping volumes; statements regarding our dividend policy; expectations concerning working capital and capital expenditures and the future actions relating thereto and the anticipation of creating value and profitability.

This forward-looking information and other forward-looking information are based on our opinions, estimates and assumptions in light of our experience and perception of historical trends, current conditions and expected future developments, as well as other factors that we currently believe are appropriate and reasonable in the circumstances. Despite a careful process to prepare and review the forward-looking information, there can be no assurance that the underlying opinions, estimates and assumptions will prove to be correct.

The forward-looking information contained in this MD&A represents management's expectations as of the date of this MD&A and is subject to change after such date. However, we disclaim any intention or obligation or undertaking to update or revise any forward-looking information whether as a result of new information, future events or otherwise, except as required under applicable securities laws in Canada. The forward-looking information contained in this MD&A is expressly qualified by this cautionary statement.

Forward-looking information is necessarily based on a number of opinions, estimates and assumptions that management considered appropriate and reasonable as of the date such statements are made, is subject to known and unknown risks, uncertainties, assumptions and other factors that may cause the actual results, level of activity, performance or achievements to be materially different from those expressed or implied by such forward-looking information, including but not limited to, those described below and referred to under the heading "*Risk and Uncertainties*" below and under the heading "*Risk Factors*" in the 2017 AIF.

The Company's volume estimates for the third and fourth quarter referenced herein are based on a number of assumptions, including but not limited to, the following material assumptions: the Company's hot strip mill outage will be of limited duration and result in improved production capabilities and efficiencies; steel prices will generally be in line with current trends and sales activities over the period; shipping capability and shipping options will remain consistent with prior periods; third and fourth quarter product mix will be comparable to Q2 2018; the Company's ability to continue to attract new customers and further develop and maintain existing customers; there are no significant additional legal or regulatory developments, changes in economic conditions, or macro changes in the competitive environment affecting our business activities, however, we note that potential further changes to trade regulations

in the United States and Canada or amendments to the North American Free Trade Agreement could materially alter underlying assumptions around our expected production and volumes; future operating expenses, capital expenditures and debt service costs; the upgrade to the hot strip mill remaining on schedule and on budget and its anticipated effect on production and finishing capabilities; the Company's ability to continue to access markets without any further adverse trade restrictions; and expectations regarding industry trends, market growth rates and the Company's future growth rates, plans and strategies to increase revenue and cut costs.

We caution that the list of risk factors and uncertainties is not exhaustive and other factors could also adversely affect our results. Readers are urged to consider the risks, uncertainties and assumptions carefully in evaluating the forward-looking information and are cautioned not to place undue reliance on such information.



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# MANAGEMENT'S DISCUSSION AND ANALYSIS

## Business Overview

Stelco Holdings is the parent company of Stelco Inc., one of Canada's leading steel producers, and is listed on the Toronto Stock Exchange (TSX) under the symbol 'STLC'. The Company was incorporated on September 25, 2017 under the *Canada Business Corporations Act* and is based in Hamilton, Ontario, Canada.

Stelco Holdings completed an initial public offering on November 10, 2017 and acquired all outstanding shares of Stelco Inc. from Bedrock Industries B.V. (Bedrock B.V.), a wholly-owned indirect subsidiary of Bedrock Industries LP (Bedrock). Bedrock continues to be Stelco Holdings' indirect majority shareholder, currently owning approximately 73.5% of the issued and outstanding common shares.

Since Bedrock indirectly acquired all outstanding shares of Stelco Inc. on June 30, 2017 and had common control at the date when Stelco Holdings acquired Stelco Inc., the Company accounted for this transaction in a manner similar to a pooling of interest method applied from June 30, 2017. This method required our 2017 consolidated financial statements to be restated for periods prior to the date of obtaining common control (November 10, 2017), to reflect the combination as if it had occurred from the beginning of the period as if the entities were under common control, regardless of the actual date the common control transaction closed.

## Overview

Stelco Inc. (formerly known as U. S. Steel Canada Inc. (USSC)) was established in 1910 and is primarily engaged in the production and selling of steel products. The Company owns one of the newest and among the most technologically advanced integrated steel making facilities in North America. Stelco produces flat-rolled value-added steels, including premium-quality coated, cold-rolled full hard and hot-rolled steel products. With first-rate gauge, crown, and shape control, as well as uniform through-coil mechanical properties, our steel products are supplied to customers in the construction, automotive and energy industries across Canada and the United States. We believe our total cash costs per net ton (nt) are among the lowest in North America and we expect our margins per nt will expand as we increase our asset utilization and regain volumes lost in recent years.

We operate from two facilities: Lake Erie Works (LEW) near Nanticoke, Ontario and Hamilton Works (HW) in Hamilton, Ontario. LEW facilities are comprised of a coke battery, a blast furnace, two basic oxygen furnace steel making vessels, a steel ladle treatment system (LTS), a RHOB vacuum steel degassing facility, twin-strand slab caster, a 6-stand hot strip mill, and three pickling lines. LEW produces hot-rolled coil and hot-rolled pickled steel that are either sold to third-parties or sent on to HW for further processing. HW facilities are comprised of a coke battery, a 4-stand cold-rolling mill and a Z-Line continuous galvanizing and galvannealing line (CGL). HW is supplied with hot-rolled pickled steel from LEW and produces high quality cold-rolled full hard and coated steel products as well as coke that is supplied to LEW to fuel its blast furnace and could be sold to third-parties. We believe our rolling and finishing capabilities represent some of the most advanced in our industry and differentiate us from our North American competitors. In addition to LEW and HW, we own a 50% interest in two separate joint ventures: Baycoat Limited Partnership and D.C. Chrome Limited that complement our finishing capabilities.

Our operations are strategically located near our raw material suppliers and core customers which we believe positions us to serve both Canadian and American customers with shorter lead-times relative to other steelmakers. Furthermore, the fact that both of our operating facilities have access to multiple modes of transportation (water, rail and truck) allows us to negotiate competitive freight rates, rapidly adapt to changing market environments, and access customers across a wide range of locations.

## U.S. Section 232 Trade Expansion Act

On April 20, 2017, the United States administration issued an executive order directing the United States Department of Commerce to investigate whether imports of foreign steel are harming US national security. The directive falls under Section 232 of the Trade Expansion Act of 1962, which allows the US president to restrict trade of a good if such trade is determined to be harmful to US national security.

On February 16, 2018, the US Department of Commerce released its report regarding the Section 232 investigation. The recommendations in that report include options regarding tariffs and/or quotas are intended to adjust the level of steel imports into the United States as it has been determined that those imports are an impairment to national security. Under the statute, the US president is required to adopt, modify or take no action on these recommendations. During March 2018, the US administration suspended the implementation of any steel and aluminum tariffs by exempting Canada, and certain other countries. On May 31, 2018, the US administration signed a proclamation that as of June 1, 2018, tariffs will no longer be suspended for steel or aluminum imports from Canada, Mexico and the European Union.

Although tariffs or quotas on any steel imports into the United States from Canada presents a potential risk, we believe this risk may be mitigated by our continued focus on the development of additional markets for our products. In addition to the risk presented by either tariffs or quotas, there is associated risk of steel imports traditionally destined for the United States being diverted into the Canadian market which could impact domestic demand and pricing.

On May 31, 2018, the Government of Canada responded to the Section 232 tariffs on steel by announcing its intention to impose surtaxes or similar trade-restrictive countermeasures on steel, aluminum and other specified goods imported from the United States, with a value of up to \$16.6 billion. On July 1, 2018, tariffs on steel imported from the United States went into force and were set at 25 per cent, the same tariff rate that the United States applied to Canadian steel under Section 232.

While these developments are not optimal, Stelco has repeatedly demonstrated its resiliency as a leading advanced integrated steel producer in North America, its agility through multiple modes of transportation (water, rail and truck) and financial security through a robust balance sheet, we believe that Stelco can operate successfully in all types of economic environments. Furthermore, the imposition of tariffs on steel imports from the United States presents a potential opportunity for increased demand for our

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products in the domestic Canadian market that could in part mitigate any impact resulting from the tariffs imposed by the United States.

We continue to monitor these developments and anticipate that the Government of Canada will continue to support the businesses and workers impacted by the US administration trade measures.

### ***Trade Remedy: Dumping and Subsidy Investigations***

On May 25, 2018, the Canada Border Services Agency (CBSA) initiated investigations under the *Special Import Measures Act* respecting the alleged injurious dumping and subsidizing of certain cold-rolled steel from China, South Korea and Vietnam. On July 24, 2018, the Canadian International Trade Tribunal (CITT) announced their determination that there is evidence that discloses a reasonable indication that the dumping and subsidizing of the above-mentioned goods have caused or are threatening to cause injury to the domestic industry. On August 23, 2018, the CBSA is scheduled to announce preliminary duties against these products. The CITT will conduct hearings and make their final determination in Q4 2018.

On July 26, 2018, the CBSA initiated investigations under the *Special Import Measures Act* respecting the alleged injurious dumping of certain corrosion resistant steel from China, South Korea, India and Taiwan. Accordingly, the CITT will conduct a preliminary injury inquiry and announce their determination during Q3 2018.

We continue to monitor imports of steel products into Canada and support the utilization of the domestic trade remedy system when and where circumstances warrant to combat dumped and subsidized imports from injuring our business and to aid in the stabilization of the domestic market.

### ***Land and Building Acquisition***

On June 5, 2018, Stelco Inc. acquired the land and buildings beneficially owned by Legacy Lands Limited Partnership (the Land Vehicle) on which Stelco conducts its operations in Hamilton (approximately 760 acres) and Nanticoke, Ontario (approximately 2300 acres), including lands in Hamilton that contain the HW blast furnace and cast houses, as well as developable lands and port facilities (collectively, the Lands). The purchase price payable for the Lands was approximately \$114 million and was financed with a 25-year, 8% per annum mortgage payable (the Mortgage) issued to the Land Vehicle. The quarterly Mortgage payments will be distributed by the Land Vehicle to fund various pension and other post-employment benefit commitments (OPEBs) for Stelco retirees.

In connection with the Lands acquisition, existing lease arrangements between Stelco Inc. and the Land Vehicle were terminated and the associated rental payments were cancelled, resulting in Stelco Inc.'s buildings' which were previously held under a finance lease to be reclassified and presented as wholly-owned buildings on the Company's consolidated balance sheet. The total purchase consideration of \$114 million included land costs of \$85 million (which excludes \$3 million of transaction costs) and the extinguishment of lease related obligations of \$29 million.

The Lands acquisition provides Stelco with the flexibility to utilize the properties for its existing operations and allows Stelco to develop these properties in a manner that both complements our current and future operations and to pursue other uses for the Lands in particular: (i) extracting additional value from our assets by enhancing operating flexibility previously unavailable to us, (ii) lowering our costs, and (iii) creating significant and previously unrealizable value for our shareholders through development of excess land and port facilities located in the Greater Toronto Area. In addition, the Company continues to receive the benefit of the environmental release in respect of the Lands that was granted by the Ministry of the Environment and Climate Change on closing of Stelco's *Companies' Creditors Arrangement Act* (CCAA) reorganization on June 30, 2017.

### ***Amended OPEB Funding Agreement***

Also on June 5, 2018, Stelco Inc. entered into an amended OPEB funding agreement (the Amended OPEB Funding Agreement) that reduced Stelco's exposure to future variable funding requirements (including future excess free cash flow contributions) and provided the independent employee life and health trusts (ELHTs) established as part of Stelco Inc.'s CCAA reorganization, with an increased fixed funding commitment over a 25 year term. The Amended OPEB Funding Agreement replaces Stelco Inc.'s funding obligations under the OPEB funding agreement that was entered into at the closing of Stelco Inc.'s CCAA reorganization (the Original OPEB Funding Agreement).

In providing more fixed annual funding of OPEBs, the Amended OPEB Funding Agreement and Mortgage payments eliminates Stelco's variable funding obligations tied to excess free cash flow that could have resulted in significant additional OPEB funding contributions and provides greater certainty to our employees as to deposits into the trusts.

### ***Common Share Dividend***

On July 31, 2018, the Board of Directors declared a special dividend of \$1.69 per common share, payable on August 15, 2018 to shareholders of record as of August 10, 2018 and a quarterly cash dividend of \$0.10 per common share, payable on August 17, 2018 to shareholders of record as of August 10, 2018. The dividends have been declared as "eligible dividends" for purposes of the *Income Tax Act* (Canada).

During the first and second quarter of 2018, Stelco Holdings declared and paid a cash dividend of \$9 million or \$0.10 per common share, totaling \$18 million or \$0.20 per common share for the first six months of 2018.

### ***Secondary Offering***

On April 4, 2018, Stelco Holdings announced the completion of a bought deal secondary offering (the Offering) of 10,000,000 common shares of Stelco Holdings by Bedrock B.V. at a price of \$21.75 per common share for aggregate gross proceeds of \$217.5 million. The net proceeds of the Offering, after deducting the underwriter commission, were paid to Bedrock B.V. Prior to the



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Offering, Bedrock B.V. held 75,283,887 of Stelco Holdings' common shares, which represented approximately 84.8% of the total outstanding common shares. Following the completion of the Offering, Bedrock B.V. holds 65,283,887 common shares, representing approximately 73.5% of the total outstanding common shares issued by Stelco Holdings.

### Strategy

Our strategy is to maximize total shareholder returns while maintaining a conservative capital structure. In order to accomplish this strategy, we are focused on four strategic objectives: (i) optimizing production from our assets; (ii) maintaining our strong balance sheet; (iii) maximizing profitability and cash flows; and (iv) growing our business. These strategic objectives are supported by the entrepreneurial culture that underpins Stelco's return-based approach to operating our business. This culture is driven by our leadership team's ownership mentality as a result of Bedrock Industries L.P.'s (Bedrock) significant ownership interest in Stelco Holdings, which is unique amongst North American public steel companies. We believe pursuing these strategic objectives will allow us to generate long-term, sustainable returns for our shareholders.

#### Optimize Production From our Assets

As a result of historical underutilization, we have excess capacity in our coke production as well as rolling and other strategic steel product production capabilities. We believe we can utilize this excess capacity to grow our revenues and lower our costs per nt. We are actively pursuing initiatives, including potential purchases of external slab and toll-rolling for third-parties, that can be implemented with limited investment to improve asset utilization. In addition to utilizing excess capacity, we are continuing to pursue initiatives such as capturing, recycling, and selling the by-products generated in our production process. We believe we can deliver significant organic growth from these types of low-capital, high-return projects.

#### Maintain our Strong Balance Sheet

We believe maintaining financial discipline leads to the delivery of sustainable, long-term shareholder returns and will ensure Stelco is well-positioned to manage the cyclical nature of the steel industry. We are committed to maintaining our strong balance sheet with sufficient liquidity and financial flexibility to support our operational and strategic initiatives. This will allow us to finance selective capital expenditure programs aimed at improving our product mix to focus on more advanced steel products, including Advanced High Steel Strength (AHSS) and Ultra High Steel Strength (UHSS) grades. Unlike many of our integrated peers, we are not encumbered by significant and uncapped liabilities associated with pensions and OPEBs. Further, we have approximately \$984 million of non-capital loss carryforwards and other tax attributes on a pre-tax basis as at June 30, 2018, which may allow us to reduce our cash tax payments and increase free cash flow generation. We seek to preserve our capital structure with low financial leverage that is largely free from legacy liabilities in order to ensure maximum free cash flow generation.

#### Maximize Profitability and Cash Flow

Our production and sales efforts are focused on products and end markets that we consider to have the highest potential for profitability and growth. We are currently focused on expanding our technical capabilities in order to produce AHSS and UHSS grades as well as fully-processed cold-rolled products. We believe these products, which are geared toward the automotive and construction end markets, will enable us to deliver higher margins and generate increased cash flow. Additionally, we seek to aggressively maintain our low cost position by controlling the cost of our raw material inputs by entering into long-term supply contracts at either fixed or floating prices and regularly reviewing these contracts with a view toward improving terms. We have also focused on improving our working capital velocity through initiatives aimed at optimizing inventory levels and accounts receivables. We believe we can maximize our profitability and cash flow generation by pursuing these initiatives.

The Company's sales strategy is focused on maximizing profits, including regaining higher margin business, increasing its expansion into additional markets outside Canada with respect to hot-rolled, cold-rolled and coated coil sales, and assessing opportunities to introduce new products. Due to the Company's recently improved financial position, we believe a major roadblock has been removed that previously impacted our ability to compete.

#### Grow our Business

We take a disciplined approach to our capital investments with a focus on return-based metrics. Our management team has a proven track record of value creation through an opportunistic and disciplined approach to acquisitions. By maintaining a strong balance sheet, we can selectively pursue organic and strategic opportunities when market conditions are favourable to us. We have adopted this return-based approach to evaluate opportunities for our business as we seek to expand our capabilities. We evaluate and consider strategic opportunities based on strictly defined financial criteria focused on pursuing projects with the highest cash on cash returns and fastest payback. We believe this will position us to grow our business through complementary acquisitions and other investments to maximize shareholder returns.

#### Non-IFRS Performance Measures

In this MD&A, we refer to certain non-IFRS measures which we use in addition to IFRS measures to evaluate the financial condition and results of operations of the business. We use non-IFRS measures that are typically used by our competitors in the North American steel industry, including "Adjusted Net Income", "Adjusted EBITDA", "Adjusted EBITDA per net ton", "Selling Price per net ton", and "Shipping Volume" to provide supplemental measures of our operating performance and thus highlight trends in our core business that may not otherwise be apparent when relying solely on IFRS financial measures. We also believe that securities analysts, investors and other interested parties frequently use non-IFRS measures in the evaluation of issuers. Our management uses these non-IFRS financial measures in order to facilitate operating performance comparisons from period-to-period, to prepare annual operating budgets and forecasts, and drive performance through our management compensation program.

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These measures are not recognized measures under IFRS, do not have a standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other companies. Rather, these measures are provided as additional information to complement those IFRS measures by providing further understanding of our results of operations from management's perspective. Accordingly, these measures should not be considered in isolation nor as a substitute for analysis of our financial information reported under IFRS. Reconciliation of these measures to IFRS can be found in the "Review of Non-IFRS Measures" section of this MD&A.

### Adjusted Net Income

Adjusted net income is defined as net income or loss for the period adjusted for the impact of impairment charges related to intangibles, property, plant and equipment and investments; acquisitions/disposition gains or losses and related transaction costs; significant tax adjustments; unrealized gains or losses on derivative instruments; remeasurement impacts related to employee benefit commitment obligations; adjustment for other significant non-routine, non-recurring and/or non-cash items; and the tax effect of the adjusted items. In this MD&A, the Company adjusted for the following non-routine, non-recurring, and/or non-cash items: (i) unrealized loss from commodity-based swaps, (ii) remeasurement of employee benefit commitment, (iii) restructuring costs, and (iv) separation costs related to United States Steel Corporation (USS) support services. Management believes adjusting net income by excluding the impact of specified items may be more reflective of ongoing operational results and uses this measure internally to assist with the planning and forecasting of future operating results. Management is of the view that adjusted net income is a useful measure of our performance because the aforementioned adjusting items do not reflect the underlying operating performance of our core business and are not necessarily indicative of future operating results. Adjusted net income is intended to provide additional information only and does not have a standardized definition under IFRS and therefore may not be comparable to similar measures presented by other companies.

### Adjusted EBITDA

Adjusted EBITDA is defined as net income or loss for the period before finance costs, finance income, income tax expense, depreciation and amortization and the impact of certain non-routine, non-recurring, and/or non-cash items. In this MD&A, the Company adjusted for the following non-routine, non-recurring, and/or non-cash items: (i) unrealized loss on commodity-based swaps, (ii) remeasurement of employee benefit commitment, (iii) restructuring costs, and (iv) separation costs related to USS support services. Adjusted EBITDA is used by management, investors, and analysts to measure operating performance of the Company and is a supplement to our consolidated financial statements presented in accordance with IFRS. Adjusted EBITDA is a helpful measure of operating performance before non-operating financial items such as finance costs, finance income and income tax expense, as well as depreciation, which are non-cash expenses. Adjusted EBITDA also removes the impact of certain non-routine, non-recurring, and/or non-cash items to enable management, investors and analysts to gain a clearer understanding of the underlying financial performance of the Company. Adjusted EBITDA is also helpful to facilitate comparison of operating performance on a consistent basis from period-to-period and to provide a more complete understanding of factors and trends impacting our business. While management considers Adjusted EBITDA a meaningful measure for assessing the underlying financial performance of the Company, Adjusted EBITDA is a non-IFRS measure and does not have a standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other companies.

### Adjusted EBITDA per net ton

We monitor Adjusted EBITDA per nt, defined as Adjusted EBITDA (defined above) divided by Shipping Volume (defined below), as a key indicator of performance during the period. Generally, Adjusted EBITDA per nt is used by management, investors, and analysts to measure profitability on a per unit basis, while excluding the impacts of finance costs and finance income, income tax expense, depreciation, as well as the impacts of certain non-routine, non-recurring, and/or non-cash items. Adjusted EBITDA per nt is also helpful to facilitate comparison of per unit profitability on a consistent basis from period-to-period and to provide a more complete understanding of factors and trends impacting our business. Adjusted EBITDA per nt is a non-IFRS measure and does not have a standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other companies.

### Selling Price per net ton

We believe another key measure of performance is Selling Price per nt, which is defined as revenue from steel products divided by nt shipped in the period. Starting in the second quarter of 2018, we have modified the revenue component (or numerator) of the Selling Price per net ton measure to only include revenue from steel products. Previously, Selling Price per net ton included total revenue, which comprised of both revenue from steel products and non-steel products. We believe this change provides a greater level of consistency with total shipments (or denominator) of Selling Price per net ton, which only includes shipment of steel products during the period. The prior periods have been restated to reflect the change in presentation.

Selling Price per nt is used by management, investors, and analysts to measure sales price on a per unit basis. Selling Price per nt is helpful in isolating a key driver in the generation of revenue, selling price, and helps facilitate the comparison of sales performance relative to peers. Selling Price per nt is also helpful in comparing performance from period-to-period and understanding factors and trends impacting our business. Selling Price per nt is a non-IFRS measure and does not have a standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other companies.

### Shipping Volume

Shipping volume represents the total volume of steel products shipped in the respective period measured in nt. Steel product shipments include hot-rolled, cold-rolled and coated coils, as well as other steel products. Other steel product shipments include non-prime steel products such as secondary steel and scrap. Shipping Volume is used by management, investors, and analysts



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to measure quantities of products sold in the period and isolate a key element in the generation of revenue. Measuring Shipping Volume helps facilitate comparison of sales performance relative to peers and comparison of performance from period-to-period. It also provides a more complete understanding of factors and trends impacting our business. Shipping Volume is a non-IFRS measure and does not have a standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other companies.

### Selected Financial Information

The following table provides selected information for the period as indicated:

(millions of Canadian dollars, except where otherwise noted)	Three months ended June 30, 2018	Six months ended June 30, 2018
<b>Financial results</b>		
Total revenue	\$ 711	\$ 1,193
Gross profit	177	247
Selling, general and administration expenses	15	27
Net income (loss)	(11)	18
Adjusted net income <sup>1</sup>	154	204
Adjusted EBITDA <sup>1</sup>	174	243
<b>Operating Results</b>		
Selling price per nt (in dollars per nt) <sup>1</sup>	898	837
Adjusted EBITDA per nt (in dollars per nt) <sup>1</sup>	233	179
Shipping volumes (in thousands of nt)	748	1,361
Hot-rolled	590	1,081
Coated	93	177
Cold-rolled	33	48
Other	32	55
As at	June 30, 2018	December 31, 2017
<b>Financial position</b>		
Total assets	\$ 1,492	\$ 1,223
Total non-current liabilities	508	352

<sup>1</sup> The definition and reconciliation of these non-IFRS measures are included in the 'Non-IFRS Performance Measures' and 'Review of Non-IFRS Measures' sections of this MD&A.

### Review of Financial Results

#### Revenue

The majority of our revenue from the sale of goods is derived from hot-rolled, cold-rolled and coated steel products. A substantial portion of the Company's revenue is derived from spot sales rather than through fixed-price contracts with customers. In addition, other product sales such as coke, iron ore fines, and by-products (tar, ammonia and light oil) are included in revenue. Our revenues include customers from the steel service centres, construction, energy, automotive and appliance industries across Canada and the United States.

Revenue was impacted by increases in shipping volumes for our steel products, non-steel sales and a general improvement in the market price of steel during the first and second quarter of 2018 which reflects macroeconomic conditions around supply and demand for steel products.

#### Gross profit

Gross profit reflects revenue less cost of goods sold. Cost of goods sold includes product-related costs, labour costs, employment benefits and other operating costs such as repairs and maintenance, and depreciation.

Our gross profit for the period was impacted by higher revenues, partially offset by an increase in cost of goods sold attributed to an increase in raw material, tariffs and freight costs, and higher shipping volumes.

Included in gross profit for the six months ended June 30, 2018, is the impact of a \$6 million inventory revaluation adjustment which relates to inventory costs included in cost of goods sold that had been recorded in a period prior to 2018. The impact of this adjustment increased the carrying value of the Company's inventory with a corresponding decrease to cost of goods sold in the current period.

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### Selling, general and administrative expenses

Our SG&A expenses are predominantly comprised of corporate functions, and include employee salary and benefits, marketing, professional and legal fees, travel, and other expenses related to the corporate infrastructure required to support our business. SG&A costs also include expenses associated with establishing and enhancing support functions and information systems that have historically been provided to Stelco by USS, such as costs related to implementing our new cloud-based Enterprise Resource Planning (ERP) system, which is expected to be completed by the end of 2018.

(millions of Canadian dollars)	Three months ended June 30, 2018	Six months ended June 30, 2018
ERP	\$ 6	\$ 10
Employee salary and benefits expense	4	8
Professional, consulting and legal fees	2	5
Management fees	1	2
Other	2	2
	<b>\$ 15</b>	<b>\$ 27</b>

#### Q2 2018

SG&A expenses for the three months ended June 30, 2018 primarily include the following: \$6 million in ERP implementation expenses relating to the separation from USS, \$4 million in employee salary and benefits and \$2 million in professional, consulting and legal fees. Costs related to the establishment of our new cloud based ERP system do not qualify as a software intangible because the arrangement is a cloud-based hosting license.

#### YTD 2018

SG&A expenses for the six months ended June 30, 2018 primarily include the following: \$10 million in ERP implementation expenses relating to the separation from USS, \$8 million in employee salary and benefits and \$5 million in professional, consulting and legal fees.

### Finance costs

(millions of Canadian dollars)	Three months ended June 30, 2018	Six months ended June 30, 2018
Remeasurement of employee benefit commitment <sup>1</sup>	\$ 157	\$ 161
Accretion of employee benefit commitment	10	19
Interest on loans and borrowings	2	4
Accretion on financial lease obligation	—	1
Foreign exchange loss	1	1
	<b>\$ 170</b>	<b>\$ 186</b>

1. Remeasurement of employee benefit commitment for change in the timing and magnitude of estimated cash flows and future funding requirements.

The Company's employee benefit commitment obligation is measured based on using a discounted cash flow analysis of expected cash flows to be paid in future periods to the independent pension and OPEB trusts that were established upon the Company's emergence from CCAA.

In connection with the Amended OPEB Funding Agreement (discussed further in the 'Business Overview' section of this MD&A), Stelco incurred a remeasurement charge of \$157 million related to the employee benefit commitment, derived as the difference between the estimated discounted cash flows from the Original OPEB Funding Agreement compared to those from the Amended OPEB Funding Agreement. The employee benefit commitment (including both the Original and Amended OPEB Funding Agreements) consists of contractually fixed payments as well as estimated payments that have been determined using management estimates of Stelco's future operating performance. Due to the nature of the underlying estimates, assumptions and its long-term nature, the employee benefit commitment is sensitive to changes in these estimates and assumptions. Estimates of expected cash flows are revisited at the end of each reporting period to determine the carrying amount of amortized cost. Refer to note 6 of the Consolidated Financial Statements for further details.

In addition, during March 2018, the Company paid a \$20 million advance contribution pursuant to the Original OPEB Funding Agreement, that was estimated as at December 31, 2017 to be paid during the year 2020. As a result of this accelerated payment and the impact to the present value of the employee benefit commitment, the Company recognized an increase of \$4 million to the liability with a corresponding increase in finance costs on the consolidated statement of income.

### Other loss

Other loss primarily includes a \$10 million realized loss from commodity based swaps. During the first quarter of 2018, the Company entered into commodity-based swaps as part of a strategy to mitigate Stelco's exposure to hot-rolled coil steel market price fluctuations in anticipation of certain slab purchases from a third party, which did not occur. These swap contracts matured and settled during May 2018. The Company did not enter these contracts for trading or speculative purposes.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Restructuring

As a result of the CCAA proceedings, Stelco incurred restructuring and other costs in 2014 through to 2018. The expenses primarily included legal fees and other related restructuring expenses.

(millions of Canadian dollars)	Three months ended June 30, 2018	Six months ended June 30, 2018
Consulting costs <sup>1</sup>	\$ —	1
Legal costs <sup>1</sup>	1	1
Other	1	3
	\$ 2	5

1. Consulting and legal costs are expected to continue during 2018.

### Review of Non-IFRS Measures

#### Adjusted net income

The following table provides a reconciliation of net income (loss) to adjusted net income:

(millions of Canadian dollars, except where otherwise noted)	Three months ended June 30, 2018	Six months ended June 30, 2018
<b>Net income (loss)</b>	\$ (11)	\$ 18
Add back/(Deduct):		
Remeasurement of employee benefit commitment <sup>1</sup>	157	161
Separation costs related to USS support services <sup>2</sup>	6	10
Restructuring costs <sup>3</sup>	2	5
Realized loss from commodity-based swaps	—	10
<b>Adjusted net income</b>	\$ 154	\$ 204

1. Remeasurement of employee benefit commitment for change in the timing of estimated cash flows and future funding requirements.
2. Includes ERP implementation costs associated with the process of separating from USS, management fees and shared services arrangement costs.
3. Restructuring expenses relates to the CCAA proceedings, which primarily included legal fees and other related restructuring expenses. The Company implemented its CCAA plan on June 30, 2017.

Included in adjusted net income for the six months ended June 30, 2018 is the impact of a \$6 million inventory revaluation adjustment which relates to inventory costs included in cost of goods sold that had been recorded in a period prior to 2018. The impact of this adjustment increased the carrying value of the Company's inventory with a corresponding decrease to cost of goods sold in the period.

#### Adjusted EBITDA

The following table provides a reconciliation of net income (loss) to Adjusted EBITDA:

(millions of Canadian dollars, except where otherwise noted)	Three months ended June 30, 2018	Six months ended June 30, 2018
<b>Net income (loss)</b>	\$ (11)	\$ 18
Add back/(Deduct):		
Finance costs	170	186
Depreciation	7	14
Separation costs related to USS support services <sup>1</sup>	6	10
Restructuring costs <sup>2</sup>	2	5
Realized loss from commodity based swaps	—	10
<b>Adjusted EBITDA</b>	\$ 174	\$ 243
<b>Adjusted EBITDA as a percentage of total revenue</b>	24%	20%

1. Includes ERP implementation costs associated with the process of separating from USS, management fees and shared services arrangement costs.
2. Restructuring expenses relates to the CCAA proceedings, which primarily included legal fees and other related restructuring expenses. The Company implemented its CCAA plan on June 30, 2017.

Included in adjusted EBITDA for the six months ended June 30, 2018 is the impact of a \$6 million inventory revaluation adjustment which relates to inventory costs included in cost of goods sold that had been recorded in a period prior to 2018. The impact of this adjustment increased the carrying value of the Company's inventory with a corresponding decrease to cost of goods sold in the period.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Review of Balance Sheets

The following table provides selected balance sheet information as indicated:

(millions of Canadian dollars)

As at	June 30, 2018	December 31, 2017
Cash and cash equivalents	\$ 421	\$ 250
Trade and other receivables	263	204
Inventories	380	448
Property, plant and equipment	382	279
<b>Total assets</b>	<b>\$ 1,492</b>	<b>\$ 1,223</b>
Trade and other payables	332	309
Other liabilities	47	68
Obligations to independent employee trusts	606	344
<b>Total liabilities</b>	<b>\$ 992</b>	<b>\$ 726</b>
<b>Total equity</b>	<b>\$ 500</b>	<b>\$ 497</b>

As reflected in the selected balance sheet information above, between December 31, 2017 and June 30, 2018, the Company increased trade and other payables from \$309 million to \$332 million (an increase of \$23 million, or 7%), reduced other liabilities from \$68 million to \$47 million (a reduction of \$21 million, or 31%), increased total liabilities from \$726 million to \$992 million (an increase of \$266 million, or 37%), and increased total equity from \$497 million to \$500 million (an increase of \$3 million or 1%).

In addition, our inventory decreased from \$448 million at December 31, 2017 to \$380 million at June 30, 2018, primarily due to a decrease in raw material levels resulting from the production of steel and higher shipping volume activity in connection with steel product sales during the period.

During the first half of 2018, the Company repaid a net amount of approximately \$32 million of the amounts drawn under the inventory monetization arrangement. Changes in the carrying amounts are primarily repayments related to receipts and consumption of raw materials by Stelco Inc. monetized under this arrangement. As at June 30, 2018, amounts drawn under this arrangement had a carrying value of \$93 million compared to \$121 million as at December 31, 2017.

The obligations to independent employee trusts increased from \$344 million at December 31, 2017 to \$606 million at June 30, 2018 primarily due a \$148 million increase in the employee benefit commitment and a new mortgage payable of \$114 million in connection with the acquisition of the Lands. The increase in the employee benefit commitment is primarily due to a remeasurement charge of \$157 million recorded in finance costs for the period in connection with Stelco Inc. entering into an amended OPEB funding agreement. The Amended OPEB Funding Agreement reduced the Company's exposure to future variable funding requirements, and provided the OPEB trusts with an increased fixed funding commitment over a 25 year term. Refer to the '*Business Overview*' and '*Review of Quarterly Financial Results - Finance Costs*' sections in this MD&A for further details.

We expect our cashflow from operations to be favourably impacted in the short to medium term due to substantial tax attributes which, as at June 30, 2018, can shield pre-tax income of approximately \$984 million (or approximately \$246 million on an after tax basis) from taxation. These tax attributes consist of non-capital loss carry forwards of \$626 million (\$156 million after tax), undepreciated capital cost deductions (UCC) deductions of \$322 million (\$81 million after tax) and scientific research and experimental development (SRED) deductions of \$36 million (\$9 million after tax), which are expected to reduce the amount of taxes otherwise payable by Stelco Inc. and form part of future deposits into the independent employee life and health benefit trusts (ELHTs). Refer to '*Commitments and Contingencies - Employee Benefit Commitments*' section in this MD&A for further details.

### Results of Operations

Stelco continues to experience improving market conditions and favourable pricing trends across its key products. Steel prices continued to increase during the first half of 2018 and remain influenced by overall international demand, trade sanctions, iron ore prices, scrap steel prices and product availability. Volatile metal prices may cause fluctuations in our financial results. We've realized higher steel shipping volumes during the quarter and have also sold excess coke to third parties. This created additional revenue and improved our costs as a result of operating leverage.

During the first quarter of 2018, Stelco was impacted by a truck and driver shortage across North America which resulted in higher transportation costs for the Company during the period. In addition, winter weather conditions made certain shipping options impractical for the first three months of 2018. As a result, in order to support our current production levels and higher customer orders, the Company expanded its distribution capabilities by adding approximately 220 rail cars to its transportation fleet through leasing arrangements. These rail cars were mostly received and entered into service during the second quarter of 2018, and we expect to add approximately 160 additional rail cars during the second half of the year. Each rail car is capable of carrying up to 90 nt of steel compared to the typical freight truck which is capable of carrying up to 30-60 nt of steel depending on the jurisdiction traveled. Furthermore, we have increased our shipping capacity through our LEW dock enhancement project which was completed in May 2018. Barges capable of being loaded from our LEW dock are typically capable of carrying between 8 to 12 thousand nt of steel and vessels up to 20 thousand nt of steel. These shipping enhancements contributed in reducing our inventory backlog from

## MANAGEMENT'S DISCUSSION AND ANALYSIS

the first quarter, which in combination with consistent market demand for our steel products, impacted our estimated delivery lead time from eight to ten weeks from the date of order in the first quarter to five to seven weeks at the date of this MD&A.

We executed a number of strategic outages during the first half of 2018, including at our hot strip mill. The outages were intended to improve reliability and efficiency, and are in preparation for hot strip mill enhancements planned for the second half of 2018 and 2019. In connection with our strategic capital expenditure program aimed at improving our product mix to focus on more advanced steel products, including AHSS and UHSS grades, we are planning to continue enhancing our production capabilities and controls over our hot rolled steel products. In that regard and as planned, during September we will be taking a strategic outage to upgrade our hot strip mill. The upgrades will provide for better gauge control and increased rolling force. These enhancements will enable us to better participate in the AHSS, High Strength Low Alloy (HSLA), and value added coated markets. Despite the outage, we still expect second half shipping volumes to be in line with first half shipping volumes, subject to timing differences between the third and fourth quarters.

Also, we continued to focus on business strategies of asset optimization and expansion of our product capabilities through initiatives such as: utilizing excess capacity at our LEW's hot strip mill and pickle lines and HW's coke ovens, restarting HW's temper mill and installing annealing furnaces, and upgrading finishing mill roll bearings at our hot strip mill. We expect that successful completion of these initiatives will ultimately help us grow our revenues, improve our steel production capabilities and lower our total costs per nt. We anticipate that these initiatives will be completed during 2019.

The Company remains committed to focus on maximizing profits, including regaining higher margin business, increasing its expansion into additional markets outside Canada with respect to hot-rolled, cold-rolled and coated coil sales, and assessing opportunities to introduce new products. Despite the recent tariffs introduced by the US administration, Stelco as a low cost leading advanced integrated steel producer in North America, with improved shipping and production capabilities, will continue to seek new opportunities in the domestic and international steel markets and expects to continue to maximize profitability and cash flows in the near term.

### Capital Resources and Liquidity

The liquidity and capital resources of the Company are dependent upon a number of factors including, without limitation, market and economic conditions and the impact of these conditions on the price of steel products, raw material costs, the ability to fund necessary capital projects, pension and OPEB funding requirements and labour negotiations and disputes.

Our principal uses of funds are for operating expenses, capital expenditures, finance costs, and debt service. Management believes that cash generated from operations, together with amounts available under our ABL credit facility and inventory monetization arrangement, will be sufficient to meet our future operating expenses, capital expenditures, future debt service costs, and support the growth of our business (primarily through working capital and capital expenditures), repay short-term obligations and for general corporate purposes.

Our ability to fund future operating expenses, capital expenditures and debt service costs will depend on our future operating performance which may be affected by general economic, financial and other factors including factors beyond our control. From time to time, our management team reviews acquisition opportunities and, if suitable opportunities arise, may make selected acquisitions to implement our business strategy.

The Company has a significant requirement for working capital related primarily to inventories due to the lead time of acquiring raw materials, the quantities of raw materials that are required to produce semi-finished steel and the amount of time required to process this semi-finished steel into a finished product. This working capital requirement is characteristic of many companies within the steel industry.

The Company expects to have sufficient working capital for the remainder of 2018 based on the following:

- the Company's overall working capital position was significantly improved because of the CCAA restructuring;
- the Company has negotiated favourable payment terms with its vendors, thereby improving its working capital without the need for additional funding;
- as at June 30, 2018, Stelco Inc. had approximately \$268 million available under the ABL credit facility;
- the inventory monetization arrangement continues to provide Stelco Inc. liquidity on certain of its raw material purchases;
- as at June 30, 2018, Stelco Holdings had a cash balance of approximately \$421 million, a portion of which could be made available to Stelco Inc. for general corporate purposes and working capital.

### Credit Facility and Other Arrangements

#### ABL Credit Facility

In connection with Stelco Inc.'s emergence from CCAA, Stelco Inc. entered into an asset-based revolving loan agreement on June 30, 2017 with a syndicate of lenders for a maximum revolver amount of \$375 million. The amount available to be drawn under the ABL credit facility will vary from time to time, based upon a borrowing base determined with reference to Stelco Inc.'s trade receivables and certain inventory balances. At June 30, 2018, the available borrowing base was \$268 million. The interest on Canadian/US dollar denominated funds is the Canadian/US prime rate plus 1% - 1.5%, depending on the amount that has been drawn under the facility, and is payable monthly. Stelco Inc. also has the option to index the interest rate to CDOR/LIBOR plus a margin of 2% - 2.5%, and may elect this in the event that it results in a lower rate of interest on its draws under the revolver. Additionally, Stelco Inc. is subject to payment of an unused line fee ranging from 0.25% - 0.375% of the unused portion of the revolver, depending on



## MANAGEMENT'S DISCUSSION AND ANALYSIS

the amount undrawn, and is payable monthly. Stelco Inc. can obtain letters of credit under the facility at a rate of 2% - 2.5%. Stelco Inc. has letters of credit outstanding as at June 30, 2018 in the amount of \$36 million. During the six months ended June 30, 2018, Stelco Inc.'s borrowing and repayment activity on the ABL facility resulted in a nil outstanding balance as at June 30, 2018.

### Inventory Monetization Arrangement

On December 11, 2017, Stelco Inc. entered into an inventory monetization arrangement which is subject to a financing rate of LIBOR plus a margin of 3.5%. Under the terms of the arrangement, Stelco Inc. receives cash proceeds based upon an agreed pricing formula and the quantity of certain raw materials on-site, less a required cash margin. Currently, iron ore and metallurgical coal inventory are monetized under the arrangement up to a specified maximum volume. Upon consumption of the raw materials, amounts monetized under the arrangement are repaid to the counterparty. Any amount remaining outstanding under the arrangement in respect of raw material inventory that is not consumed during the term, is due and payable on October 31, 2018 with an option to terminate the arrangement earlier, on either August 31, 2018 or September 28, 2018. The arrangement also provides the parties an option to renew the agreement for additional one-year terms, subject to both parties electing to renew.

Cash amounts advanced under this arrangement represent a financial liability to the Company which is recorded within other payables on the Company's statement of financial position. As at June 30, 2018, amounts advanced under this arrangement were \$93 million compared to \$121 million as at December 31, 2017.

### Share Capital

The Company's authorized share capital includes an unlimited number of common shares with no par value and an unlimited number of preferred shares issuable in series. No additional shares were issued during the six months ended June 30, 2018. Refer to note 7 of the Consolidated Financial Statements for further details.

### Dividend Policy

The Company's primary objective is to deploy capital in a disciplined manner that creates value for our shareholders. We plan to evaluate our capital allocation policies on an on-going basis to ensure that we are maximizing returns for our shareholders. These policies may include initiating payment of a dividend on our common shares at some point in the future. Any determination to pay dividends in the future will be at the discretion of our Board of Directors and will depend on many factors, including, among others, our financial condition, current and anticipated cash requirements, contractual restrictions and financing agreement covenants, solvency tests imposed by applicable corporate law and other factors that our Board of Directors may deem relevant.

In accordance with the Company's Dividend Policy, Stelco Holdings management and the Board of Directors will regularly review the Company's rate of dividends to ensure an appropriate level of dividends. At its most recent meeting on July 31, 2018, the Board of Directors declared a special dividend of \$1.69 per common share, payable on August 15, 2018 to shareholders of record as of August 10, 2018 and a quarterly cash dividend of \$0.10 per common share, payable on August 17, 2018 to shareholders of record as of August 10, 2018. The dividends have been declared as "eligible dividends" for purposes of the *Income Tax Act* (Canada).

### Commitments and Contingencies

#### Employee Benefit Commitments

- Stelco Inc. has funding commitments with certain pension and OPEB trusts. Stelco Inc. committed to pay up to a maximum of \$430 million to fund five main defined benefit pension plans previously sponsored by Stelco Inc. (Main Pension Plans).
- Stelco Inc. entered into an Amended OPEB Funding Agreement, replacing the Original OPEB Funding Agreement, and committed to fixed contributions of approximately \$494.5 million over twenty five years to the ELHTs created for receiving, holding and distributing funds on account of OPEBs for legacy employees of Stelco Inc. In addition, Stelco Inc. agreed to pay a portion of its free cash flows (as defined) and certain tax-related savings amounts to the ELHTs.
- Bedrock has guaranteed certain minimum contributions to the Main Pension Plans up to a maximum amount of \$160 million. The amount of such guarantee is reduced based upon, among other things, certain contributions being made to the Main Pension Plans over time. The guarantee will be discharged upon the earlier of the \$160 million being reduced to zero or the aggregate amount of all payments made by Stelco Inc. or Bedrock reaching \$300 million.
- Certain components of the employee benefit commitments are tied to Stelco Inc.'s future cash flow generation and certain tax-related savings amounts. The carrying value of the employee benefit funding commitment liability recognized by the Company in its consolidated balance sheet is determined based upon the present value of those future payments as estimated by management. Changes in the magnitude or timing of those estimated future cash payments may result in the employee benefit commitment liability balances being adjusted upward or downward in future periods. If such adjustments to the liability carrying value were to occur, the Company would also recognize a corresponding expense item in its consolidated statements of income as an element of finance cost. Management will assess estimates of future cash flows related to these employee benefit funding arrangements each period.

#### Other Commitments

- Iron Ore Contract - Stelco Inc. committed to purchasing all of its iron ore requirements up to a specified amount from USS through the 2021 shipping season.
- Transition Services Agreements - USS agreed to continue to provide certain business and transition services to Stelco Inc. for a maximum term expiring no later than June 30, 2019.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

- Union Agreements - Stelco Inc. has collective bargaining agreements with USW Local 8782, USW Local 8782(b) and USW Local 1005, each for a term of 5 years ending July 1, 2022.

### Operating Leases

The Company has operating leases on certain machinery and equipment, with lease terms between three and five years. Additionally, in connection with the Stelco Inc.'s emergence from CCAA, Stelco Inc. sold and leased back the land on which HW and LEW are situated under a 25 year lease. In connection with the Lands acquisition on June 5, 2018, the HW and LEW land leases were terminated and the associated rental payments were cancelled. Refer to note 4 of the Consolidated Financial Statements for further details.

### Finance Leases

As at June 30, 2018, the Company has a finance lease obligation with a carrying value of \$5 million (December 31, 2017 - \$25 million) associated with certain equipment and buildings on its consolidated balance sheets. During the second quarter of 2018, Stelco Inc. acquired the Lands from the Land Vehicle resulting in the derecognition of the Company's building finance lease obligation of \$24 million. Refer to note 4 of the Consolidated Financial Statements for further details.

### Claims and litigation

The Company is involved in various claims and litigation arising in the normal course of business. While the final outcome of such legal proceedings and actions cannot be predicted with certainty, it is the opinion of management that the resolution of such proceedings and actions will not have a material impact on the Company's consolidated balance sheets, results of operations, or cash flows.

### Contractual Obligations

The following table sets out a summary of our future contractual obligations as at June 30, 2018:

(millions of Canadian dollars)	Payments due by period			
	Total	2018 <sup>3</sup>	2019 to 2022	Thereafter
Trade payables	\$ 234	\$ 234	\$ —	\$ —
Inventory monetization arrangement	93	93	—	—
Operating leases	8	3	5	—
Finance lease obligations	6	—	2	4
Purchase obligations - non-capital <sup>1</sup>	618	403	137	78
Purchase obligations - capital	30	30	—	—
Obligations to independent employee trusts <sup>2</sup>	1,219	26	354	839
<b>Total Contractual Obligations</b>	<b>\$ 2,208</b>	<b>\$ 789</b>	<b>\$ 498</b>	<b>\$ 921</b>

<sup>1</sup> Purchase Obligations — non-capital includes contractual commitments for the purchase of raw materials, energy and material processing.

<sup>2</sup> Represents estimated undiscounted obligations to independent employee trusts.

<sup>3</sup> Amounts pertain to the remaining six months of 2018.

The Company's contractual obligations can be funded by existing cash on hand, cash flow from operations, our inventory monetization arrangement and ABL credit facility.

### Related Party Transactions

Parties are considered to be related if one party has the ability to control, jointly control or exercise significant influence over the other party in making financial or operating decisions. The definition includes subsidiaries, joint ventures, investments in associates, among other entities and persons.

Upon being acquired on June 30, 2017, Stelco Inc. became a related party of Bedrock. Stelco Inc. has executed a management services agreement with an affiliate of Bedrock under which Stelco Inc. will receive senior management, commercial, business development, operating, financial, human resources, and executive recruitment services, as well as other services that may be required from time to time. Fees for services will be based upon actual costs incurred by Bedrock, plus a 2% mark-up on management services fees up to \$5 million, and any services above \$5 million will be reimbursed at cost. As at June 30, 2018, Stelco Inc. has payables related to Bedrock of \$1 million. The Company has incurred expenses of \$2 million in management services provided by Bedrock and its affiliated entities for the six months ended June 30, 2018.

### Subsidiaries

Transactions between Stelco Holdings and its subsidiaries meet the definition of related party transactions. These transactions are eliminated on consolidation and are not disclosed in these consolidated financial statements.

### Key Management Personnel

The Company's key management personnel, and persons connected with them, are also considered to be related parties for disclosure purposes. Key management personnel are defined as those individuals having authority and responsibility for planning, directing and controlling the activities of Stelco and comprise the Executive Senior Leadership Team (ESLT). Effective July 1, 2017,

## MANAGEMENT'S DISCUSSION AND ANALYSIS

the ESLT is comprised of the Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Executive Vice-President, and General Counsel & Corporate Secretary of the Company.

During the three and six months ended June 30, 2018, the Company recorded \$1 million and \$2 million, respectively, as an expense related to key management personnel salaries and benefits, post-employment pension, medical and termination benefits.

### **Deferred Share Unit Plan**

The Company has a deferred share unit (DSU) plan for its independent directors which provides that each independent director receives, on each date that the director fees are payable, an amount of DSUs which the director has elected. Each independent director can elect annually a specified percentage of director fees or compensation as DSUs. The number of DSUs granted to an independent director is based on the closing price of the Company's common shares on the Toronto Stock Exchange on the grant date. At such time as an independent director ceases to be a director, the Company will make a cash payment on the outstanding DSUs. As of June 30, 2018, there were 7,507 DSUs outstanding, for which the Company recognized a liability of \$0.2 million.

### **Significant Accounting Policies**

Stelco Holdings' Consolidated Financial Statements have been prepared by management in accordance with IAS 34, *Interim Financial Reporting*, as issued by the International Accounting Standards Board (IASB). The consolidated financial statements comprise the financial statements of Stelco Holdings and its subsidiaries (collectively the Company). Under International Financial Reporting Standards (IFRS), additional disclosures are required in the annual financial statements and therefore, the Consolidated Financial Statements and accompanying notes should be read in conjunction with the notes to Stelco Holding's audited Consolidated Financial Statements for the six month period ended December 31, 2017 (2017 Annual Financial Statements).

The Consolidated Financial Statements have been prepared using consistent accounting policies and methods used in the preparation of the Company's 2017 Annual Financial Statements, with the exception of the accounting policies impacted by the adoption of new standards and interpretations effective January 1, 2018, as noted below. Certain comparative information has been reclassified to conform to the current period's presentation.

### **Change in accounting policies**

Stelco has adopted each of the standards and policies noted below on January 1, 2018:

#### **a) IFRS 15 - Revenue from Contracts with Customers (IFRS 15)**

IFRS 15 establishes a five-step model to account for revenue arising from contracts with customers and outlines two approaches to recognizing revenue: at a point in time or over time. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized. Under IFRS 15, revenue is recognized at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The Company has adopted the new standard using the modified retrospective application method with no restatement of comparative information. The adoption did not have an impact on the Consolidated Financial Statements.

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured, regardless of when the payment is received. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes and certain duties. The Company recognizes revenue as a principal in all of its revenue arrangements since it is the primary obligor in all the revenue arrangements, has pricing latitude, and is also exposed to inventory and credit risks.

Revenue from the sale of goods includes sale of goods from the Company's production of steel products. Revenue from the sale of goods is recognized when the performance obligation is satisfied by transferring the promised good to a customer. A good is considered transferred when the customer obtains control, which is defined as the ability to direct the use of and obtain substantially all of the remaining benefits of an asset. Revenue from sale of goods under bill and hold arrangements is recognized when the buyer obtains control of the goods and the following criteria are met: the reason for the bill and hold arrangement is substantive, the product can be separately identifiable as belonging to the customer, the item is ready for delivery, the Company does not have the ability to use the product or direct it to another customer, and the usual payment terms apply.

Revenue from the sale of products is measured at the fair value of the consideration received or receivable, net of returns and allowances, trade discounts, volume rebates and other incentives. Shipping and other transportation costs charged to buyers are recorded in sales and the related costs recorded in cost of goods sold.

#### **b) IFRS 9 - Financial instruments (IFRS 9)**

IFRS 9 introduced new requirements for the classification, measurement impairment of financial instruments as well as hedge accounting. The Company adopted the new standard using the modified retrospective application method with no restatement of comparative information. The adoption did not have an impact on the Consolidated Financial Statements.

Stelco's financial assets and liabilities (financial instruments) include cash and cash equivalents, restricted cash, trade and other receivables, derivative financial instruments, trade and other payables, long-term debt, as well as employee benefit commitments.

The classification of financial instruments is typically determined at the time of initial recognition, within the following categories:

- Amortized cost
- Fair value through income or loss
- Fair value through other comprehensive income

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### *Financial instruments carried at fair value through income or loss*

Financial instruments in this category include derivative financial instruments which are presented on the consolidated balance sheets as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

### *Financial instruments carried at amortized cost*

Financial instruments in this category include cash and cash equivalents, trade and other receivables, trade and other payables, long-term debt and the employee benefit commitment. Financial instruments are recorded initially at fair value and, in the case of financial assets and liabilities carried at amortized cost, adjusted for directly attributable transaction costs.

Trade and other receivables include originated and purchased non-derivative financial assets with fixed or determined payments that are not quoted in an active market and are subsequently measured at amortized cost and is computed using the effective interest method less any allowance for impairment.

Trade and other payables, long-term debt (including the current portion of long-term debt), the employee benefit commitment, as well as the finance lease obligations, are subsequently measured at amortized cost using the effective interest rate method. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees. The effective interest rate accretion is included as finance costs in the consolidated statements of income.

### *Impairment of financial assets carried at amortized cost*

Trade and other receivables are subject to lifetime expected credit losses (ECL) which are measured as the difference in the present value of the contractual cash flows that are due under the contract, and the cash flows that are expected to be received. The Company applies the simplified approach at each reporting date on its trade and other receivables and considers current and forward-looking macro-economic factors that may affect historical default rates when estimating ECL.

Financial assets, together with the associated allowance, are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Company. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or decreased by adjusting the carrying value of the loan or receivable. If a past write-off is later recovered, the recovery is recognized in the consolidated statement of income.

## **Future Changes in Accounting Policies**

Stelco monitors the potential changes proposed by the IASB and analyzes the effect that changes in the standards may have on its operations.

Standards issued but not yet effective up to the date of issuance of these Consolidated Financial Statements are described below. This description is of the standards and interpretations issued that the Company reasonably expects to be applicable at a future date. Stelco intends to adopt these standards when they become effective.

### **IFRS 16 - Leases (IFRS 16)**

IFRS 16 introduces a single, on-balance sheet accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard - i.e. lessors continue to classify leases as finance or operating leases. IFRS 16 replaces existing leases guidance including IAS 17, *Leases*; IFRIC 4, *Determining Whether an Arrangement Contains a Lease* (IFRIC 4); SIC-15, *Operating Leases - Incentives*; and SIC-27, *Evaluating the Substance of Transactions Involving the legal Form of a Lease*. The standard is effective for annual periods beginning on or after January 1, 2019. Obligations under operating leases and related right of use assets will be recorded on the Consolidated Balance Sheets. To assess the impact of this new standard, the Company has formed an internal working group and continues to progress on its in-depth assessment. The Company expects to report more detailed information, including estimated quantitative financial impacts, if material, in its Consolidated Financial Statements as the effective date approaches.

### **IFRIC 23 - Uncertainty over Income Tax Treatments (IFRIC 23)**

In June 2017, the IASB issued IFRIC 23 to clarify the accounting for uncertainties in income taxes. The interpretation provides guidance and clarifies the application of the recognition and measurement criteria in IAS 12, *Income Taxes*, when there is uncertainty over income tax treatments. The interpretation is effective for annual periods beginning on or after January 1, 2019, and the Company is currently assessing the impact of IFRIC 23 on its Consolidated Financial Statements.

## **Controls and Procedures**

At June 30, 2018, the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) of the Company, together with the assistance of senior management, have designed disclosure controls and procedures to provide reasonable assurance that material information relating to the Company is made known to the CEO and the CFO, and have designed internal controls over financial reporting and disclosure to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with IFRS.

The CEO and CFO are assisted in this responsibility by senior management of Stelco. Stelco's senior management has established procedures so that it becomes aware of any material information affecting the Company in order to evaluate and communicate this information to the CEO and CFO, as appropriate and determine the appropriateness and timing of any required disclosure.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

It should be noted that a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Given the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. These inherent limitations include, among other items: (i) that management's assumptions and judgments could ultimately prove to be incorrect under varying conditions and circumstances; (ii) the impact of any undetected errors; and (iii) controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override.

### **Risk and Uncertainties**

We believe our performance and future success depend on a number of factors that present significant opportunities for us. For a discussion of risk factors that have been identified by the Company refer to the 2017 AIF and the 2017 Annual MD&A and are available through the SEDAR website at [www.sedar.com](http://www.sedar.com).

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## Corporate Information

### Executive Management

**Alan Kestenbaum**  
Chief Executive Officer

**Don Newman**  
Chief Financial Officer

**Sujit Sanyal**  
Chief Operating Officer

**David Cheney**  
Executive Vice-President

**Paul Simon**  
General Counsel & Corporate Secretary

### Board of Directors

**Alan Kestenbaum**  
Executive Chairman and  
Chief Executive Officer for Stelco Holdings  
Inc.

**Michael W. Dees** <sup>4,6</sup>  
Partner, Lindsay Goldberg

**Jeffrey B. Bunder** <sup>2</sup>  
Partner and Chief Financial Officer, Lindsay  
Goldberg

**Alan Goldberg**  
Co-Founder and Chief Executive Officer,  
Lindsay Goldberg

**Brian Levitt** <sup>2,3,6</sup>  
Chairman of the Board of Directors of the  
Toronto-Dominion Bank

**Peter Bowie** <sup>1</sup>  
Corporate Director

**Jacob Lew**  
Partner, Lindsay Goldberg

**Indira Samarasekera** <sup>5</sup>  
Corporate Director

<sup>1</sup> Chair of the Audit Committee.

<sup>2</sup> Member of the Audit Committee.

<sup>3</sup> Chair of the Compensation, Governance and Nominating  
Committee.

<sup>4</sup> Member of the Compensation, Governance and Nominating  
Committee.

<sup>5</sup> Chair of the Environmental, Health and Safety Committee

<sup>6</sup> Member of the Environmental, Health and Safety Committee

### Auditors

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Hamilton, Ontario  
L8P 4W7

**Transfer Agent and Registrar**  
**Computershare Investors Services Inc.**  
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North Tower, Toronto, Ontario M5J 2Y1  
Telephone: 1 (800) 564-6253 or  
(416) 263-9200  
Fax: 1 (888) 453-0330  
Website: [www.computershare.com](http://www.computershare.com)  
Email: [service@computershare.com](mailto:service@computershare.com)

**Stock Exchange Listing**  
**The Toronto Stock Exchange**  
Stelco Holdings Inc. trading symbol: STLC

### Shareholder Information

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### Shareholder and Investor Contact

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Chief Financial Officer  
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