Q2 2021 Earnings Call

Company Participants

- Benjamin Steinbruch, Chairman of the Board, Chief Executive Officer
- Edvaldo A. Rabelo, Cement Director
- Luis Fernando Barbosa Martinez, Executive Officer
- Marcelo Ribeiro, Chief Financial Officer, Investor Relations Officer

Other Participants

- Caio Ribeiro, Analyst
- Carlos De Alba, Analyst
- Daniel Sasson, Analyst
- Leonardo Correa, Analyst
- Thiago Lofiego, Analyst
- Unidentified Participant

Presentation

Operator

Good morning and thank you for waiting. Welcome to CSN's conference call to present the results for the second quarter of 2021. Today we have with us the company's executive officers. We would like to inform you that this event is being recorded and all participants will be in listen-only mode during the company's presentation.

After the company's remarks are over, there will be a question-and-answer session. At that time, further instructions will be given. (Operator Instructions) We have simultaneous webcast that may be accessed through CSN's Investor Relations website at ri.csn.com.br/en/ where the presentation is also available.

The slide presentation may be downloaded from the same website. Please feel free to flip through the slides during the conference call. Before proceeding, we would like to declare that some of the statements herein are mere expectations or trends and are based on the current assumptions and opinions of the company's management, and that future results, performance and events may differ materially from those expressed herein, which do not constitute projections.

In fact, actual results, performance or events may differ materially from those expressed or implied by forward-looking statements. As a result of several factors, such as, the general and economic conditions in Brazil and other countries, interest rates and exchange rate levels, future rescheduling or prepayment of debt, denominated in foreign currencies, protectionist measures in the US, Brazil and in other countries.

Changes in laws and regulations and general competitive factors on a global, regional or national level. Now I will turn the conference over to Mr. Marcelo Ribeiro, Investor Relations Executive Officer, who will present the company's operating and financial highlights for the period.

Please Mr. Marcelo, you may begin your presentation.

Marcelo Ribeiro {BIO 7199930 <GO>}

Good morning, everyone. Thank you for participating in this conference call. This is yet another call in a quarter of very good numbers, very good news. We will start this presentation on page number two with the highlights for the period mentioning a record EBITDA and practically all the financial metrics of the company reached record numbers, except for the net income where the number of quarter one was even higher by the time it was impacted by the IPO of CSN Mineracao.

At this time, it was BRL5 billion of net income and with excellent operational results. It's a historical number. However, it's a short history because with such positive trends in terms of prices and costs we are expecting that the next coming quarters are even better. So this has allowed us to reach some leverage targets that were expected only for the end of the year, but we were able to bring our leverage to very low levels.

We even reduced the net debt to less than BRL15 billion and we inaugurated a new phase in the company's journey. We are now focusing more on capital reallocation so the highlights of this quarter mark the start of this phase with the purchase of a cement plant inaugurating the investment strategy of CSN in this industry. On slide number three, we see the evolution of our EBITDA numbers with the six consecutive quarter of record growth reaching BRL8.2 billion and a margin of 53% and in less than one year, we had an 80% lower EBITDA. So, this growth was achieved in record time and practically in all segments of the company contributing to the positive results of this quarter in particular. And the greatest growth was seen in steel making due to some cost related factors, price related factors. In nominal terms, mining grew more than 1.3 billion and the cement business also reached record numbers in terms of volume, revenues and profitability. So we grew 40% or BRL2.4 billion in one single quarter.

Next page. We have our cash flow indicators with very good news about our CapEx advancement, and it's growing where it needs to grow in mining. This was what was forecast for the year. And in this quarter, we have already delivered the purchase of very important assets such as the magnetic concentrator number three; a project that will allow for improvement in production quality. And we have a guidance for the year of BRL3 billion.

Regarding our net working capital, it grows in the period very much due to the very healthy evolution of prices and volumes. This led us to growth in our stock account and this was partially compensated by the growth of our suppliers and also one event, which was the dividend payout during this period.

On page number five, we see how this is leading to cash generation in our adjusted -- record adjusted cash flow of BRL5.4 billion; also the fifth consecutive quarter of growth. And in this quarter, it reached high levels, despite the impact of the growing CapEx, according to the expectations and also the variation in the working capital and the financial -- one off financial expenses, for example, the ore hedge and other financial operations, such as the bonus we buy -- the bonus buyback.

And on page number six, we see how this very pronounced cash generation resulted in a very fast drop in our net debt in this quarter, also supported by the exchange made, the devaluation of the dollar and valuation of the real -- against the dollar, which brought our debt down to lower levels. And sales of using shares, the BRL1.3 billion is coming from this operation, which compensated the dividend payout of BRL900 million. So, our net debt dropped by 35% in one single quarter reaching below the 15 billion, which was a target, and now we see it as a ceiling of our net debt. And the leverage was also 1.6, also below the new ceiling that we have. A topic that we still have to address is the gross debt, which was BRL35 billion in this quarter, positively impacted in this quarter by the loan with maximum of $350 million to support the growth of the mining business.

On page number seven, we see how the gross debt issue will be addressed in the very short term. Today, we are announcing the buyback of the perpetual bonuses $1 billion or BRL5 billion, which added to the buyback of the bonus from 2023 in the prepayment of banking debts, will allow us to decrease by more than BRL10 billion or gross debt in the next coming months, reinforcing the very responsible capital structure of the company, which has contributed to a very fast increase in our credit ratings, which reached the BB -- and are on the right track for improvement in the future.

Now, I will go over the financial indicators for each segment on page number nine. We have steel and we see that in terms of volume, we sold everything that we had. So, the demand, both from the external and domestic markets, are still very strong. We saw an unexpected recovery, and non-localize recovery, reaching all segments from automotive, civil construction, everything related with agri business and packaging. Martinez will go into more details about the performance of the sector.

But what really contributed to the profitability this quarter was the price evolution, accompanying the international market in the cost evolution in this quarter 26% up, which led the EBITDA to 2.7 billion and a margin of 33%. Regarding our operational performance on page 10, we see this lead production in this quarter was focally impacted by the anticipation of a 60 hour maintenance; that's why we had a slightly lower slab production, And of course, this has an impact on the dilution of fixed costs. But this is a one-off event that we had this quarter, together with increase in price of raw materials such as -- gold and ore. We had an increase of 25% of the cost in reals. This was more than offset by the increase in sales and the increase in the average price of the EBITDA per ton reached 2.107 real, which is a historical record for the company.

Now, for mining, on page 12. We also have a record-breaking quarter supported by good sales volumes, which could even have been better considering that production exceeded the sales and we accumulated stocks due to problems of efficiency that we had this quarter, partially impacted by maintenance and rainfall. So, we had the stock to make the most of this good price moment and we were very positively impacted by an excellent price realization.

There was a 26% increase in our price and the market indicators points at only 20%, which shows the quality of the ore that we sell; that's why our net revenue increased by 34%. The EBITDA increased by 36%, reaching record breaking margins close to 70%. For the cement business, we are also going through a very unique moment. And not just CSN, but the market as a whole is going through a renaissance period with increases year-after-year in the national volumes. Recent data showed that the trend will continue and CSN has reached its maximum production. So, we have capacity of about 4.6 million tons, 4.7 million tons and we are expecting to reach these volumes in the next few quarters. And making the most of the good price increase, the revenues also have reached record numbers with good operational performance and dilution of fixed cost. We reach record margins of 43%, reaching an EBITDA of BRL147 million for the period.

So, these were the operational indicators for each business. And on page 15, we will give you an update about our strategic priorities in the past three or four years. We communicated to the market based on priorities related with an operational turnaround, which we have reached and also a reduction of our debt, which we also were able to achieve.

And now we're turning the page. Now, we will start talking much more about efficient and disciplined capital allocation. So, the cash generation has to be well delivered to generate returns to our shareholders but also conservatively. So, we will always maintain this low leverage below the one-time level. And high liquidity, which has always been a characteristic of CSN. The second pillar is innovation and we're going to show you the progresses that we have been achieving through CSN and over. And third, our ESG agenda, the new pillar, the new ESG pillar, which is gaining traction in our company at very impressive speeds.

So, just a brief update on each of these pillars on page 16. I'll start with our capital allocation. Capital allocation will mean growth with opportunities -- organic growth, in the case of mining. In the case of cement, we will grow through new plants and also sector consolidation. So, in the case of the Elizabeth Cimentos plant, this shows us that we are actually implementing that this capital allocation strategy. It's a modern and integrated plant in the Northeast of the country; a region where we have better prices than in the Southeast, which diversifies our presence and brings us potential synergies, very strong potential synergies. They're related with our strategy, our commercial activities, our differentiators, our capacity to gain scale and reduce costs through working with supplies.

So this demonstrates that we are really willing to grow fast in the cement business. It is still under analysis by the (inaudible), but we expect to have this approval in the next few weeks. Regarding the CSN, another pillar -- one innovation that we have for this quarter is that, first, we have a demonstration of CSN's commitment to innovation by increasing the resources available to this pillar.

So CSN in over had a fund of BRL30 million. And now it has BRL100 million available, considering the very good results of the first initiatives that we have implemented, analyzing startups that could add value to CSN. And the first venture is 2D Materials, company from Singapore, one of the pioneer companies in developing graphene, a material that can be used for several applications, which has a lot of synergy with our steel and cement businesses.

So, the founder of the company got a novel price for he was one of the people responsible for developing graphene, and they are bringing diversified knowledge and expertise. They learn a lot about how to improve their own products and it will allow us to enter new verticals. And as for ESG, I will ask our ESG to talk about key updates in this area.

Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

Good morning, everyone. First of all, we would like to announce the publication of our integrated report for 2020 with a little bit of CSN's history. CSN just celebrated its 80th anniversary. So, this was our first integrated annual report. It brings the largest number of indicators ever reported by CSN and the main events and results of the past year in terms of financial management, economic aspects, environmental aspects of our five segments; mining, logistics, energy, cement. This was outsourced to an independent company.

According to CVM's instruction [ph]14 of 2020 so I invite you all to read the report, which is already available on our platforms on CSN's website. And in this quarter, we also concluded our TCFD. And this is all available in the global aviation records. And this was all prepared according to the [ph] GHD methodology. For the seventh consecutive year, we got the golden stamp. We concluded our disclosure [ph] inside of action -- about our environmental and climate related performance; water capture, supply chain, all this information is also available to our investors through this very important platform; CDP.

In this quarter, we also had the start of the training of our executive officers and other members of the staff. The construction of a risk matrix and climate opportunities matrix, which allows us to venture and incorporate the impact of our climate related initiatives in our financial report. We also have GROUP CLIMA forum with many executives in different areas that will allow us to discuss and supervise implementation of initiatives related with our decarbonization roadmap.

And we are also using an AI tool that creates an imaginary curve showing the results of all -- projected for all projects. So, it allows us to calculate the impact of the emissions that will be avoided. And in the end of this year, we will have new targets, even more ambitious and aggressive targets than what we presented in our initial plan. And also, in addition to what we already said today regarding innovation, we also CSN and CSN Mineracao sign an MOU with Itochu Corporation for a agenda and digital transformation of CSN Mineracao to study and develop new technologies for low carbon steel production through the use of hydrogen and other technologies. So, this has been a very productive quarter, very important quarter for our ESG agenda.

In the safety pillar, I always say that we can't have a good operational result, if we don't have a good safety results. That's why we always talk -- insistent -- and talking about safety. And this has been the best year historically in terms of operational safety. We closed the quarter with very good rates. In the first quarter, we also had the best historical level of our reportable accident rate. We had a slight increase in the quarter two, but we are accumulating a reduction of nearly 9% of year-over-year, and 2020 had already been the best year of the last years with the company.

And we had a significant reduction in the severity rate of these incidents. And despite having a slightly higher number of incidents, they were less severe. So, we closed with a 21.3% reduction in the severity rate of quarter-over-quarter. For dams and water, you know that we are working on this area. And in the first half of the year, we started the works of the Vigia dams build channel. And the contracting of the works for the B4 build channel. And this is also a milestone for the start of the characterization of these two dams. And we have a great indicator, we closed the first half of the year with a reduction of 8% in water capture specifically for steel production. So with the higher production, but without increasing the use of water. And this is a very important indicator considering that CSN has reduced it by 70%, the water consumption for steel production in the past few years.

Social and diversity, we also want to double the number of women in our payroll. We've had a more than 11% increase in female participation in the company. We adhere to MOVE. MOVE is a movement for racial equity; an important initiative. 45 companies from different industries working in favor of racial equity. This should create 10,000 positions for blacks and train 1000 of people by 2030.

So we are advancing fast in our ESG agenda with a lot of initiatives, and we've been the source of all these initiatives as we can see in this slide.

Marcelo Ribeiro {BIO 7199930 <GO>}

Thank you. [ph]Milena And before we open for questions, I would like to hand the conference over to our Chairman and President, Benjamin Steinbruch for his considerations. I think we're having connection problems so I apologize. So, I suggest that we open for questions and maybe Benjamin can join us for the final remarks. Thank you all.

Questions And Answers

Operator

Thank you, ladies and gentlemen, the floor is now open for questions. (Operator Instructions)

The first question is from Daniel Sasson, Itau. Mr. Daniel, you may proceed.

Q - Daniel Sasson {BIO 19234542 <GO>}

Hello, good morning. Thank you for the opportunity. My first question is perhaps to Martinez about steel -- your steel business, can you talk about your expected margin looking forward based on the 33% of this quarter. So how far can you reach considering that you still have some price carryover from the second to the third quarter and also the evolution of the cost of raw materials?

And the second question maybe is for Marcelo, with the low leverage levels and very strong perspectives in terms of results there is a natural question that arises about capital allocation, do you see more opportunities after the perpetuals that you're going to [ph] rest in September. So, in which business lines of the company today, except of course for the projects that we already know and have already been approved in mining and cement, what are the business areas today where you see your major opportunities? And if you allow me, I'd like to ask about cement. We saw a price increase of 6% in the quarter. So, can you also talk about what you expect -- so, for the second half of the year, do you think that these price increases will continue in the second half of the year and will continue to help the results of this business unit? Thank you.

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

Hello, Daniel. Good morning. This is Martinez. So, let's start with your question about the expected margin for quarter three. I don't know if you remember, but when we started the profitability recovery plan of the company. Marcelo used to say that 1.5-year ago, and that was in dollar per ton of EBITDA. And fortunately, with all the work that was done, and with other factors that also helped, supply demand and cost factor, we closed the first quarter with a margin of $400 per ton of EBITDA. And the forecast for quarter three is to reach a margin of about $530 per ton.

Of course, we expect that in this quarter costs will behave a little better although -- well, people didn't really pay attention to this in the market, but today, for example, for one ton of coal, we are already paying about $200 per ton. So, if you look at what is happening regarding costs, for example, the cost of coal today, which was 140, 150, now it's 210 FOB Australia. Coke remains the same, the same price. FOB China and for iron ore, 203 to 215.

So part of this has already been priced in and another important thing is that we should have a price carryover to quarter three between 13% and 17%. There are some reasons for that are very peculiar to CSN's work in their strategy. And what is motivating this? For example, in July, there was a change in the pricing criteria for customers that had manual or even half yearly contract and that doesn't exist anymore in CSN.

All our contracts now are quarterly and we work with a very small number of contracts today. So, we changed the sales profile to work with 75% to 80% and this has been of great help. Just to give you an idea, in July, in the industry, we accumulated an increase of about 120% to 130%. So, we should certainly have this price carryover, which will help us, our profitability quarter three; in the magnitude of 13% to 17% and an EBITDA of $500 to $530 per ton.

Well, now, as for your question about capital allocation, we have our priorities very well defined by segment. For example, in the case of steel we are very much focused on product activity gains considering the current volumes. These are projects under UPV in particular, which will lead to improved efficiencies, centralization of our coke shops, and removing bottlenecks. This will increase the production volume in about 10% to 15% and we do (Technical Difficulty) with production costs. So, this is what we have planned for steel.

In mining, we have a very ambitious plan of tripling our production rates using the IPO funds. And in the case of cement, there is a mix of inorganic growth via sector consolidation and we have the appetite to do that if we have adequate price conditions. And also organic projects that are exceptional projects that count with long lasting sources with excellent technology and equipment, a very privileged location. So, this will reinforce our presence in the Southeast. These are the growth focus actions that we have planned.

In the case of mining, we're talking about BRL30 billion of CapEx in a period of seven years to eight years, mixing equity and debt. We already announced the financing of $350 million, in a 12-year term, very favorable conditions. We will also be issuing an infrastructure debenture, 10 years to 15 years of maturation, subsidies of 2431. So, the company's debt from now on will be very much based on this type of project financing; long term and low cost. And the liability management, we'll follow the strategy of improving the conditions of the current liabilities. We are retiring the perpetual, which has a high cost of 7%. Just for comparison purposes, we have our 10 year bond negotiating at 4.2. So, we will possibly be prolonging further our debts, but always seeking to reduce the average cost, trying to reach the investment levels of our credit ratings. This is Martinez, Daniel, your question about cement, just to give you an overview of what we are going through right now. The Brazilian market is growing at about 15.8. Of course, this is very much impacted by last quarter, which was very bad. But we expected -- and CSN is growing at 16.2, considering that in the Southeast the market has grown 12%. So, we are gaining share in the market that we chose. Another important point is that the Market will probably close the year with a growth rate of about 6% to 8%, which is what we always talk about -- what we talk about when we prepared for the IPO. Another important point is price. Price in Brazil is still very low. Cement in Brazil is the cheapest in the world. So, what happens today, just to give an idea is that coke, the coke that we use as fuel for cement reduction, has doubled in price. And today, it accounts for maybe 30% to 40% of our cost. So, the increase of price in cement is not about recovering profitability, it's about recovering your costs. So, we increased by 6% quarter-over-quarter. We already see some increases. Cement has a different dynamic. We have some more focal increases, monthly increases. So, the expectation is to reach an FOB net price of BRL295, which should be the industry price to allow us to have the good profitability in this segment.

Operator

Thank you. Daniel for your questions.

Q - Daniel Sasson {BIO 19234542 <GO>}

Thank you. Thank you. Martinez and Marcelo.

Operator

The next question is from Leonardo Correa, BTG Pactual. Leonardo, you may proceed.

Q - Leonardo Correa {BIO 16441222 <GO>}

Good afternoon, everyone. My first question is also about capital allocation. I would like to further explore the avenues that you're implementing. For example, in cement, your strategy is very clear. The strategy of growing through M&As and you're already delivering on that strategy and you have other opportunities inside. You also have the growth in mining, which is very well defined and already been implemented.

So, I'd like to explore if you have been looking at new business opportunities and maybe you could consider a more aggressive capital allocation or if you will keep focusing on the core services of CSN where you already have a presence and you still have room to grow? So, I would like to understand what is the strategy that you have planned for capital allocation? And also, still about capital allocation, the theme of the buyback, we saw CSNA3 negotiating with your consensus accounts, a paper that is very deep, low versus historical levels of valuation.

So, how do you see the possibility of a buyback -- potential buyback? And a second question to Martinez. Martinez, you already talked about the market and the price carryover but at the same time, we realize that we are at a crossroads in Brazil regarding price?

Of course, the scenario is still very positive, the recent increases were very strong, but when we look at the recent new flow of distributors and small adjustments and discounts, when we look at the pressure of the government for potential small reduction in import rates, and all the noise that we hear about this informal price agreement, which was then denied. Looking at the premiums, we see that the premiums are getting fuller between 15% and 20%. So, it seems that it is somehow losing momentum and customers are having some difficulty in some isolated cases. So, I'd like to hear more about price in Brazil and how you see this current moment and the new elements that were brought into the discussion.

A - Marcelo Ribeiro {BIO 7199930 <GO>}

Now, about capital allocation, we have five segments. It's not just mining and steel and cement, we also have energy and infrastructure. So, this gives us more broadness in the terms of how we search for opportunities. We are reinforcing our staff. We are training our senior executives with very good results. We have a very interesting pipeline but within these segments that I mentioned. And we don't see any possibility of diversifying beyond these five segments. What we have is an interesting discussion that has always been present in CSN, which is geographical diversification, considering the recent global crisis and national crisis that we see, it's very interesting to be present and disconnected -- economies for risk mitigation purposes and exposure in different markets. So, CSN already has a presence abroad, but that could be improved in the future.

So, this is certainly something that is included in Benjamin concerns and he will address this in his final considerations. And regarding the buyback, we do think it's a very interesting use of our cash. We already have a short-term buyback program that we have started. So, in the next weeks and months, we will see part of our cash being used for that purpose. And regarding price, I think Martinez is the best person to answer your question.

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

The one important thing, first, we need to consider what is happening in the world. We already heard about this in the first call this morning, but this is all somehow permeating and being transferred to Brazil regarding the imports pillar, which has grown greatly. China today has the control, it has decided that they will have a strong production control in the second half of the year.

We have heard from different plants that will be working at much lower levels. And in steel production, this is very positive, because this certainly means that prices will increase in China compared with the current prices of about $930, $940. Other data like industrial production, retail and automotive, and a reduction of the rebates that they have today for export products.

So, this is what's happening in China. In Russia, for example, which is a country that we didn't used to mention a lot, but on August 1st, they're going to have the implementation of temporary tariffs for imports of iron and non-iron products. So, this will certainly impact us.

And another important subject, which is very interesting and important for Brazil, is that we are going back to apparent consumption levels after 2013. In 2013, we had 14.5 million, then we reached that value of 11 or 10, and now in 2021, from what we see, we should close the year at 14.5 or 15. And why do I think this price can be sustained over time?

One important thing is that today in Brazil, because of supply and demand, and also because of the service level that we have been providing, which improved greatly, particularly in CSN. I think we are allowed to maintain higher premiums. Premiums of about 15% are not as same today, vis-a-vis instability of the market, the fluctuation of the dollar exchange rate at the market, supply and demand. As I said, we have a good relationship today. And another important point that I just mentioned, is that costs, although we think they are totally controlled, they're not controlled. Coal has skyrocketed to $210. Iron ore is still at very high levels. The prices are around the world and we are not different from the rest of the world.

They're more appreciated than in Brazil. Today, in Brazil, we have prices -- so maybe a BQ of about $1.4000 or $1,420 similar to Europe. In the US, they are higher. And with this current global situation the peak of imports has gone by already, of course, there will be a carryover for the next few months. The exchange rate variable is exogenous. We do not have full control, but we believe in the level of 5.10, 5.20 which is still healthy for us.

So, these are basically the items that are supporting our strategy and we can even think of a price increase in the future, depending on the cost and depending on the premium or the dollar exchange rate. Regarding import tariffs, I think this makes no sense. And it would actually be counterproductive because we don't want to compete. All these steel industries in the world, from their door in, are very competitive. But what motivated the discussion about the import tariffs was supply. So, what causes the import cost is the low stock and this doesn't happen anymore. We have full supply currently.

And regarding competition, we are already preparing for the drop in these tariffs. And it's interesting to see this happening in Brazil because this means that the other reforms will be happening in parallel.

So, having this competitive strategy and the other reforms taking place, I don't see why we should reduce the rates. And regarding the import tariffs, this was very polarized in a few sectors. Today, markets are well replenished. And when we talk about imports, we see a lot of imports coming in.

We have 900,000 tons imported this year, it was equivalent to the whole of last year. So, competitiveness is full in this industry. I don't think that will be a relevant threat. I don't even think that will be a priority for the government. The highest priority for the government, based on our conversations, was supply. And we don't have a supply problem now. We have full supply on all product lines.

Operator

The next question is from Caio Ribeiro, Credit Suisse. Caio, please, you may proceed.

Q - Caio Ribeiro {BIO 18420483 <GO>}

The first question is about your dividend payout policy. Today, your policy is 25% of your net income, but with this low leverage and potential tax reform and potential taxation of dividends, is there any chance you will be announcing extraordinary dividends this year or even extending a policy to a higher payout linked to cash generation may be? And also, my second question is about steel. Could you talk more about how you see the evolution of the delivery terms of your products? How this has evolved in the last few months and how these terms compare with the terms that you had in the first and second quarter of last year? How you see the steel inventory levels and the sales mix in the internal and external markets, I know you're focusing on the domestic market, but do you see any changes plan for that?

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

Thank you for your question. Regarding the dividends, of course, we're very attentive to the repercussions of eventual reforms, any reforms that may happen. And this will guide our strategy and behavior. But regarding the CSN Group, based on the reform that we had, we don't see any intra-group losses. Of course, from the standpoint of the shareholders, the possibility of taxes on dividends would decrease efficiency.

So, this could be a trigger for new decisions taken this year. But looking from the structural standpoint, this new phase of liquidity and capital allocation is very recent. So, we have our radar very attentive to any potential opportunities and these opportunities are coming up, because this is a time of de-synchronized recoveries. We have some industries doing really well and others not so much. So this is the time of opportunities. But it's a little premature to talk about increasing dividends when we can have new opportunities arising and we have a clear indicator, which is reaching the level of investment from the standpoint of our credit rating, also the low leverage, and this will be our priority before increasing dividend payout.

But shareholders do have a different level of distribution. Last year, we distributed BRL900 million. And now, only in the first half of the year, we have distributed twice as much. So, the dividends will come with the improved results. And of course, we will study the impact of this recent reform. But for now, CSN's and CSN Mining's policies will be maintained.

Q - Caio Ribeiro {BIO 18420483 <GO>}

Hi, this is Caio and as we heard from Benjamin, quarter three is a given, right? You talked about delivery terms and delivery terms of products are fully under control. There may be some very short delays, but also anticipation, which compensates for the delays. Another important point is that we have a pipeline of orders of about 900 tons. So, we'll have a full quarter three. And with the price carryover of 13% to 17%. You can expect that our results in quarter three will be even better than in quarter two, and that's for everything.

And regarding inventory levels, this is also an important question. Distribution which used to be a sector where we heard a lot about how we had to have 3 months or 3.5 months of inventory. The inventory went from 2.3 to 2.6, so we didn't have that much of a recovery. And of course, the other businesses in the sector, they are more conservative now in terms of increasing their stocks.

We see a lot of anxiety and fragility around the world towards changes. So, they are planning to keep the stocks at 2.6. There is even a possibility of distribution recovering some of it's stocks because they have never made so much money in the history of steel making in Brazil and in the world. And the upstream than the downstream chains will have a healthy recovery that will allow customers not to lose sales. For example, in the auto industry, we thought they were going to go back to 35 to 40 days of stock in their plans, but it's not that high.

So, despite the growth mentioned by (inaudible) the stocks are not increasing. And this is very positive. Now regarding the mix, being cautious is never too much, right? So, what we are doing is the export quota to the US, at the full price level that we have today. We will close the year at 250, 000 tons to 300,000 tons of products to the US with a better margin than we have in Brazil.

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

The second point is BQ supply, which is relatively well supplied in Brazil. We are trying to empty our stocks and sending our full supply to Portugal. Portugal consumes 400,000 tons, 450,000 tons per year. And from now on, we will send them whatever they need. And we are also accelerating the exports of metallic sheets. So, we will have an outlet or a way out or some accommodation based on the level of full supply that we currently have in the market.

So, we're very confident about quarter three because we have volumes already sold. We have prices realized and we will wait for our EBITDA results, which will certainly be the magnitude $500 to $530 per ton.

Q - Caio Ribeiro {BIO 18420483 <GO>}

Thank you, very clear. Thank you, Marcelo and Martinez.

Operator

The next question in English is from Carlos De Alba, Morgan Stanley. Mr. Carlos, you may proceed.

Q - Carlos De Alba {BIO 15072819 <GO>}

Great, thank you very much. So, couple of questions. First one is obviously, extraordinary results, expected for acquiring of (Technical Difficulty) EBITDA per ton in the steel business, but looking here at historical numbers, going back to 2003, the highest annual EBITDA per ton was in 2008 of 151. This is a cyclical industry. So, how do you see the sustainability of the current or the expected third quarter EBITDA per ton margin and what do you expect will be a more recurring sustainable long-term margin?

And then, if I may ask, on capital allocation. Now that the IP of the cement business is postponed or cancelled, would the company still pursue an acquisition on that sector and maybe finance it differently with that, and cash on hand?

A - Benjamin Steinbruch {BIO 1499059 <GO>}

Hi, Carlos. Well, from the standpoint of sustainability, well, I was happy to go through that situation in 2003, 2004. I was already here. So, I understand what are the major differences. The world is very different. The first point is that in operational excellence, so from the standpoint of productivity, CSN is launching now. It's at full speed. It has all its maintenances, regular and anticipated, some of the maintenances in quarter two to prepare ourselves for quarter three and four.

Of course, we are being a little more careful with coal because the price has increased a lot and this certainly has an impact on our costs, and ore prices are also at a high level and that will sustain the price level. Regarding supply and demand, what I said, we have a good situation and looking at all the possible scenarios in Brazil and all the markets, the agribusiness market, the railway market, or the roads, civil construction, all the markets are now at a very privileged situation in Brazil. Imports, differently from what people think -- I think that it has a decreasing trend in imports because of the rebalancing of the steel chains in the world considering Europe and US. So we truly believe that this margin of $500 to $520 per ton of steel going beyond quarter three will be sustainable even for our quarter four.

And, of course, the next year, we still don't know but there is nothing pointing to a bad scenario in the next six months at least. That's what we think in terms of sustainability of our steel business as a whole.

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

And, Carlos, just to add two what he said, is that vision of stronger for longer.

We think that from the standpoint of global demand, there is no half turn in the stimuli for future consumption. So, at least for the next two or three years. And this will even be a lesson learned after the crisis that we had in 2008-2009. Developed countries, and developing countries will take good care of their societies and the way they were affected by the pandemic. So, demand will keep being really strong. And supply has been disappointing from the standpoint of volumes and also structurally as we can see from the activities of the Chinese government.

So, structurally, we will see margins above the historical margin of 150 margins or at least double that amount in the next three years. And regarding cement, thank you for asking about cement, the IPO was not canceled, not at all. We are still updating our numbers for quarter two. We had excellent record breaking numbers.

So, we're very excited with the mid and long term of this business, not the short-term, but mid and long term. So, yes, we are looking for opportunities to finance this growth. That's what we are seeing in mining. We committed to the IPO and we moved on and we actually made it. But we think there's additional time to update with the numbers of quarter two, will be very useful so that we can keep training and educating the investors that don't know much about this segment, at least not for now. So, we will continue with our IPO plans and we will continue with our strategy of M&A's and consolidation in the sector.

Of course, the timing of one may not be the same as the other, but these things will be taking place even without the IPO and always condition to our capital structure, we always will respect our capital structure. We will not make any moves that will increase our net debts to more than 15 billion or deleverage to more than one-time. But today, we don't see any acquisitions that could bring us to above these levels that we established. We are looking for the right M&As.

Q - Carlos De Alba {BIO 15072819 <GO>}

All right, thank you very much Marcelo and Martinez.

Operator

The next question is from Thiago Lofiego, Bradesco BBI. Thiago, you may proceed.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Good morning, everyone. I have two questions. Martinez, going back to the issue of price and focusing on car makes and the automotive industry, will you revise the frequency of your contracts with car companies? You talked about that, but I would like to understand more, what is the current situation? Is there any chance of having quarterly contracts with the car industry as well? And what about the rest of the industry, other industrial customers that you may have?

And the second question is about cement. Martinez, what is the risk that you see for quarter -- for the second half of the year and even for 2022? Or perhaps seeing some deceleration and retail demand with all the reforms? And any changes in the current pace and the current rhythm?

So, what will be the equation for cement demand in Brazil in the second half of the year 2022?

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

Hello, Thiago. Good morning. As for your first question, just try to explain in very clear terms, what we're doing here in CSN. Well, first, there was always this desire on the part of CSN to eliminate the gap that exists between distribution and civil construction products and contract products, contract based products, even for white-line appliances or car mix. And this is not a problem that was led by CSN, it was actually the contrary. There was a lot of deviation that was causing great distortions in the market as a whole. So what's happening today is that, of course, there's price situation, the cost situation that we have in the market, allowed us to do something more coherent in terms of our business policies.

As I said in the beginning of this call, we defined a new sales policy in CSN And these contracts, I don't even think this is good for the customer or for CSN; those annual contracts. What we need is to close a certain volume and deliver this volume and discuss this on a half yearly basis is at the longest. And I'd rather do it quarterly with very few customers that we have today are based on this model. For example, today, in our product breakdown and market production breakdown, we have 34 in distribution, plus 16 in civil construction so 50, 17 in general industry, with spot price 67, and 10 more in packing. We are the only producer in Brazil, so 77.

So we have practically 75% to 80% of our customers in spot price. The other 20% will be working with very short-term contracts and much more corrected because we don't want to have distortions in the value chain, So, there is no chance. And this is CSN's policy. I don't really care about what the market is doing. The market is doing a lot of things that are wrong.

So, we will work with the things that we think are right to maximize profitability to our shareholders. So, this is our commercial policy and we will not be making any changes. Now, regarding cement, to be honest, Thiago, we only see good things for cement.

We are not expecting to have problems in the markets and we discussed this, when we were preparing for the IPO. The accumulated growth of the market is 16%. The forecast for the year, considering the second half of the year, compared with last year is 6% to 8%; very promising. And the self-construction -- the construction stores are still open.

The number of new projects has increased. Last month, the number of foundations, which is also in the backlog, has increased. And traditionally, the second half of the year is always stronger. So, I don't see any problems. We don't foresee any problems for the cement sector.

The only point is the difficulty that the sector is having, and maybe the sector should be a little bit more eager or stronger to be able to recover its profitability, because the prices that we have here in Brazil are very low compared with the rest of the world. And with the increase in costs that we are seeing, for example, for coke, the prices will increase. There is no other way. That accounts for 30% to 40% of the price, and it has doubled in price. So, from the standpoint of the market, I don't have any worries. We will continue to see a very positive outlook and we also work with long products and everything that uses cement has to do with long products. Though interest rates are relatively low, we have good liquidity in the market and we have the willingness and the trust of the business community. We have to consider facts and data and that's what we will use as a base to guarantee our second half of the year.

And the second point, which I want to highlight today, and Edvaldo may even add if he wants, but the acquisition of Elizabeth, what it will bring us is a very strong entry in a market that was practically unknown by CSN. And it is very strategic. And it will also allow us to have better integration of the markets, the customers and etc.

I don't know is Edvaldo wants to add anything about the acquisition of the Elizabeth, which I think is a very important milestone for CSN this year.

A - Edvaldo A. Rabelo {BIO 18024264 <GO>}

Thank you. Well, it's important to mention that Elizabeth represents to us a fast entering in the Northeast market and a growth of 30% in our production capacity. It's a very competitive plant. We certainly have a lot of expectations in terms of synergies and upsides with Elizabeth. And the summary of these upsides and opportunities, is that we are going to replicate what we have done in the past 10 years in the company in our commercial strategy of selling little too many.

And in manufacturing, our focus on results and cost optimization, that's what we expect in a very important market, which is the Northeast of Brazil.

Q - Thiago Lofiego {BIO 16359318 <GO>}

Very clear. Thank you very much for your answers.

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

Thank you.

Operator

The next question in English is from Alexandra. Alexandre, you may proceed.

Q - Unidentified Participant

Hi, thank you for the opportunity to ask questions. So there was this article in Bloomberg saying that now the Finance Minister said that Brazil cut a deal with shell company to not to raise prices in 2021. I already see higher realized prices in the reports and yields, which is a bit what you might consider higher in the Q2. So, yes, can you please help me understand what the signal was and how this is being referred to as I said before. And also, next question that I have is that in the morning you announced the buyback of the (Technical Difficulty) will this be financed 100% from cars? Can you please remind me of your leverage target? How that's changed? I think last time that we spoke it was four to five times net debt to EBITDA. Thank you.

A - Marcelo Ribeiro {BIO 7199930 <GO>}

Well, regarding the price control that the government is supposedly implementing, I once again must tell you that, first, Brazil today has a full steel supply condition. We don't have any customer or any productive chain today either for flat or longs that is not fully replenished. We don't have that today. We have full supply. Another important point is that the steel plants in Brazil and CSN, particularly due to the integration of our assets, is very competitive.

As I said, from its doors in. I don't have any control, or actually, we are paying for the lack of control of the Brazil cost. So I can say for sure, we're not looking for protection, we're looking for competitive isonomy regarding other products. And the third important point is that Brazil is totally open for imports. As I said, in the first half of the year, the imports of flats was equivalent to the imports of the entire year, last year. So, there is no possibility of stock-outs of steel.

So, the trend is that the government, if they choose to do something, they'll do the 10% of 12%, which is 1.2. I think that is also very unlikely. And I even -- well, that could even take place if the administrative and tax reforms would be effectively implemented simultaneously. And I don't see that as a threat in terms of price control for Brazil. Now, regarding the buyback, we will be doing that with our own cash. We will not need new emissions to buyback the $1 million of the perpetual. That doesn't mean that over time we will not find good opportunities in the market. But looking at this horizon for the buyback of the perpetual, we will be using our own cash.

Q - Unidentified Participant

Okay, thank you. So, for your leverage targets, can you remind me, the leverage target, what it is now in terms of net debt to EBITDA?

A - Luis Fernando Barbosa Martinez {BIO 17456025 <GO>}

The target, well, it's actually more of a ceiling. It's one time the net debt EBITDA ratio. Right now, we are at 1.6 times, but by the end of the year we will be below 1.

Q - Unidentified Participant

Thanks so much.

Operator

Thank you, ladies and gentlemen. Since we have no further questions, I hand it back over to Mr. Marcelo Ribeiro, Executive Director of Investor Relations for his final remarks. So, now, let's hand it over to Benjamin for his remarks. But this is just an attempt because we still have some connection problem. Benjamin, can you hear us? Can you hear me, Marcelo?

A - Marcelo Ribeiro {BIO 7199930 <GO>}

Yes, we hear you.

Operator

We hear you. Go ahead.

A - Benjamin Steinbruch {BIO 1499059 <GO>}

Well, I apologize for the technical problems. Good afternoon, everyone. Thank you for attending this conference call. I would just like to tell you that we are very happy to having been able to deliver these very good results. It was actually as if we had completed 12 months in six. So, by the mid-year, we have reached what we had proposed for the full year.

So, very briefly, I will go over the next priorities that we will have from now on, just to bring everybody to the same level. The first intensive priority will be the investment grade until the end of the year. We will be doing whatever we can to be considered an investment grade company.

We will maintain our leverage level close to zero or below one. Don't be surprised if we have zero debt by the end of the year. Our greatest priority is to have this zero leverage. Investments will be made with long-term financing compensated by our cash. We will maintain high cash levels, I heard a lot of questions about the fact that we are a cyclical industry, having highs and lows, so how we fight that. We're going to do that through a low debt level and a high cash level. Investments will be based on this strategy, both organic investments and also any potential M&A opportunities. They will be listed on the stock exchange, their respective currency, so that we can tap the opportunities without the need to increase our debt level. We will be very conservative in everything that we do and we will preserve as much as we can this investment grades that we are seeking to achieve by the end of the year.

We are always striving for quality, increasingly striving for quality; that's our main premise. So, both were ore and cement and also steel. We will also be looking for added value, improved quality, always based on the highest price. And our great project for the second half of the year is to control and lower our costs. We did everything possible and impossible to update our prices based on the cost increase and we will now be strongly working to reduce these costs so that -- so we can assure the best competitiveness possible.

So, I'm very confident. I'm expecting an exceptional second half of the year. Quarter three, as we heard, it is a given. And in quarter four, unless we have any unexpected disaster, there is nothing that will change this; a good trajectory that we are seeing this year with increasing results.

We're very optimistic about our company and about the market. And we are very proud of our team. We are proud of our company, of the targets that we we're able to reach. As we said, six months -- 12 months in six months. And many wouldn't have believed if we have had told the story in the beginning of the year.

Today, we have a company that is totally different from what it was in the past. What we still have is good assets. And based on that, we will be working on a totally opposite way. We have to manage accesses now and not the efficiencies. And this is something that we will be doing surgically with maximum dedication; always looking at our investment grade, always looking at our zero debt target, always looking at our high liquidity targets, and low debt targets. So, these are the premises that will guide us moving forward. Thank you very much for attending. Congratulations to everyone in our company, worked really hard, much more than you can imagine, our analysts and everyone. And we're very proud of the results that you helped us achieve and thank you all for your hard work. This was exceptional work and I would like to congratulate each and every one of you, our employees and everyone involved, because this certainly required a lot of dedication, hard work and energy and the results are very good. We are very proud of communicating these results to the market, the results that we had in the first half of the year and that we are expecting for the rest of the year as well.

Thank you all for attending this conference call. We are always at your service should you have any further questions. And a big hug to all of you. Thank you, Marcelo.

A - Marcelo Ribeiro {BIO 7199930 <GO>}

Thank you, Benjamin. I think everything was very clear. I'd like to thank all investors and analysts who attended this call and we are at your service should you have any further questions. Thank you very much.

Operator

Thank you. This conference call is now finished. You may disconnect your lines now. Have a great day.