Q4 2013 Earnings Call

Company Participants

- Clovis Torres, General Counsel
- Galib Chaim, Executive Officer of Capital Project Implementation
- Jose Carlos Martins, Executive Director, Ferrous & Strategy
- Luciano Siani, CFO
- Murilo Ferreira, CEO
- Peter Poppinga, Executive director, Base Metals & IT
- Roger Downey, Executive Director, Fertilizers and Coal
- Vania Somavilla, Executive Officer of HR, Health and Safety, Sustainability and Energy

Other Participants

- Alex Hacking, Analyst
- Andreas Bokkenheuser, Analyst
- Carlos de Alba, Analyst
- Ivano Westin, Analyst
- Leonardo Correa, Analyst
- Marcelo Aguiar, Analyst
- Renato Antunes, Analyst
- Rodolfo De Angele, Analyst
- Thiago Lofiego, Analyst
- Wilfredo Ortiz, Analyst

Presentation

Operator

Good afternoon, ladies and gentlemen. Thank you for standing by. Welcome to Vale's conference call to discuss the Fourth Quarter 2013 results. If you do not have a copy of the relevant press release, it is available at the Company's website at www.vale.com at the investor's link.

At this time, all participants are in a listen-only mode. Later we will conduct a question and answer session, and instructions will be given at that time. (Operator instructions).

As a reminder, this conference is being recorded. To access a replay, please dial 55 11 46 88 6312, access code 5485124 hashtag. The file will also be available at the Company's website at www.vale.com at the investor section.

This conference call and the slide presentation are being transmitted via Internet as well. You can access the webcast by logging on to the Company's website, www.vale.com, investor section, or at www.prnewswire.com.br.

Before proceeding, let me mention that forward-looking statements are being made under the safe harbor of the Securities Litigation Reform Act of 1996. Actual performance could differ materially from that anticipated in any forward-looking comments as a result of macroeconomic conditions, market risks, and other factors.

With us today are Mr. Murilo Ferriera, Chief Executive Officer, CEO; Mr. Luciano Siani, Executive Officer of Finance and Investor Relations, CFO; Mr. Jose Carlos Martins, Executive Officer of Ferrous and Strategy; Mr. Roger Downey, Executive officer of Fertilizers and Coal Operations and Marketing; Ms. Vania Somavilla, Executive Officer of Human Resources, Health and Safety, Sustainability and Energy; Mr. Galib Chaim, Executive Officer of Capital Project Implementation; and Mr. Peter Poppinga, Executive Officer of Base Metals and Information Technology.

First, Mr. Murilo Ferreira will proceed to the presentation, and after that we will open for questions and answers.

It is now my pleasure to turn the call over to Mr. Murilo Ferreira. Sir, you may now begin.

Murilo Ferreira {BIO 1921488 <GO>}

Good morning. Good afternoon. Thank you, everyone, for being with us in this conference call.

Vale delivered a strong performance in 2013, with solid results across all the businesses. 2013 was a year in which we realized the benefits of our cost cutting efforts, CapEx discipline, and a focus on core business, also a year in which we lay out the conditions to deliver solid value and free cash flow growth.

So let's look first at our financial performance. 2013 was a strong year for both financial and operational performance. Our underlying earnings reached $12.3 billion. Our adjusted EBITDA was $22.7 billion, the third highest ever, increasing 18% in relation to 2012.

We had record sales volumes in iron ore and pellets, with 306 million tons in 2013. Sales of copper, gold, and coal were also records, and nickel sales were the highest since 2008.

Despite the increase in sales volumes, we had a reduction in costs and expenses across all our businesses, with savings, net of depreciation charges, of $2.8 billion year-on-year.

Cost of our products reduced $972 million. SG&A went down $860 million, almost 40%. R&D decreased $663 million, or 45%.

Our cash generation allowed us to distribute dividends of $4.5 billion in 2013. As previously announced, we are committed to a minimum dividend of $4.2 billion in 2014, which means a dividend yield of about 6% at Vale's current share price.

2013 was equally remarkable in terms of implementing the disciplined capital allocation which I have been conveying to you from day one as Vale's CEO. In 2013, we reduced $2 billion in CapEx year on year, making another consecutive year of CapEx reduction.

As we complete our projects and become increasingly more selective in approaching new projects, you shall expect further reductions in Vale's capital expenditures.

We sold non-core assets and investments worth $6 billion in 2013, enforcing our commitment to the simplification of our asset base. We are now exploring beneficial partnerships such as one in the Nacala Corridor that will create value and reduce our capital commitments. We are also open for partnerships in our global co and fertilizer segments.

Now when we look at major issues we dealt with, we reduced important business uncertainties in 2013, allowing management to focus even more in our operational and strategic schemes.

In November 2013, we joined an income tax settlement program called REFIS for income tax and social contribution of earnings of non-Brazilian subsidiaries. Our participation in the REFIS program resulted in substantial reduction in our penalties, fees, and interest on the taxes, elimination of tax uncertainties while preserving potential fines from legal challenges to the tax regime in foreign subsidiaries.

Last year we were also granted the implementation permits for S11D and associated logistics, paving the way for growth in iron ore production beyond 2016.

And to add to this, at the beginning of this month, we had more positive progress, being granted authorization to mine additional areas around N4E mining, which supports the production targets of 120 million tons in Carajas in 2014 and increases confidence in our growth program for 2015 and 2016.

I am also proud to comment on the projects we delivered in 2013. We completed a number of projects required to grow iron ore production in the years from 2014 to 2016.

The Conceicao Itabiritos plant started up in the Fourth Quarter. It is the first of our satellite projects which will improve quality and extend mine life, allowing full utilization of the South and the Southeast System capacity.

Plant 2 in Carajas, now as additional 40 million tons per year, is currently ramping up. And we expect to operate it up to the limit of the logistic capacity of our Northern System.

Also, the CLN 150 project, including a new pier in Ponta da Madeira terminal, will reach 150 million tons capacity at the port and 128 million tons per year at the railway, supporting our production growth in Carajas in the short run.

In addition, we are ramping up at base metals projects. Salobo is already operating close to the nominal capacity. In December, it produced over 1,000 -- 80,000 tons, which is basically our nominal capacity on a yearly basis. We are now using the lessons learned from Salobo 1 to improve our future operations in Salobo 2.

The Onca Puma plant restarted successfully. And in December, its output was 1,300 tons. This represents about 62% of its nominal capacity of 25,000 tons per year for one single furnace.

Nouvelle Caledonia is going well. And in 2013, VNC produced about 16,000 tons in nickel oxide and nickel hydroxide cake.

Marking the end of an investment cycle, we completed an important project in base metals. Long Harbour is currently being commissioned. The total mining is ramping up, and they expect to provide in excess of 8,000 tons per year of nickel, in excess of 10,000 tons per year of copper.

So where do you go from here? 2013 was another year of relentless focus on health and safety. Our indicators improved. In spite of our efforts, we still had accidents. This is not acceptable, and we will not relax until we achieve our goal of zero harm.

In 2014, we will continue with our cost cutting efforts to preserve our strict discipline in CapEx allocation. We will concentrate on completing our ongoing projects and on delivering volume growth.

We are totally committed to creating value for our shareholders. And we are focused on generation of free cash flows, which we will manage firmly to reduce our debt levels and distribute increasing dividends to our shareholders.

Now our team will be available for a question and answer session. Thank you.

Questions And Answers

Operator

Thank you. Ladies and gentlemen. we will now begin the question and answer session. (Operator instructions.) Please restrict your questions to two at a time. Carlos de Alba, Morgan Stanley.

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

Thank you very much, Murilo. Congratulations on the results. The first question seems to be the iron ore price. The realized price was really strong. We all see what the spot prices, or at least the plants and other industries, have done. And even so, the company managed to surprise us positively.

So I wonder if you can explain what do you think drove the better prices. And you can break it down by the different components. I will certainly appreciate it so we can fine-tune our numbers going forward, particularly if this is something that you believe is going to be sustainable and really going to differentiate the company from other competitors.

Then, the second point is just trying to understand, in the Portuguese call, you said that iron ore prices are difficult to come down, or really that it's difficult for iron ore prices to be down below $110 on a sustainable basis. And I just wanted to understand what is the logic behind that.

If we assume that the market goes into slow close and it doesn't -- it no longer needs the high cost Chinese mines, we will lose the support that those high cost users bring to the market. And therefore, that opens the possibility to have prices sliding below $110. And so, I just wanted to understand what is the rationale behind those comments. Thank you very much.

A - Murilo Ferreira {BIO 1921488 <GO>}

Thank you. Carlos Martins, please?

A - Jose Carlos Martins {BIO 1715332 <GO>}

Okay, Carlos. As far as the iron ore price, we have some factors that influenced the better performance. Part of it was the quarterly price proportion. We have many contracts that are based on lagging quarters.

So as the price was going up and then it stabilized, we have the impact of those contracts. That brings some additional increase in price. We calculate one-third of this price increase was due to this fact.

Another issue is that, as you know, we are working hard to increase our CFR proportion in our sales, okay? So by doing that, so we have the impact of the freight on the average price. So one-third of this increase is due to the CFR sales.

And at the end, we have a mix of contracts that are better in this quarter. So I wouldn't put it as a thing that can be kept, but in this quarter was particularly very favorable.

On top of it, as you know, we had some improvements in the price of high quality ore. That can offset a big part of the total discounts that we needed to give for lower grade ore.

So I think the scenario was very favorable in this quarter. And as far as going forward, we believe that as a -- on a comparable basis, we believe that we can perform better.

Although the average price in the market is now a little bit lower than what it used to be in the last quarter, why we think that the price came up to below $110 is not on a sustainable basis. It's because of the high cost of local producers, okay? We are talking about more than 350 million tons of local ore, and a big part of this ore have costs much higher than $100.

And so, as the price is driven down, part of this supply will be taken out of the market. Sure, if you have a very big increase in supply the price could be driven down a little bit more. But that's not the case we assume for this year.

We believe this year the additional ore coming to the market is around 100 million tons. And 60% of this will be taken by the global consumption. So the remaining 40 million tons is the one that we will compete with local ore in China. So I think this is a very low quantity when you compare 400 million tons of additional capacity against 350 million tons of high cost local ore.

So that's the reason we keep our view that the price cannot be driven below $110 in this year. So that's the way we see it.

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

Thank you, Martins. And just from me a follow up, on the CFR sale that you mentioned, what is the average freight cost that Vale is seeing today when you are selling on those terms?

A - Jose Carlos Martins {BIO 1715332 <GO>}

Our average cost of freight is around $22.00, okay? (Multiple speakers.)

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

Thank you very much. Yes, of course.

Operator

Alex Hacking, Citi.

Q - Alex Hacking {BIO 6599419 <GO>}

Good morning, and thank you for taking my question. First question is on iron ore, if it's okay. I mean, you just talked about how the price probably could not be sustained below $110 a ton. But in the very short term, how concerned are you that we could see some kind of a destocking event in China similar to October 2012, given some of the negative data that we're seeing on inventory and steel demand in China? So do you have any kind of short term concern on the price?

Then, the second question will be on base metals. I know on a -- you're looking for sort of $3 billion to $4 billion of EBITDA from this business at today's metal prices. How far towards that goal do you think that you can get in 2014 now that we have Salobo at full capacity plus partial operations in Onca Puma and VNC? Thank you.

A - Jose Carlos Martins {BIO 1715332 <GO>}

So as far as price, when we talk about $110, we do not talk anything shorter than three months, okay, three months average, because nobody takes a decision to shut down a mine or to shut down a blast furnace with a one week price or a one day price.

So you only have to look at three months' average. And in three months' average, all the points you raised about the destocking, stocking will be kind of absorbed.

I think the Chinese iron ore market is very dynamic, okay? We never had in the history of the world anything so dynamic as the iron ore market in China. So all those effects happen constantly. One year in China, you can see very big movements. You can see prices going down, up to $90, and three months later to be $150. It's all about the numbers.

So I think to talk about the short term average price in China is quite difficult. We always look at bigger periods. And we look before and we look after, and we do not see why the price can be below $110.

So that's our basic assumption. And I have been telling you about this not from today. And if you look at the track records, I think you'll have to believe a little bit more in what I'm saying.

In the short term today in China what we see is really a monetary constraint which is affecting the civil construction mainly. And that is affecting steel, and indirectly affecting steel production and iron ore consumption. And at the same time, you have a big increase in Australian production.

But even with this situation, price in this period never went below $117. Today it increased a little bit again. So I think there is a very strong resistance in price in the range of the local Chinese iron ore cost. So it's not driven by supply and demand, but it is driven mainly for cost structure.

So that has nothing to do with the short term's movement. That we will continue to see in China, okay? Now we have this pollution issue. We have the monetary constraints.

But when you talk with the customers in China, they are willing to buy my ore. They are willing to increase their production. They are willing to modernize their facilities.

And even the main institute in China, which is CISA, the steel association in China, they delivered a very decent forecast for this year, 3% growth in steel production and near 7%

growth in iron ore imports. And I think they are very qualified to make this projection because they work with all the steel industries. They have cross connections with the planning areas of the Chinese government. They are aware about the pollution issue.

So that's the facts that we are looking for. And we put our assumptions based on facts, based on reality that we can see, and think that we can really capture in the Chinese market, in the Chinese environment.

So I believe that this year, considering the big increase in supply, will not be as good as last year in terms of price. But the pricing continues to be very favorable and very profitable for Vale.

A - Murilo Ferreira {BIO 1921488 <GO>}

Please, Peter Poppinga about the base metal.

A - Peter Poppinga {BIO 17245689 <GO>}

Okay. Thank you, Alex, for your question. I will try to answer your question looking into 2015 and then we'll talk about 2014.

If you take the 2013 realities into account with 2013 prices and then you add the ramp ups, you can add roughly $1 billion from Salobo in terms of EBITDA. I am talking now 2015. You can add $400 million to $500 million depending on the mix from VNC.

All the North Atlantic optimizations we are doing with the increased productivity in mine plants and also talking coming on-stream in Long Harbor, you can add around $500 million. If you go now to Onca Puma, we are talking at least $200 million. And of course, you have to deduct the pre-operating expenses, which will decrease drastically, if not disappear, and then you reach already your $3 billion of EBITDA, this under very similar price scenarios.

Now, you add this to the $1.6 billion EBITDA we had this year. It becomes $4.5 billion or higher, and now you at least consider $20,000 in nickel prices. This adds you another $1.5 billion in EBITDA, which leads us to our $6 billion, which is very conservative because we think prices can be much higher than that because of the export ban of Indonesia. You're well aware.

Now, if you go to 2014, I guess the reality would be in between what we have today and what I just said. So it's something around $4 billion to $4.5 billion.

Operator

Thiago Lofiego, Bank of America.

Q - Thiago Lofiego {BIO 16359318 <GO>}

I have two questions, the first one if you could give us an update on your Malaysian distribution center project. Do you expect any benefits on your realized iron ore prices once it's fully ramped up? And when do you expect to be fully ramped up there?

And the second question is regarding your Valemax vessels, if you could give us an update on the situation there, how the authorizations for you to berth in China are now, and what's the outlook there.

A - Murilo Ferreira {BIO 1921488 <GO>}

Thiago, thank you very much. Galib Chaim for the first question, and Martins for the second one.

A - Galib Chaim {BIO 17562473 <GO>}

Well about the Malaysian distribution center, we expect to receive the first vessel in next month to start in the unloading system. And the construction is going very well, and we expect to start the first loading in the exportation berth in the second half of this year.

I believe that Malaysia, it's our best project. And everything is being done in the best way, under -- below the budget. We don't have any concern up to now.

A - Murilo Ferreira {BIO 1921488 <GO>}

Okay. Martins, please?

A - Jose Carlos Martins {BIO 1715332 <GO>}

Well as far as Malaysia impact on the results, we believe that will be felt in the next year because we are starting sending the ore to Malaysia during March. And we want to be able to export from there after July.

So then we'll have a period that we are building some inventories and then blending ore. Then, in second half, we can deliver what we call the green Brazilian blend, which is the kind of ore that we expect to blend with different ores from Brazil. And that can be used to generate less carbon emission, okay?

We are designing a kind of blend that can reduce carbon emission in the blast furnace in China. So this ore, we don't have how the market feels to the prices for this ore. But we really believe that the acceptance will be very good.

Also, Malaysia will allow us to use our Valemax fleet completely and much more efficiently. Even if we are not able to berth in China, our 35 vessels that we have owned or contracted can be used at their maximum efficiency through Malaysia, through Oman, and through our floating station, also with the ports that now are accepting Valemax.

Today we can berth Valemax in three ports in Japan, two ports in Korea, and another port in Philippines. So we are less dependent on China acceptance to use our fleet, so that will bring a cost reduction. So Malaysia distribution center will be very important for us to increase not only the efficiency of our blending of material, but also our fleet.

As far as entering China, China recently established a new regulation. And we believe the regulation was a big improvement from the last regulations they had, first because they are transferring to the ports the decision to accept ships bigger than the port's capacity; second because they are allowing the ports to have an increase of up to 10% of their capacity; and third because they say in the regulation that the trend to use big vessels is a reality and that the Chinese ports have to be adapted to receive those vessels.

So I believe that the law, the regulation itself, is a big incentive for the Chinese ports to prepare themselves to receive larger vessels like Valemax and others. So I cannot put when it will be possible, but I believe that as time goes by the chances for China to accept the Valemax is increasing.

But as we always said, China is a sovereign country. They have their regulations. They have their constraints, and our issue is just to adapt ourselves to what they establish. We already did. Also we made the ships to go to China. And it was not possible, and we found a way to keep it operating in a high performance level. And now with Malaysia, we are completely free from this dependence.

Operator

Rodolfo De Angele, JPMorgan.

Q - Rodolfo De Angele {BIO 1541593 <GO>}

Hi, everyone again. I wanted to speak two questions. I'm going to ask you to answer again a question I did earlier, because it's a recurring theme with investors. And the question is really on the caves issue. Is that past us? What does it mean for volumes that were guided in the Vale Day for this year? And how do you see your volumes getting back or continuing to increase into the coming years in regards to the caves issue that we discussed so much in the last year? So that's my first question.

And the second question is also trying to address a recurring theme that I get from investors, especially the global ones that are looking at your kind of period in Australia. Investors are more and more looking for capital discipline, and dividends have been of particular importance for them when looking at the different mining companies. We understand that Vale is in a different moment of -- it's true it's been investing in such a big and important project.

But if there is a liquidity event in the year, be it a spike in iron ore price or an agreement on Aquila that makes you avoid CapEx, how should we expect Vale's management proposal to the Board with regards to this? That's it from me. Thanks.

A - Murilo Ferreira {BIO 1921488 <GO>}

Vania Somavilla.

A - Vania Somavilla {BIO 15867577 <GO>}

Good afternoon. Regarding the first question about the caves, as I mentioned before all the regulatory uncertainties are over now. We have overcome the studies. There were some uncertainties about how we would do our studies. Now we have completely understood, together with the environmental agency, what are the necessary studies, biological, hydrological, and speleological studies.

So we have discussed the methodology now. As soon as we need deliberations, we are presenting the studies. They analyze. And it's completely in phase with our strategic planning, assuring us that we are going to get the necessary production for 2014 and for 2015.

So the next thing is known. It depends on what we call (Portuguese spoken). That is already under study, and the deliberation for this is completely on schedule. As I mentioned before also, we already have some people from IBAMA go in there, in the Carajas region, just to verify the caves.

And so, it's on the schedule. It depends much more now on our planning and the studies that we are conducting, because the methodology is already clear.

A - Murilo Ferreira {BIO 1921488 <GO>}

And about the second one, in case of having a cash flow in the most positive way, for sure we can reduce debt. We can increase dividends or even to buy back shares, as we did in 2011.

Now, what we can assure you, that we will stay with a discipline in our leverage, which is extremely important because, as you know, we intend this to finalize the first stage of our Moatize project, which means for next year 11 million tons of coal.

And we intended to see the first wagon of Nacala Corridor until the end of the year, and the fourth facility in the First Quarter of next year, the first shipment from the Nacala port facility. Then I believe that we have many things to complete, many more again in Brazil, with the S11D and the fertilizer project.

But regardless of this, we always pay attention in case of having further cash in our position. And for sure, we will bring the value to our shareholders. Thank you very much, Rodolfo.

Operator

Wilfredo Ortiz, Deutsche Bank.

Q - Wilfredo Ortiz {BIO 6113152 <GO>}

Yes. Good morning. A couple of questions. On the cost cutting front, do you have an overall US dollar amount target for 2014 in addition to that $2.8 billion achieved in 2013?

I believe you mentioned the 10% reduction in SG&A and that you would be cutting in half your pre-operating and stoppage expenses of 2013. So I get to about $1.1 billion just on those two effects. Are you targeting a higher amount, or is there something along the lines of what you're expecting this year?

And my second question is regarding the new iron production capacity being brought on-stream by the Brazilian steel producers. As more of the Brazilian steel producers become more self-sufficient, how could this impact Vale's iron ore sales to the domestic market going forward?

A - Murilo Ferreira {BIO 1921488 <GO>}

Luciano Siani, the first one, please?

A - Luciano Siani {BIO 15951848 <GO>}

Thank you for your question. You just mentioned -- reproduced the guidance that we gave at Vale Day on the SG&A and pre-operating expenditures, and they are maintained. So we're very comfortable that we are going to deliver on both. I would say that we started in the year very well in terms of SG&A and on pre-operating stoppage.

If you just take two numbers, we spent $120 million last year just at Onca Puma, which is now producing very well. So no property expenditures from this moment on anymore. And Rio Colorado, we also spent $384 million on that. So just these two, we are talking about $500 million. So your calculations are correct for these two items.

On cost of goods sold, we are not giving guidance. But we believe that the initiatives that we started in 2013 are starting to bear fruit in 2014. We believe that we have more opportunities to increase workforce productivity.

We believe that the comprehensive review of contracts and the procurement approaches are starting to bear fruit more at a speed which is higher than what we had last year. And we are looking forward to the dilution of fixed costs that we are going to have as we ramp up production in all of our projects, especially in the iron ore projects.

We've been saying that once we are able to ramp up, the marginal cost of producing -- the marginal ton of iron ore will be much lower than the existing tons. And so, this is an effect that, as soon as we've ramped up production, should come into the cost figures as well.

A - Murilo Ferreira {BIO 1921488 <GO>}

Martins?

A - Jose Carlos Martins {BIO 1715332 <GO>}

As far as the second question, our participation in the domestic market is decreasing, as you probably know, because a big part of the steel producers in Brazil are developing their own mines. So as time goes by, possibly our sales in domestic market will be lower and we probably will send more ore to export.

We have some exceptions to this. One is CSA, which we have a long term contract to supply up to 80 million tons per year, and also in the future CSB, which will consume 6 million tons of ore. But for the other companies, it will depend very much on their strategy, because all of them are developing a strong verticalization strategy.

So our main target is the export market, okay, seaborne market for our ore. And we believe that the seaborne market has conditions to absorb everything that we are able to produce and ship.

Operator

Marcelo Aguiar, Goldman Sachs.

Q - Marcelo Aguiar {BIO 3721791 <GO>}

Hi, gentlemen. Thank you for the opportunity. The question will be regarding the REFIS. I mean, you guys explained correctly, I mean, how you arrive at a lower impact on your balance sheet.

But I would like to cover more on the tax payments going forward, looking to 2014 and 2015. Are you able to use the credits, like of close to BRL8 billion, to reduce the tax to be paid in 2014 and 2015? Can we assume this full amount deductible for the tax has to be calculated?

The other question will be regarding the mining law in Mozambique. I mean, can you elaborate a little bit on what's happening there? I mean, how secure are you guys in terms of royalties, the whole legislation? And also, if you could indicate the cash cost we should expect, I mean, in terms of the met coal at the port when Nacala will be fully operational and also the cash cost for the thermal coal as well. Those will be my questions. Thank you.

A - Murilo Ferreira {BIO 1921488 <GO>}

Please, Clovis Torres, our legal counsel, and Luciano Siani, and later on Roger Downey.

A - Clovis Torres {BIO 17711179 <GO>}

Good morning, to everybody. The REFIS, as you know, it was provided by law. And we have now recorded a provisional merger. The provisional merger is regarding the future tax for the CFC legislation. And as such, it has amended in a couple of articles the existing REFIS legislation.

One of these amendments actually provided for an exemption on the potential tax that would arise on you taking advantage of the expenses that you had on the litigation.

For example, if we had needed BRL40 billion, it was 40 billion reais, at that time $22 billion, that you could take advantage in your balance sheet. If the REFIS would reduce it because of the cut it gives on interest and penalties, you would be able then to take advantage only of those that you actually put in your balance sheet, not really the full amount. Otherwise, you would be taxed on the difference, on the reduction of your debt.

So as such, the MP 627s amended the law to say that the gain that you have on the difference of the full amount of your debt and the one that you actually enter, your REFIS, would not be taxable, is exempt. Therefore, you could take advantage of the full amount and not actually have any tax on your future gains.

So that's really the basis for the way that we have accounted for the REFIS in our balance sheet.

A - Luciano Siani {BIO 15951848 <GO>}

Marcelo, this is Luciana. You are correct. So we will have minimal cash outflows for tax payments in 2014 because of those credits. It will be a significant impact on our cash outflows.

A - Roger Downey {BIO 7419641 <GO>}

Hi, Marcelo. Answering your questions on Mozambique, regarding the new or proposed new mining code, so far there haven't been any developments. Obviously, Mozambique is gearing up for its annual elections, and there hasn't been any development on that front.

In our discussions with the Minister of Mines in Mozambique, she has basically told us that, well, this is probably something that's going to go further down the road. And if it does, we won't be affected because existing contracts will be honored, which is a relief for us and we see it very positively.

Obviously, things are changing in Mozambique. It's a different environment today than it was a few years ago. Ours is the most advanced project and the only project that is realistically advancing. And I think this has changed a bit the attitude towards mining.

Regarding our business there, we produce met coal and thermal coal basically at the same cost, right? It is the same processes, essentially. So we cost them at the same level.

Once Nacala is fully operational and we've ramped up both Moatize 1 and then Moatize 2 to 11 million and 22 million tons per annum run rates respectively, we should be definitely working at a FOB cost within the first quartile.

You have to remember that Moatize is an open cut mine. Once we have a large scale and very efficient railway and port running in Nacala along the Nacala railway and the Nacala port, we will have world-class operations from mine to ship. And obviously this is going to take us down to where we should be really, with that sort of deployment.

Operator

Ivano Westin, Credit Suisse.

Q - Ivano Westin {BIO 17552393 <GO>}

Hi. Thanks for the questions. Just two points, the first one on your debt level. Just want to get a sense on how much room you expect to reduce your debt. I mean, what is your comfortable level?

And the second question is on cash cost for iron ore. While you are ramping up your production in 2014 and 2015, what sort of cash cost change can we expect, if any? Thank you, so much.

A - Luciano Siani {BIO 15951848 <GO>}

The current debt level is -- when compared to EBITDA is very comfortable, right, and when compared to our future projection is comfortable. I would say the bias would be, with this excess cash, more to pay dividends than to pay down debt, although some reduction would be desirable given that we should sum up the REFIS liabilities.

And to reassure, as you know, we have a negative outlook from S&P since the application for REFIS. So I would say that, from that respect, it would be advisable to have a downward trending debt in order to reassure the current credit ratings. But I would say the bias would be to use excess cash more towards dividends.

In terms of cash costs in iron ore, we are very close to $21.00 per ton on cost of goods sold per ton of iron ore FOB, right? So that's -- you get to that number when you exclude the freight expenditures and not considering also the expenses. So I'm referring to the segment -- business segment information on the financial statements.

I would say it's -- without giving you guidance for this year, because it will all depend on the pace of the ramp up, there are some adjustments and expenditures that we will have to incur in order to -- one-off expenditures in order to ensure a good ramp up, perhaps putting some part of our fleet, idle fleet, in order to -- in working condition and so on.

So you should see more of the effect of the dilution for this particular reason in 2015. And today we have a split of around 50/50 in terms of fixed costs and marginal and bearable cost. So the way to think about it going forward is that the additional production is more -- costs more than marginal production, more bearable cost than fixed cost. So I believe with that you can use some of the math for 2015.

Operator

Andreas Bokkenheuser, UBS.

Q - Andreas Bokkenheuser {BIO 7182883 <GO>}

Yes. Thank you very much, and thank you for taking my question. Just following up on the debt question, looking at your balance sheet and your cash flow statement, it looks like your total debt was unchanged in the Fourth Quarter versus the Third Quarter, but your long term debt went up about $6 billion, $7 billion, about 13%, and there was no change in your short term debt. So can you sort of clarify how that was possible?

And secondly, it also looks like you've been in the market lately raising debt or looking to raise debt in the First Quarter. In view of declining iron ore prices, from where I'm sitting it sort of looks like that you are financing your dividend payments by debt rather than internal cash flow. Can you confirm that being the case? Thank you very much.

A - Luciano Siani {BIO 15951848 <GO>}

Okay. The total debt was stable when compared to 2012, the gross debt. The net debt, as you pointed out, increased from the third to the Fourth Quarter. Had we received the proceeds from VLI from the sale of the logistics service arm, this wouldn't have happened. So we believe to return to the levels of net debt of the Third Quarter after we receive those proceeds.

The reason why the short term debt decreased and the long term debt increases is because we had mobilizations in the Fourth Quarter which are a part of our short term debt. And we financed this with long term debt.

The reason why we are going -- we went to the market, to the Brazilian market, the bonds that we issued internally, they had tax breaks for individuals. So we were able to fund ourselves at a rate which, when swapped to the US dollar, was between 100 and 150 basis points below the current yield curve that we had.

And the strategy was to use that to anticipate our funding needs for this year, which are minimal. So you shouldn't see Vale go into the markets again. And that was not a big transaction. It was BRL1 billion, so we are talking about $400 million.

So basically we have all our refinancing needs for the year already provided. So going forward -- so, we have not paid dividends last year from that, and we do not look, going forward, to pay dividends out of that.

There are a few items that can provide us good, surprising cash for this year. One was already pointed out, the prices of iron ore. We have the VLI proceeds, the divestures which will be used to offload part of the CapEx which was budgeted for the year, some of the tax credits already mentioned in the conversation. So we are very confident that we're going to be able to do both, to pay good dividends and keep our debt on a downward trend.

Operator

Leonardo Correa, HSBC.

Q - Leonardo Correa {BIO 16441222 <GO>}

Hi. Good morning. Good afternoon, everyone. Thank you for taking the questions. The first one is back to Martins. Sorry, Martins. It's just on the quality premium side. I think it's probably one of the most important issues and themes to discuss on Vale going forward.

But just to confirm, I am understanding that most of the Carajas shipments are being sold on a CFR basis, and also if you can indicate what type of premium levels for that type of material you've been reaching. I mean, we've been seeing some spot transactions at close to $10.00 premiums. So just wanted to confirm that.

And second, bringing back Roger in the discussion, I think you've been very clear on the coking profile of the business, on Moatize. It's non-recurrent to consider these type of earnings sustainable. There is a pricing issue, but you also have logistics issues which are weighing on profitability. So I think that upside source is clear.

I just wanted to understand, on the fertilizer side, there also have been some issue on pricing, on market structures. So that clearly has had an impact on overall profitability. Is there anything else from a cost perspective, Roger, we can see going forward to turn around those operations that had been profitable a couple years back? So just wanted to get your views on what can be done and what steps you're taking on the fertilizer side. Thank you very much.

A - Murilo Ferreira {BIO 1921488 <GO>}

Martins, please?

A - Jose Carlos Martins {BIO 1715332 <GO>}

Let's start with the premium, okay? Sure, we have been selling Carajas with a premium up to $10.00, okay? It's true. We apply the formula price for the 62% plus what additional content we have in Carajas as well, and then on top of it we put up to $10.00, okay?

But this is very dynamic, okay? It depends upon the situation of the market. So I cannot -- we don't believe we can keep it, but the pent up from the quarter is the situation in the markets there.

Going forward, I believe that the premium can be increased on Vale average price realization as long as we put in operation our projects in the Southern System because, as you know, we have some discount that we needed to give for high silica ore that we are now producing. So this high silica ore discount almost offset the gains we have experienced with Carajas.

But as long as we bring on those projects that you know, the itabirite project that we have -- so, we have many projects in the Southern System designed to increase quality to the former levels. We are going to get rid of those discounts, and then our average price realization tends to increase. But I think that will be more -- we are going to feel this more from 2015 on.

A - Roger Downey {BIO 7419641 <GO>}

Well you're absolutely right in terms of your views on Mozambique. Obviously, things will be transformational once we have the world-class operations and we fully dilute our capacity with production. And we have been today penalized by the fact that we can't move the coal to the markets.

Regarding fertilizer, yes, it was a very tough year in 2013. We saw big disruptions in demand. The rupee made it -- the devaluation of the rupee made it very difficult for the Indian market to retain and remain a big importer of fertilizers throughout the year, and also they had some inventory.

So we saw one of the biggest players in the market exiting at the same time that a big phosphate mine entered the market. I'm talking about Maaden in Saudi Arabia. So we had an increased supply matched immediately with a sharp decline in demand.

What happened is that we saw a lot of those tons loose in the market, and they all came to Brazil. Brazil is still presenting a lot of growth. Brazil is being eyed by every fertilizer producer in the world as the growth market. So it's natural that whenever you have changes in the environment like that that Brazil is going to be hit hard.

So what we saw is very aggressive pricing, especially on behalf of Asian suppliers. And we saw SSP, superphosphate prices, as low as $120, $130 per ton in Brazil. So that's -- we're talking very, very low prices indeed.

Having said that, in terms of discontinuities and our operations in themselves, two things we'll certainly see in 2014 related to 2013. First of all, in 2014 we -- in 2013, sorry, we put in a new plant in Uberaba, a new SSP plant and a new phosphate bicalcium plant, and they started ramping up at the end of last year. So we will have a -- and these are new plants, so they will have lower running costs, lower costs, and that will average down our cost in Brazil.

Also, in Bayovar we are ramping up and we are reaching -- we have reached pretty much nominal capacity there and obviously diluting costs as well, and we are using more Bayovar rock in Brazil from mid last year. And that again makes us more cost competitive on the coast of Brazil in Cubatao.

So what we will see is certainly some improvement in our cost competitiveness. We should also see further improvement in markets. Things are looking a little bit better. We've already seen the MAP prices, the monoammonium phosphate products -- which normally are leading indicators as to where phosphate prices are going, we've already seen an improvement there, which means that we can be optimistic about where the fertilizing industry is going this year.

And with regards to potash, yes, we have seen big disruptions in the way -- in the market structure. However, if you look back over the past decade, it only went back to where it was before, a market that's between four or five players. Even though BPC is still a bit of a question mark there, we also have indications that things are back to normal.

So the pressure on prices has been lower than anticipated, I think. And that just tested the appetite for potash in markets in general. And again, our business plan is focused on Brazil. Brazil can't get enough potash. And as a result, we still find Brazil a very promising market for our fertilizer business. Thank you.

Operator

Renato Antunes, Brasil Plural.

Q - Renato Antunes {BIO 17439917 <GO>}

Good afternoon. Thank you for taking a follow up. And the question is simple. On the S11D project, you mentioned in the presentation it was a 30 year mine life. I just wanted to confirm that this already takes into account the impact from the whole preservation of caves story. This is the first one.

The second one, just to clarify, I mean if you could, out of your volume growth over the next five years, you mentioned a 453 million, I think, production target. How much of that comes from your South System? If you could just give us a sense on how much is coming from the South System, it would be great. Thanks.

A - Murilo Ferreira {BIO 1921488 <GO>}

Vania, please?

A - Vania Somavilla {BIO 15867577 <GO>}

Good afternoon, Renato. Regarding the life of S11D, we got the license in July 2013. And all this cave story is already concluded, and concluded in the license process.

So we have already got to preserve 137 caves, and these are also included in the studies that you have mentioned. So we consider that the caves issue in S11D is overcome.

A - Murilo Ferreira {BIO 1921488 <GO>}

Martins, the last?

A - Jose Carlos Martins {BIO 1715332 <GO>}

So to ask you again, in which period are you asking the increase in the production of the southern area against the north area? Which period you are considering?

Q - Renato Antunes {BIO 17439917 <GO>}

The long term target you guys provided. I think it's 453 million, if I'm not mistaken. I think it's a five year target, not referring to the short term. I think it's in 2018.

A - Jose Carlos Martins {BIO 1715332 <GO>}

So if you look -- so, Vale will increase production until 2018 to 436 million tons, okay? That will be our target production for 2018.

From this -- a big part of this will come from the North System, because in the southern area a big part of the capacity increase, the projects will be to replace depletion and also to increase quality and to extend the mining life.

So the increase in production in the southeast area and southern area will be marginal. If you look long term, the total increase will be around 10 million tons only, because the big part of the increase will come from the north.

In the Southern System and the Southeast System, because the ore produced in this region is also high cost, it has a higher cost than in the north. Our idea is to keep using the logistics system that we have. So we want to keep optimizing our logistics assets, which is very big in this area. So the big increase in our production will come from the north area.

A - Murilo Ferreira {BIO 1921488 <GO>}

Thank you very much for being with us in this conference call. And before going today, I'd like to say thank you for your comments. Your comments bring us more motivation.

For sure, we are very focused on the discipline in capital allocation and to bring returns to our shareholders. Thank you very much.

Operator

Thank you. That does conclude Vale's Fourth Quarter 2013 results conference call for today. Thank you very much for your participation, and have a good afternoon.