Q1 2020 Earnings Call

Company Participants

- Eduardo Bartolomeo, Chief Executive Officer
- Luciano Siani Pires, Executive director, Finance and Investor Relations
- Marcello Spinelli, Executive Director for Ferrous Minerals
- Mark Travers, Executive Officer for Base Metals

Other Participants

- Alex Hacking, Analyst
- Alfonso Salazar, Analyst
- Andreas Bokkenheuser, Analyst
- Carlos De Alba, Analyst
- Christian Georges, Analyst
- Jon Brandt, Analyst
- Sylvain Brunet, Analyst
- Timna Tanners, Analyst

Presentation

Operator

Good morning, ladies and gentlemen, welcome to Vale's Conference Call to discuss First Quarter 2020 Results. At this time, all participants are in a listen-only mode. Later we'll conduct a question-and-answer session and instructions will be given at that time. (Operator Instructions) As a reminder, this conference is being recorded and the recording will be available on the Company's website at vale.com at the Investors link.

This conference call is accompanied by a slide presentation also available at the Investors link at the Company's website and is transmitted via Internet as well. The broadcasting via Internet both the audio and the slides change has a few seconds delay in relation to the audio transmitted via phone.

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. Eduardo de Salles Bartolomeo, Chief Executive Officer; Mr. Luciano Siani Pires, CFO; Mr. Marcello Spinelli, Executive Officer for Ferrous Minerals; Mr. Mark Travers, Executive Officer for Base Metals; Mr. Carlos Medeiros, Safety and Operational

Excellence Executive Officer; Mr. Luiz Eduardo Osorio, Executive Officer of Sustainability and Institutional Relations; Mr. Alexandre Pereira, Executive Officer for Business Support; and Mr. Alexandre D'Ambrosio, General Counsel and Mrs. Marina Quental, Director of People. First, Mr. Eduardo Bartolomeo will proceed to the presentation of Vale's First Quarter 2020 performance and after that, he'll be available for questions and answers.

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

Eduardo Bartolomeo {BIO 15365202 <GO>}

Okay, thank you. Good morning, everyone. First of all, I hope that you and your families are well and able to maintain social distance. This will be a very decent call as our management team is also apart from each other, each one in its house or office.

First thing I would like to point out is that Vale facing this unprecedented scenario brought by the COVID-19 with responsibility, discipline and sense of urgency. This management team we have been managing the company remotely. Just to give you an idea, we went from 600 to 20,000 remote access and we continue to operate our assets.

Definitely, we are in a war scenario, with a common enemy. For this reason, Vale joined forces with communities, governments in our value chain with a humble attitude to win this war. That main message that we have been communicating to our employees, partners are resilience and overcome.

Resilience because of this war will not be a quick one. Overcoming because I'm sure that we'll succeed and come out much better as a company and a society. I also want to emphasize that our effort with the full reparation of Brumadinho remains firm. Finally, reparation, safety and people remain our priorities in are very up to date in the face of this crisis. Would you please pass the slide.

Well, we have a very solid plan to face the pandemic. In January, we started to monitor the scenario and to structure implement preventive and safety actions. Our response plan is ongoing and is updated constantly. It has five fronts, which prioritize first the continuity of the reparation of Brumadinho and our dam safety our actions, the health and safety of our employees and our neighboring communities, the support in fighting the pandemic honoring our new pact to society, the support to our value chain and finally the stability of our business. Would you please pass the next slide.

As I said earlier, our effort to fully reparation of Brumadinho remains firm and goes together with our actions during pandemic. We remain committed to the reparation and so far almost 7,000 people our part of the civil or labor agreements already signed, which totaled about BRL3.6 billion with emergency aid paid so far as well. Regarding safety, the dam decharacterization plan remains on track in our daily management system is improving. We have implemented the function of the Engineer of Record as an additional step in assessing our structure in Brazil. The Engineer of Record is external for the operations and is directly linked to Vale's line of defense. Thus, our commitments to Brumadinho and safe continue. Please, if you go to the next slide.

Second front of our plan addresses the health and safety of our people, which is our top priority. In all of our operations, we have implemented world-class safety standards to face the pandemic. And we believe we would one of the first companies in Brazil cut off the home-office a regime on March 13.

On the slide you can see we mentioned the name at-risk, but the watchwords are safety and discipline at home, in our operations at all times. So far, three sites have adopted more restrictive measures as we already disclosed in Malaysia, Canada and Mozambique. Although the impacts COVID are currently contained, advance in the pandemic may lead to more restrictive measures in these or other operations.

Could you please go to the next slide. We are fully aware of our responsibility to society and our essential role in the economy. At the same time that we took our operational actions in a listening process we offer support to society. We have already committed BRL500 million to fight the pandemic in Brazil, of which BRL353 million were already spent. But it's not just about financial resources. We made use of our logistics structure in China, where we have been present for almost 50 years to purchase and bring to Brazil over 30 million personal protection medical equipment and 5 million rapid test to detect new coronavirus. In total 15 cargo planes will bring these volumes. In addition we are providing resources to expand the capacity of existing hospitals and to build huge hospitals in territories that we operate. In other countries where we operate, we have also made important donations to the healthcare system, for example, in Malaysia, Mozambique and Indonesia.

Next slide please. On the front of our value chain, we are committed to keeping it very healthy and preserving the jobs. Any time when we are experiencing great uncertainty, we are using our presence at the base of the production chain to help our suppliers face the pandemic. We have anticipated payments to around 3,000 small and medium-sized suppliers in Brazil injecting over BRL900 million into the local economy to-date. We have also provided financial support to the contractors and projects suspended by us so far. We believe that with these actions we are helping society overcome together the challenges of this crisis.

Next. Finally, we continue to stabilize our production. In the first quarter, the impact COVID in our business were limited but there are still many uncertainties, therefore, stabilizing of production remains a challenge. We started to see the fruits of our work in North Atlantic, with a solid week of production in the first quarter this year and the last quarter of '19, as a consequence of relevant actions to stabilize the value chain that we took last year. In other word, quarter was very difficult. On the positive side, we hope to resume Timbopeba activities as early as next week. This is another important step to resume and stabilize our iron ore production in the Southern and Southern leases system. Next slide please.

Well, as we've been saying, in addition to the pandemic plan, which also addresses the reparation of Brumadinho, the improvement of our safety, and the stabilization of our production, capital discipline is fundamental to the (inaudible). We have been reinforcing this point in other opportunities.

In this regard, I would like to point out the withdraw $5 million from our revolving credit. We continue with our approach of prudence reinforcing our balance sheet to face an environment of great uncertainty. It was an insurance at an interesting cost increasing our margin of safety.

Finally I'd like to reinforce, as I said, that we keep working quickly in risk quality in the reparation of Brumadinho and to reduce the uncertainties regarding the COVID-19 impacts. With that, I believe that we will have better conditions to restore our dividend policy.

Next slide please. Well to conclude, given this context I'm sure that Vale in a solid position to face critical scenario. Iron ore is one of the least impacted commodities to-date. Our main market China is already recovering, although we can expect a reduction in Europe or in some other countries as well. Moreover, Vale has already proven that it's capable of resisting and recovery. The commitment of this Executive Board and our Broad of Directors is to continue to do everything in our power to ensure the safety of our employees and our operations.

Finally, I want to thank very much our employees and partners for their efforts over the past weeks.

I now pass the floor to Luciano so that he can detail the results of the first quarter, 2020. And thank you all for your attention, I will be back for the Q&A. Thank you.

Luciano Siani Pires {BIO 15951848 <GO>}

Good morning, good afternoon. I'm going to address five items here today. First item costs. As you saw costs were high in iron ore in the first quarter $16.2 per ton. It's seasonally high because of low volumes, but we had even lower volumes this quarter and we also had some additional impacts like the merge in the north, the lineup of vessels like waiting for to be charged because of problems with moisture and for the excessive rains in the north and we had also problems with maintenance. We had a fatal accident in Mozambique in one of our conveyor belts in January. So we stopped and did extra work in all of our conveyors around the world, including the iron ore conveyors. And so we spent a little more on maintenance.

We had a little offset for the exchange rate. But the final result was the 16.2, you saw. The outlook for next quarter is of a slight decline but very marginal because we still have some important effects that will weight on costs. The first one is the carryover part of what we produced has gone into inventories at a higher cost, so it will impact next quarter.

Some COVID-related expenses. For example, we're providing additional benefits for our employees, which may weight $0.30 to $0.40 on the costs next quarter. And because we are resuming operations in Timbopeba, for example, which is higher cost, because it's not going to be a blasting operation, we're not going to use explosives. We're going to use mechanical dismantling of the ore. So it's going to be high cost and also because of the mix we're going to have more ore being sold from the South and the Southeast. We are also undergoing the scheduled 10-day maintenance of the long conveyer belts in S11D as we speak. So mainly also small effects that will add up and will not allow us to see the major impact of the currency devaluation on cost on the second quarter.

However, in the third quarter, we're very confident that with cost dilution, with no maintenance we're going to run certainly below USD14 per ton. And if the exchange rate continue at current levels, certainly, maybe even at USD13 per ton. The second topic is freight. You also saw sharp declines in spot freight rates and in the oil price.So how is the outlook for freight within Vale, given that the decline was very small this quarter just USD1 per ton to USD17 per ton. While the spot freight rates will not influence also freight in the second quarter because Vale uses mostly the spot market when it produces more. So -- because the production in the second quarter is not as high as in the third and the fourth quarter, the use of spot affreightments will be naturally smaller. So we will use more of our own fleet.

But in the third and fourth quarter, If the spot rates continue to be lower, we're also going to go more to the spot market and will take advantage of that. But the oil prices you will see a significant impact already in the second quarter. Vessels are refueling, actually we even had a small increase in fuel costs this quarter because of the IMO regulations and the -- because we fill part of our fleet with the low-sulfur oil, which is more expensive. But starting from next quarter you will see the impact and we are forecasting a decrease of at least $3 per ton in freight rates next quarter.

The third aspect is foreign exchange. We had a 29% devaluation of the Brazilian real, in the quarter end-to-end, very unusual. Compares only to what happened in the third quarter of '15. And as the balance sheet of Vale officially everything is measured in Brazilian reals there are all sorts of impacts from such a devaluation in our accounts.

And I would like you to pass on to the first slide after Eduardo presentation, where we show a number of the balance sheet accounts that are -- were heavily impacted by the devaluation in this quarter. So, on the right-hand side you see in blue, commitments of Vale Brumadinho, REFIS, Samarco and Renova in our gross debt and the numbers you see already translated in US dollars are the declines in those liabilities, given the devaluation.

So those liabilities are originally measured in reals, but when you translate them back to US dollars to present the accounts for you, they have as much smaller value. So, almost USD3 billion declines in the value of commitments, which is very good for Vale.

But on the asset side, we do hold balances in cash in Brazilian reals, actually, we were holding a lot of Brazilian reals when the devaluation came so those same balances when translated to US dollars they lost 914 million in value. And then you have the losses on the swaps because we have so many commitments in the Brazilian reals, and we see ourselves as a company, we manage the company in US dollars. We hedge part of those commitments in Brazilian reals back into US dollars, and this a USD1 billion is the offsetting effect of some of the declines you see in blue.

So some of the declines were actually not naked, they were hedged, and this is the offsetting effect and that flows through our balance sheet -- to our income statement, because this is a derivative instrument so that flows into the financial results.

But net-net as you can see there is a positive gain and also because Vale has paid amounts related to Brumadinho into REFIS the expanded net debt when you add on top of Vale's net debt, all those commitments has reduced substantially over the quarter being a major shift in order balance sheet position.

The fourth item is cash flow generation. You saw that the cash flow generation in the quarter was relatively small compared to past first quarters. It's naturally also seasonally lower and the biggest impacts were from inventories and working capital, the accounts payable. The inventories were part decision of Vale. For example, we decided not to sell nickel at those depressed prices. We also sold less copper than we produced, we sold slightly but less iron ore, then we produced. So we have a USD200 million buildup in inventories mostly expanded play in base metals.

On the accounts payable, we had some important payments on the quarter. The first one is the take or pay in the South System of MRS, so because we are not transporting enough ore through the railway which is jointly owned with other companies, we had to pay the top-up for the take or pay in this quarter of USD120 million. You should not expect this obviously to repeat itself in the second, third quarter, that's a yearly expense.

And we also had a USD200 million payment -- profit-sharing for our front-line employees. So a number of one-off expenditures. Some of them unique, some not so one-off like the profit-sharing, but that affected cash flow generation in the quarter. But looking forward, we expect cash flow generation to again be robust as the working capital accounts, they recover themselves. So to boost cash flow.

Finally, COVID, some highlights on the financial impacts. I'm not going to discuss volumes, because volumes were already considered on the guidance that we made public last week on the production report, I'm not going to discuss prices. This we may speculate here in the Q&A session. But I'm focusing here just on cost and expenses, out of pocket expenses because of COVID. And the ballpark number that we see so far, including not only what we already spent, what we look forward over the next few months is USD500 million. And they will appear in many different accounts, including -- the most part of this is expenditure with the stoppage of projects. For example, it's costing us USD55 million to stop the project in Canada in Voisey's Bay, stoppage of projects in Brazil is costing about USD50 million per month. And this will not flow through EBITDA or income statement. This will accrue to the project costs, but it is an economic impact.

We will spend about USD100 million in humanitarian aid. We have also capital injections in our steel subsidiary in the north of Brazil need to be made. We had some benefits for employees about USD50 million each of those accounts. So when you put this altogether, the estimate is about USD500 million of out-of-pocket additional costs and expenses for Vale.

And finally, if you think about other impacts on cash flow, you're seeing that we're supporting our value chain, we're supporting suppliers with advanced payments, we may support clients, but this will be mostly offset by the savings, the temporary savings on CapEx because of the stoppage of projects, although they are costing us economically, we're spending less than if they were at full steam and the works were ongoing. So, therefore, as you saw CapEx guidance was revised downwards and should basically be offsetting the working capital deterioration because of the support to the value chain.

With this, we can open for questions-and-answers.

Questions And Answers

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions) Our first question comes from Carlos De Alba, Morgan Stanley.

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

Good morning, everyone. Hopefully you and your families are doing well. Just a question we have, starting on dividends. I understand the difficulty of the situation, clearly not only Brumadinho but the COVID-19 pandemic and the pressures that this puts on the company's different stakeholders and how the company is responding very responsibly. But can you maybe Bartolomeo or Luciano will give us a roadmap or what needs to happen for the company to resume the dividends. Clearly it has a strong balance sheet, it generates very strong cash flows and at some point, I think it -- the company wants to resume dividends, but I just wanted to understand how do you see the roadmap ahead?

And then are there any other potential uses of cash. Like you, buying back the preferred shares that were sold a few years back, or other uses of cash that could improve the cash flow generation going forward? Thank you very much.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Thank you, Carlos. Our families are doing well, thank you. I think dividends is a thing that the roadmap as we've been saying since the beginning is, the reparation, the quality and the speed of the reparation.

We believe that is undergoing pretty well by the fact, by the way we repaired the environment, the level of indemnities. So I think this is on -- this roadmap is really you online on where we think it should be. What happened is that, you mentioned, the level of uncertainty that brought to us with COVID made us, how can I say that, bring some extra cushion to our balance sheet.

So that's why we took the revolver. Why we did that? We have to look at in a timely basis. It was the beginning of the crisis that impacted us on the beginning in March and we had like -- there were sales risks that we wouldn't see at the time. One is a second wave of contamination in China that still not done but looks even not very reasonable now, but still on the table.

And secondly, any other kind of stoppage in our operations. I think to answer your question objectively, as long as we are able to get back the revolver. I think we are able to do what I meant about capital discipline is to allocate to the shareholders their part. So I think dividend can come back after the uncertainty COVID. It's out of the equation, because we believe that we know the size of the damages that we created in Brumadinho, we are repairing and with that in mind I think after paying the revolver, we could resume dividends. Of course, propose that to the Board of Directors and resume our policy. For the use of cash I would like to ask Luciano to elaborate a little bit.

A - Luciano Siani Pires {BIO 15951848 <GO>}

Carlos, we used USD800 million last quarter of last year to buy back the preferred shares and there is already a benefit this year, so there will be not USD200 million outflow towards those preferred shares because we bought them back. And we do not anticipate any other major alternative uses of cash. So the cash will be redirected towards the shareholders once we repay back the revolver.

Operator

Our next question comes from Jon Brandt, HSBC.

Q - Jon Brandt {BIO 5506998 <GO>}

Hi, good afternoon. Thanks for taking my questions. Kind of a follow-up the Carlos's question, I know you've talked a lot about UAD10 billion in net debt, but if you look at sort of your adjusted liabilities including Brumadinho, and Samarco, and the REFIS et cetera, total liabilities is closer to USD15 billion.

So I guess sort of a two-part question, are you saw comfortable at that USD15 billion level or would you look to potentially, especially given that the weak BRL, would you look to maybe prepay a portion of that sort of non-debt liabilities? And then if you could just sort of explain once you're cleared for dividends, given the weakness in the share price, how do you look at sort of the cash dividends versus buybacks at this point? Thank you.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Luciano, go ahead.

A - Luciano Siani Pires {BIO 15951848 <GO>}

Okay. John, the do you reason why we talk about those USD15 billion on expanded liabilities is to call your attention that when we think about capital allocation, w have in mind those additional commitments. That's the purpose. The USD10 billion net debt target was established in a situation before the Brumadinho dam rupture in which we already had part of those additional liabilities.

So we already had paid fees at that time, we already had Samacro and Renova liabilities and we established the USD10 billion considering those commitments already. But today we stand at USD5 billion, right, the headline net debt without those additional commitments. So you may see. Okay. So now you're USD5 billion below your original target which you established when those additional commitments were already there.

However, there is one additional commitment that was not there when we established the USD10 billion target, which is Brumadinho itself, which today stands at USD4 billion in our balance sheet. So you may say, you are USD5 billion below your original target but you have an additional commitment that did not exist of USD4 billion when you establish that target. So today we are slightly better, so to speak then the target we set, which means that we don't intend to make additional uses of money in order to payback any of those that headline debt or those commitments. In fact, we cannot pay because they have a schedule, which is not controlled by us. REFIS and Brumadinho and Renova, it's as we execute on our programs.

So, therefore, the money generated will be available fully to return to shareholders. We frankly do not believe that in a post-COVID world in a world where we repay back the revolver that the share price will continue to trade at today's levels. And I'm not saying because I have a strong opinion on Vale share price. I'm just saying that all share prices, all equity prices across the world are affected by COVID-19 and Vale is no different. So we will need to make that decision of dividends against buybacks once we see what the new normal level for the Vale share price will be after we repay the revolver.

But if you ask me what my bias is obviously we did a -- the last time we did a buyback was the prices, which were above today's prices. So a buyback option if it was today would be strongly considered as an additional option for capital allocation at today's share prices.

Q - Jon Brandt {BIO 5506998 <GO>}

Great. Thank you, Luciano. Very clear.

Operator

Our next question comes from Alex Hacking, Citi.

Q - Alex Hacking {BIO 6599419 <GO>}

Good morning. Well, I guess good afternoon in Rio and thanks for the call. So a couple of questions. Firstly, could you give us any update on how demand for iron ore is outside of China? I guess in April is it possible to quantify demand from Europe, Japan, Korea elsewhere? That would be helpful.

And then the second question on your iron ore operations in Brazil and operations in Brazil in general, how are the logistics there? I think you gave us an update about a month ago Luciano and you said there were some challenges, but things were basically going okay. Has it gotten I guess better or worse since then? And are there any concerns that you have around your ability to kind of keep the operations going in Brazil? Thank you very much.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Go ahead, Spinelli.

A - Marcello Spinelli {BIO 16240257 <GO>}

Thank you, Alex. Thanks for your question. Well, update about ex-China demand is a challenge. It depends on how would be the duration of the crisis, but we have some figures about this. Europe, we see they were really fast to downstream and upstream decisions shutting down operations. The main impact was the automotive production and also the steel, different from the Middle East. Middle East is -- we have an additional crisis is the oil crisis, the basis for the growth. We see that they are struggling with the same problem with demand, but they are trying to keep the price and they do you have a breakeven with the compare with these scraps, they compete with the process of production in Middle East, so we see a problem, different from Europe. And Japan, they are a little bit delayed compared to Europe but now they are now slowing down production automotive even construction. We have some problems coming from fuel. But now, how will be the crisis is the question. What we see that part of the demand will or the supply will go to China, but even the supply is being affect in many regions in the world. So we have -- you offset this extra iron ore that go to China, China is back. And regarding the iron ore operations, obviously, we have really -- we are learning with the COVID actually. So we've been doing a lot of effort for our social distancing, we reduced a lot of workers in our plants, almost 6%, to guarantee that we have less people in the canteens or even inside the buses. We are scanning body temperature, we start now the test of our team and also contractors and it is very important to understand that this is a daily process that to control the absentees. So we have a daily checklist that the people can find this, if they have any symptoms of they have a problem. After that, we can track the people and put them in quarantine, so the main thing here is to guarantee the health of our people and also the other people that had contact with the people. So this is a daily process that we need to keep the operation. So far, we didn't have a problem in logistics in any of our operations, but we are just in the middle of this crisis.

But we think that we are seeing that there will be the new normal. So we need to be good to guarantee that we have a great control and also using technology, GPS technology to track people, to guarantee that they are health and to keep the operation. So this is the problem that we're facing now.

Operator

Our next question comes from Timna Tanners, Bank of America Merrill Lynch.

Q - Timna Tanners {BIO 6766897 <GO>}

Yeah. Hey, good afternoon and thanks for the detail. I hope everyone is healthy. I wanted to follow up with Alex's question just to get a little more on the timing of the European recovery and how we think about the translation to pellet premiums. And then if you wouldn't mind giving us an update on the co-operations and your progress there and what governs the decision to stay offline and how that could proceed going forward? Thanks.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Hey, Timna. I'm going to answer your second question. I ask Spinelli to elaborate a little bit more about European recovery. About Moatize, we are still on track to do the plant's -- overhaul of the plants, because of the lockdown that happened in South Africa and Mozambique we had to postpone.

So due to that we're going to have to reschedule. That is the good side on it because we can plan better, in a better way, but we don't know time frame for that. That's unfortunate, that's the fact. By the way Mozambique and coal's operation that it has been more mostly heated by the COVID on this example that I just mentioned about the intervention of maintenance.

And secondly about them the demand -- India is our main customer and was locked down as well. So it's created a problem. We were operating better well in March that creates an optimism about when we come back we've come back with the overhaul, with the improvements that we see.

But, of course, we need market as well, but anyhow, in a nutshell I think Mozambique, we need to do the overhaul, we need to prove, we need to correct that asset quick to run at a 50 million ton rate and then decide what we're going to do, not the way -- not the other way around. And I'm going to discuss about selling JV anything before we correct the asset. But to correct the asset we are going to need a window after COVID. And for the European recovery, Spinelli?

A - Marcello Spinelli {BIO 16240257 <GO>}

Well, Europe I think as I mentioned, they are really fast to say but you see, we have many scenarios similar to see this. Definitely there will be a double-digit reduction. Depends on, again, the duration of the recovery. We don't -- if you consider six months to go back and even not to the same level, it will be something between 10% or even 30% reduction of production this year. So this is really -- there are a lot of uncertainties. We are tracking some leading indicators. We have some information from satellite that you can see people now going back to other factors trying to reestablish. We see some announcements during May that some governments are returning to their operations. Again, there will be a new normal. The fact that it will be an impact, definitely it will be double-digit, but we need to track how it's going to happen, the evolving of the disease.

A - Luciano Siani Pires {BIO 15951848 <GO>}

Tim, just -- Luciano, just to complement on coal. It's disappointing that the month that we had a very good production March, which was almost 11 million run rate was followed by a month in which demand collapsed. So, in April, we are going to produce about 700,000 and maybe less in May. Not because we are not able to produce but because we don't have where to storage -- to store more coal. We cannot sell coal into China because of specs of our coal. So unfortunately we have that situation, but just to give us some color because although the operations run really well in the next month, they are going to be severely impacted.

Operator

The next question comes from Christian Georges, Societe Generale.

Q - Christian Georges {BIO 1557701 <GO>}

...for holding this call. Two questions, the first one on the pellets again, assuming that we can see a relatively high-risk that European demand is going to be seriously affected. Your (inaudible) one and two, were stopped in the first quarter. I mean would you be considering not restarting them in coming weeks?

And the same question also does it makes sense to maybe slow down the restart of Samarco or are you adding on Samarco as you were planning to, in the first place?

And my second question is on the Brumadinho and saw some headlines that you may be finding a solution to divest the operation. I mean is this realistic or is the closure a more likely outcome? Thank you.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Thank you, Christian. Let me begin with the (inaudible), and then I'll pass to Mark to elaborate a little bit because I think we have some by the way follow-up that -- what we said to you in the past and a good follow up by the way because we closing the refinery. And I believe that we are on good approach to exit the business healthy.

So I would ask Mark to answer and then Spinelli could elaborate on balance as well, and so Mark I can come back to the questions as well.

A - Mark Travers {BIO 16687422 <GO>}

Okay. Thanks, Christian for the question. So Eduardo has already addressed the closure of the refinery, which is progressing well and we should see the last of the material running through the circuit by -- in the coming days by next week. But so just so that brings us to the exit strategy for Vale New Caledonia, which we announced back in December of 2019. As you'll recall from prior analyst calls, we mentioned that the process with Rothschild's circuit for investors is progressing well. We did have nonbinding offers received at the end of February and we are progressing fairly well with a couple of potential investors. And, of course, the crisis did come in March and -- but we don't think that will impact the process too much.

So we have a good level of confidence that we should be finding a potential investor in the next month or two. So we would say that that's the route that's higher likelihood than a closure at this point in time.

A - Marcello Spinelli {BIO 16240257 <GO>}

Okay. And what about balance Spinelli, then I go back to Samacro. Thank you for the question. Regarding the pellets, first, we decided to change the guidance from 44 to 35 to 40, but this decision was related to the different production side, the supply side, we are limited with pellet feed coming from Brucutu. You may have seen that we are struggling with the return after the full operations in Brucutu waiting for new assessment in the Laranjeiras dam. But now after COVID we are checking, if we have demand for those pallets. So again, the main thing is value over volume, we are not going to produce more than that we need. Our market -- natural market is Europe, JPT and also the Middle East. The problem now is a temporary problem that's not related to price, but the demand. So we check this decision every day actually, so we can -- we are flexible to shutdown some plant and sell directly pellet feed to China or even blend in BRBF. So we are taking the decisions every day. If you don't have short-term demand, we can switch the program and keep the best margins.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

And, Christian, about Samarco. I think Luciano is back, right? And Luciano is our Samarco expert. But the rhythm ramp up and the commitment to come back with Samarco is not changed. But if -- if you want to elaborate Luciano on Samar, can you? I don't think Luciano online, but I think just answering your question, we are coming back on -- I think I'm out.

Operator

Our next question comes from Sylvain Brunet, Exane BNP Paribas.

Q - Sylvain Brunet {BIO 3194710 <GO>}

Hi, good afternoon. Two questions for me, please. First one on iron ore flows. Just if you could give us some indication, even in broad terms on how much more business you did with China or Asia in general in April versus March. So we get a sense of your ability to address and redirect flows there?

And my second question is a bit more on the modeling side maybe Luciano has a way to help us with some sensitivity around hedging, if there is any rule of thumb that would help us through the P&L with the impact of the reals? Thank you.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Okay. I can take the first one. Well, China is back actually, they have really put in a lot of effort scheme of those to -- to put the economy back. We have many indicators. More than 90% of the infrastructure projects are back and we have a very interesting information from ore properties, they sold more than 130% in April compared to March.

And still we have a record -- high record last week in price -- in sales, sorry for rebar. So China is trying to make the best effort to fight against the worst scenario that they face. So we are sold out in China actually and in from the -- since last year after Brumadinho, our market share -- see there the wholesale -- and Europe was level -- lower level than in the past. So our exposure in that region ex-China wasn't really high.

So we don't have any problem to sell more products in China in -- we need to remind -- probably you remember the last call, we said that we have -- we still have to make up better inventory of BRBF for the blending. And we sold almost the full stocks in the end of the year -- last year, and now we are rebuilding the inventory.

So we have -- the inventory is our source of the demand, but actually we are selling the whole BRBF we have and also Carajas fines.

A - Luciano Siani Pires {BIO 15951848 <GO>}

Okay, Luciano, before I answer to Sylvain just back on Christian's question on Samarco. Hard commissioning will start in July, the filters are being installed, so we are on track for December although we had a little bit of buffer and we are eating up on this buffer, but December 2020 is our best guess still for Samarco restart. On the hedge as you saw we had approximately USD1.1 billion change loss in the value of derivatives, currency derivatives. This is an accounting economic loss because we do not pay this. This will -- those derivatives they match the profile of the debt. So if the reals stands where it is for the next 7 to 10 years, that's how we are going to realize those losses in terms of the cash flow, but I show the -- the slide I showed in the mine production, it shows that the value of the rial denominated debt decreased by USD500 million -- approximately USD500 million, so part of this hedge it is actually the offset of the decrease in the real denominated debt of Vale. So in other words, when we took those liabilities, we immediately swapped them back into US dollars, because it was convenient at the time, it's a policy of Vale to try to put its commitments as much as part in US dollars.

So, the value of the debt declined by USD500 million, we're losing USD500 million out of the USD1.1 billion in the derivatives, but still there is another USD600 million of losses and those USD600 million actually they were entered into in order to hedge the commitments of Brumadinho, Renova, REFIS, but only a partial hedge.

So as you saw also on the slide that I showed the -- those other liabilities significantly decline in value in the Brazilian real, to the point that our expanded net debts, so to speak, the way we define the release has decreased by more than USD2 billion. So all in all, even in the balance sheet, the situation is extremely helpful and favorable for Vale the devaluation of the Brazilian real.

It happens that the only thing that flows through the balance sheet on all those things on Brazilian reals is the change in the value of the financial derivatives, the derivative instrument. The other changes do not flow into the income statement because originally the income statement of Vale is prepared in Brazilian real. So in Brazilian real there is no change. So there is no impact. It is only translated into US dollars to show to you.

So that's the logic behind the hedge.

Q - Sylvain Brunet {BIO 3194710 <GO>}

Thank you.

Operator

Our next question comes from Alfonso Salazar, Scotiabank.

Q - Alfonso Salazar {BIO 18358082 <GO>}

Thank you. Most of my questions outside iron ore have been answered, but I have one about the base metals division and specifically nickel. You have been optimistic about demand increasing from electric vehicles revolution, but with auto industry facing very challenging times probably things have changed and electric vehicles investments -- investing in electric vehicles is not a priority at this point, so if you can provide an update on the short term and longer-term fundamentals for nickel in your view? And how you plan to adapt to market conditions, so you can maximize the value of your nickel reserves and perhaps you can leave it out at this point to VNC and focus on the other nickel assets that you operate? Thank you.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Thank you, Alfonso. I think we pointed out, very -- very clearly, we are exiting VNC focusing our world-class assets in both Canada and Indonesia. So -- but you will see we also raised a very interesting point about the change in -- how can I say, the expected patience about the electric vehicle. I believe this is a short-term problem, but I'll ask Mark to elaborate because I'm not running base metals anymore. So Mark must have more view on that. But we're still positive on EV for sure.

A - Mark Travers {BIO 16687422 <GO>}

Yeah that's right, Eduardo. Thanks, Alfonso, for the question. And I would echo what Eduardo just said is that in the short term there definitely is an impact. In particular, the EV market in China in the first two months obviously a significant drop. We don't see as much of an impact in Europe this year. But in terms of Vale exposure in the short term, it's not that significant. And especially as we are excluding the VNC results from our guidance, et cetera.

But -- and in fact, the product that we do sell from VNC into the market, the VNHC nickel hydroxide cake is actually doing fairly well and we've had some good contracts recently. So in the short term, it certainly is impacting the overall growth of the electric vehicle demand for nickel and we will see -- we will see a decreased demand overall in the market for that material.

As we would see, we think in the stainless steel market overall. So our overall view in the short term, including electric vehicles, is that we probably will move from what we expect it to be a deficit this year to a surplus of nickel -- in the supply-demand equation. That said, we are a strong believer in the growth of electric vehicles in the coming years and we remain committed to that.

Operator

Our next question comes from Andreas Bokkenheuser, UBS.

Q - Andreas Bokkenheuser {BIO 7182883 <GO>}

Thank you very much. Just one question from me and I'm not sure whether that's one that's easy to answer, really, but how do you think about your kind of long-term breakeven cost to China, given the new situation we're in? I can definitely see how your cash cost will come down when you ramp up volumes again because it will dilute the fixed cost base. And I can definitely also see how currently lower oil price benefits you on the freight side. But if we kind of look beyond that once you start putting more volumes back into the market and assuming that oil prices kind of recover from here. I would expect freight rates to go back up again and maybe even coupled with some BRL strengths, which I fear could end up offsetting some of the cost savings you would you be getting by ramping up production.

So when I kind of look at your breakeven cost to China it's gone including which sustaining CapEx and then pellet adjustment and so on. We've seen that breakeven cost of China, go from early 40, sorry, early 30s per ton to now basically USD49 a ton. So how do you think about that USD49 going forward? Is that something we are going to see go back into the 30s are we going to stay in the 40s and again I realize, see a lot of this is going to depend on freight rates and BRL and a bunch of other things that are very hard to kind of to look at. But just to get your kind of broad view on where do you think we kind of like even out in the longer-term here?

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Okay, Andreas. This is a tough question really. I'll ask Luciano to answer that because it's so fluid, everything is so correlated, when you talk to iron ore or talk to iron ore price and it's very short term problem, but I think we do some more exercise as well here.

A - Luciano Siani Pires {BIO 15951848 <GO>}

Yeah. Andreas. The last time we had more stability in our production was in 2018 and we were very firm and very close to USD30 per ton all-in costs without sustaining capital. And at the end of 2018 with the increase in premiums we went actually below, we got to USD28 per ton and that would normalized higher oil prices, higher spot rates and so on.

And at the time we were discussing how we could do some internal self-help and work with digital transformation, with efficiency in order to try to get this down to USD25. I would say that in a normal life situation, we would be naturally back to that USD30 per ton, ex-sustaining capital, perhaps a little lower, because at that time S11D was not fully ramped up and we would be in a more stable, steady-state. We will be targeting again goal and try to aim at USD25 per ton. So the logic of Vale per COVID pre-Brumadinho was pretty much like, okay, give me a USD60 long-term iron ore price.

I'm going to shoot for USD25 per ton, USD35 margin times 400 million tons, that's a USD14 billion business as the base load for the cash flow generation at Vale and we also have the other business to improve and to fix. That was kind of the long-term view and I think we're going to get back to pretty much something around this after everything normalizes.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Luciano just to add another point, I think it's part of that is we are building the fleet of Valemaxes and (inaudible) and long-term we're going to have the benefit of that. So this is a long-term view to stabilize lower freight and also with the installation of the scrubbers, we can offset the impact of the low-sulfur bunker.

So it was a another component to guarantee that we are on the right track for the 30s.

Operator

This concludes today's question-and-answer session. Mr. Eduardo Bartolomeo at this time you may proceed with your closing statements.

A - Eduardo Bartolomeo {BIO 15365202 <GO>}

Okay. Thank you. Thank you all for your questions and interest in our results. And I would like to reinforce that we will keep facing this unprecedented crisis with humbleness, responsibility, sense of urgency and discipline. And more importantly with listening, I think it's the new way to see that Vale and I would like to invite you to read our sustainability report. It's a lot there that's going to be shared with you, that of course, we don't have the time to do on this call. Okay. Have a good day. Thank you again, and see you in the next call.

Operator

That does concludes Vale's conference call for today. Thank you very much for your participation. You may now disconnect your line. Thank you.