Q1 2009 Earnings Call

Company Participants

- Eduardo Bartolomeo, Executive Officer, Logistics
- Fabio Barbosa, CFO
- Jose Carlos Martins, Executive Officer, Ferrous Minerals
- Roger Agnelli, CEO
- Tito Martins, Executive Officer, Non Ferrous Minerals
- Unidentified Speaker, Unknown

Other Participants

- Alex Simlert, Analyst
- Carlos de Alba, Analyst
- Felipe Hirai, Analyst
- Jim Richards, Analyst
- Jim Young, Analyst
- Leonardo Correa, Analyst
- Marcos Assumpcao, Analyst
- Tony Rizzuto, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Thank you for standing by and welcome to Vale's Conference Call to discuss First Quarter 2009 results. If you do not have a copy of the relevant press release, it is available on the Company's website at www.vale.com at the Investor's link. At this time, all participants are in a listen-only mode. And 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. The replay will be available until May 13th, 2009. To access the replay, please dial 55 11 4688 6312, access code 454. The file will also be available on the Company's website at www.vale.com at the Investor's section. This conference call and the slide presentation are being transmitted via internet as well. You can access the webcast by logging onto the Company's website, www.vale.com, Investor's section, or at www.brnewswire.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 in Rio de Janeiro are Mr. Roger Agnelli, Chief Executive Officer, Mr. Fabio Barbosa, Chief Financial Officer, Mr. Jose Carlos Martins, Executive Officer for Ferrous Minerals, Mr. Tito Martins, Executive Officer for Non Ferrous Minerals, and Mr. Eduardo Bartolomeo, Executive Officer for Logistics, Project Management, and Sustainability.

It is now my pleasure to turn the call over to Vale's executives. Gentlemen, you may now begin.

Fabio Barbosa {BIO 21197136 <GO>}

Good morning, to you all. It's a pleasure to be here with you. This is Fabio Barbosa speaking. I will start. Then after the presentation, Mr. Roger Agnelli will make some comments as well. Our agenda today involves two major items -- first, how we are dealing with the current environment, and second, how we see the future.

On the first topic, we believe that the performance of Vale First Quarter was a very solid one, given the environment that we are facing. And we posted just at EBIT margin 31.6%, as you can see there. Our EBITDA reached $2.3 billion, net earnings $1.4 billion. We invested $2.6 billion, including the acquisitions that we paid for in the First Quarter. And we managed to keep a very strong balance sheet with our liquid assets position at $12.2 billion at the end of the quarter.

As you can see on the next page, Vale was really affected by the shift we observed in the seaborne market. Vale is the most global company in terms of iron ore market exposure. So we had a very strong presence in every single market in the world. And what we see here in page six was a major change in the geography of the seaborne demand and, of course, affecting Vale sales.

We used to have 55% of our sales in the Western Hemisphere. And in the First Quarter of '09, this percentage went down to 19%. At the same time, this has a direct correlation with the seaborne demand performance that in the First Quarter of '08, 79% of the seaborne was in the Eastern Hemisphere. And in the First Quarter of '09, this number jumped to 93%. So we were affected, more affected than the other players in this case, due to this specifics of the geographies that we operate.

What we face in this environment, we properly react to the circumstances by adjusting our costs. You can see there in the next page that we made a major effort in cost reduction, almost $1 billion if we also add the -- more than $1 billion if we also add the R&D effort that we did in the First Quarter of '09 compared to the Fourth Quarter of '08. Of course, the decline in EBITDA responded was direct result of the decrease in sales volume and also price changes that we observed.

But as we mentioned before, we are not quiet waiting for the better times. We are working very hard to slash our cost structure in order to provide the Company with the financial strength it deserves and to our shareholders with the returns they aspire. So there's a major concern in the way to combine a short-term reduction with enhancement of the foundation of our long-term competitiveness, as we put there. And we believe that those savings will be much more visible over the next six to 12 months.

In the First Quarter of '09, what we can already indicate is that in terms of discretionary spending, we reduced in $89 million several items, like infrastructure and support, construction services, outsources services, travel, advertisement, et cetera, so very important items, very discretionary items that we slashed by almost two-thirds in the First Quarter of '09 compared to the Fourth Quarter of '08. Also, working capital requirement was sharply reduced by almost $900 million.

And the result of this could be visualized in chart 10, as it's also spread in our operations. As we see, the unit cost for iron ore and nickel declined visibly in the First Quarter of '09 compared to the First Quarter of '08, but also on a year-by-year base. On a quarter-over-quarter basis, the decreases were 35% and 23%, respectively, despite the reduction in volumes that were observed.

We achieved that through several measures. We are trying, of course, to work with a leaner corporate center. We are insourcing some activities. We are resourcing, renegotiating contracts with suppliers. We are cutting costs of project developments. We are optimizing plant and labor utilization, optimizing the flow of materials, streamlining line of products, and shutting down higher cost operating units.

At this stage, I would like to invite Tito Martins from our nickel operations to make some comments of what we have been doing in our metal business to cut down costs.

Tito Martins {BIO 3374920 <GO>}

Thank you, Fabio. I think it's important to stress -- and I will not be long in my speech -- but it's important to stress that despite the difficulties we faced in second semester of last year due to the drop in the price in the market, we tried to first to, as was mentioned before, streamline the production and at the same time work on some overhead costs we had in our operations worldwide.

We are right now working on a better definition of some functions, not only in Canada but in the operations in Indonesia and New Caledonia. We do have an extra effort related to the cost reduction when we're talking about the line of products and some specific items of consumption.

I could stress energy and a few consumptions. That's why we decided to shut down part of the operations in Indonesia by the end of the year. And that's why we decided to have the shut down in the following weeks in Sudbury. We decided to do that as a response to the market condition and at the same time to go for a methods process in our furnaces in Sudbury.

Fabio Barbosa {BIO 21197136 <GO>}

We also -- we have promoted a structural shift in our output towards Carajas as we put the earning by '12. And of course, you all know Carajas is a low-cost, high-quality operation. And we just now released our 20-F report and we filed our 20-F report in which we indicate that we are doubling our probable and proven reserves. And now, total Vale reserves in iron ore reached 14.2 billion tons. And Carajas alone, we had 7.2 billion tons of iron ore at 67% Fe content. It's a major reserve. It's the largest reserve of the highest-quality material that's available in the world.

And so, we are supplying this high-quality ore and in relatively high proportions. So we are trying to maximize or capture of the higher value-in-use of our ore. And today, 43% of our iron ore production is coming from Carajas against about one-third in the last five years. At the same time, we continue with our initiatives in terms of strengthening our competitiveness through changes in our logistics and also in our iron ore marketing policy.

In logistics, I would like to invite Eduardo Bartolomeo to comment on what we have been doing on the acquisition of ships and contract (demonstrations).

Eduardo Bartolomeo {BIO 15365202 <GO>}

As you mentioned, we keep on our strategy to increase our control over the maritime fleet towards mainly Asia. We have no under our control 20 ships, either ownership of the old fleet we used to have, the three old ones. We bought five ships. And we have around 12 COAs. And we're very looking to the market. We see a lot of opportunities on that sense, conversion of tankers. So we've been able to secure a very, I would say right size of freight as this change is happening in the market.

Fabio Barbosa {BIO 21197136 <GO>}

Well so, we have ordered already 12 VLOCs and we have options for four more. And we are looking for more ships in the market in order to speed up our -- the coverage of our sales into Asia. So we are trying at the same time to increase our customer base by developing new markets, new client base. We are, of course, with the distribution centers in the Middle East and Asia in order to optimize our product mix. And we are adopting a more flexible stance towards iron ore pricing.

And I'd like to invite Martins to comment -- may some comments on that as well.

Jose Carlos Martins {BIO 1715332 <GO>}

As we have already announced to the market, we are flexibilizing our price policy in order to cope with the customers' requirements and also with the competitors' moves. Cost-wise, we have the conditions to sell iron ore at lower prices it was bidded. But we are always managing the price volume situation. If we increase too much our sales, probably we're going to drive prices down a lot. On the other hand, we can't pressure freights to Asia.

So we are operating under these three points, which is the price that was needed to sell our production in markets where we really have this elasticity because, for instance, in Europe, Japan, and the Western world market, price is not the issue. People will not buy because you have a lower price. The only elastic market today is China because you have a local production which has a higher cost. So our flexibility today is mainly related to the Chinese market because of this situation. And we also needed to cope with our competitors' movements. So that's for now that way we are operating.

Fabio Barbosa {BIO 21197136 <GO>}

Yes, so flexibility will be the name of the game.

Jose Carlos Martins {BIO 1715332 <GO>}

That's it.

Fabio Barbosa {BIO 21197136 <GO>}

-- policy.

Jose Carlos Martins {BIO 1715332 <GO>}

That's it.

Fabio Barbosa {BIO 21197136 <GO>}

Okay. Let's move to the second section of our presentation today, where we have some comments about how we see the future. First point we'd like to make is, of course, the performance of the PMI. It's yet in the negative spectrum of the index. But it, in our view, is issuing clear signs of stabilization of industrial production, which is good news as industrial production is the most difficult related with mineral and metals demand.

On the other chart, we see the very positive combination as well of declining inventories and increasing -- and writing new orders, indicating that we may actually have reached the bottom of the current crisis. This is a possibility. We expect that this is the case. Of course, nobody could be absolutely sure, but very strong indications in this direction.

Chinese PMI is also in the 50-plus region. It's also a very important indicator, considering the weight of China, Chinese demand in total consumption of our industry. And in slide 18, we see that the fixed asset investments responded very quickly to the stimulus package implemented by the Chinese government. So the growth of fixed asset investments reached over 28% in the First Quarter and the last month of March.

So global steel production, of course, reacted to the negative environment. But now, it's showing signs of recovery, particularly in China. That's already showing a growth on a three-months average seasonally adjusted basis, 14% growth compared to the previous level at the end of the year of a 50% decline. And this is driving back the global steel production. It's still in the negative territory, but less negative than it was in the last quarter of '08.

As a result of this recovery, of course, the Chinese demand for iron ore imports is showing a very strong performance. And now over the last 12 months, the level reached was 476 million tons. So we believe we are dislocating some high-cost local producers. And we have been able to share part of this growth that was showed by the Chinese imports that they are growing now at 18% average. That is relatively closer to the peak observed in the mid of last year, 2008, with 23%.

Another element that will give us more hope about the future is that the loans to property sector are expanding very quickly, as you can see in slide 21. So we are talking about growth of around 9% to 10%. That compares to the minus 2% observed in the last quarter of '08.

So the tightening observed in the credit property sector was reversed. And there, we have now an expansion at levels that are even higher than the ones observed in 2007. And the floor space sold also is showing the same trend after the drop in over minus 25% in the end of last year. We are showing now a recovery. And they are close to zero. It's not brilliant. But it's much better position than we had the end of 2008.

And this is very important. As you can see on page 22, this is very important for our market, our iron ore in particular, the weight of the construction sector and the demand in the steel consumption. So we show there in slide 22 that construction response of 51% of the steel consumption in China. And out of it, property, residential property's 37%. Commercial property's 40%. Infrastructure's spanning 23%. So it's very good news what is happening in this specific segment as it has a direct effect on the demand for steel and consequently iron ore.

And in this connection, I would like to point out an important point. And I would like Martins to comment as well how well Vale is poised today to catch the future upside in the iron ore market. Martins, if you could comment, please.

Jose Carlos Martins {BIO 1715332 <GO>}

Yes, I think the worst of this First Quarter result is the volume we lost because of this trend in the geography of the market. Okay? We lost a big part of the slowdown in the seaborne market Vale took. So we lost around 100 million tons per year volumes.

But on the other hand, from now on, all our competitors are operating fully capacity. So an additional market that will come and for sure will come and mainly in Europe, Vale's prepared to take advantage of it. So we are now the only producer that has spare capacity to supply the market. And we are prepared to do it as long as it's needed. So we have this upside potential that for sure will be captured in the next quarters.

Fabio Barbosa {BIO 21197136 <GO>}

Well then it's now to the nickel demand. It's also showing the same pattern. There are some early signs of recovery. And stainless steel production is nearer the 5 million tons level. It's far from the peak of 7.7 million in the last two years ago. But it's moving up. And this is good news. And also, the austenitic ratio is also starting to recover, as you can indicate there, reaching almost 75% in the First Quarter of '09. And the reality is that the prices of high-nickel stainless steels have plunged.

So the demand, the elasticity -- there is, of course, an elasticity of the demand regarding prices, as we could see in the last few years. So it's operate to bring down demand. And it should operate the other way around now when prices are low, very low, compared to the peak level we reached in 2007. And they are back to the levels observed in January or early 2004. So it's important to have the view that the combination of low inventories and low prices could bring the foundation of that respect for the nickel business in the future.

I would caution, of course, we are positive about the future considering the environment that we're facing. But we see that there's still a long way to go before we can say that the crisis is over. Recessions caused by global financial crises, as we put, they tend to be longer. And this is precisely the case. We had a massive destruction of wealth worldwide. We had an erosion of the capital base of banks. There's still and issue today with the financial system. And of course, credit is a key element in the recovery of economic activity on a sustainable basis.

Of course, we believe we reached a situation in that the downside risks are very limited. And the government policies are having important effect in bringing back the economy to the positive territory. So this is good news. And in this connection, I'd like to stress again that Vale's very well prepared to also to capture value in the recovery of the economy when it happens. And we are, of course, prepared to, as we put there, to continue to generate value across the cycles.

Thank you very much for your attention. Now, I'd like to turn the floor to Mr. Roger Agnelli to make his comments. Roger, please.

Roger Agnelli {BIO 14016988 <GO>}

Thank you, Fabio. Well. Good morning, everybody. It's a pleasure again to be here with you. I think Fabio, Martins, Tito, and Eduardo said almost everything about the results, about the performance of the Company in the First Quarter. I would like only to add some comments about that. Last October, we started to face the crisis. Our first decision was to rethink our business model, our strategy, rethinking our investments, rethinking the cost structure, et cetera, et cetera. And we made some commitments to be achieved in the First Quarter of 2009.

We said, well, until March I think we needed to go forward carefully. Let's wait a little bit to see how the market we will accommodate, how the market will be reacting different in the different areas that we are operating. And in March, we are going to take our decision how to go forward. I think this is the most important thing to mention to you. So everything that is happening right now or everything that we are showing in our First

Quarter results, I think we are happy. We are happy because we reached almost everything that we were committed to achieve.

The first thing is the unit cost for nickel, for iron ore, logistics, and first rate in our operations is right now the same as it was before the crisis, even considering a much lower volume, a much lower level of operation. I think this was a very good result for us. Of course, we took some very tough decisions to shutdown some mines here in the Southeast and bring volumes through Carajas. I think that was correct.

If you see the unit cost of iron ore or the cash cost of our iron ore business dropped 35% in the First Quarter compared to what was last year. In the nickel business, the same thing. We rethink the material flow. We rethink the working capital involved in the operations. And we reduced the cost outright.

We adopted our corporate core activities to a new level of activity. We were growing very fast. And now, we are -- we can say that we are stable in terms of growth. Of course, we are keeping investing in our projects. But we are not really in a hurry to increase our production or increase our opportunities for M&As, et cetera. So we are, let's say, calm, very, very calm. And we are not in a hurry.

So from last September to last March, we reduced the number of employees involved in our operations or working now in our sites by 2,000 employees, which is really very, very strong adjustment. And we made that until the end of last year, until December. So of course, we are keeping our balance. We are keeping our people. And we just insourced some work that contractors used to do for us. So we reduced the workforce indirectly involved in our operations by 2,000 employees. So this is something that wasn't good but was imperative for the Company to do to achieve our goals.

The other point is we carefully drove our iron ore business. We said, well, we have the lowest-cost operation in the world. We have the best iron ore in the world. We have our natural market, which is Europe, affected much stronger by the crisis than other areas in the globe. We are far from China. In the first moment, we reduced our shipment to China. We were talking with our clients. We discussed a lot with our clients about the future of the iron ore business, our supply capacity. We discussed a lot about the benchmark system or spot market or index or whatever.

Now, I should say that we are prepared for anything. We will be very happy if our clients decide to keep the benchmark system. We will be very, very happy because we truly believe that this is the best model for the steel chain. This is very important for everybody, brings a lot of stability, is a reducible activity of the market. And we can really predict the cuts of expenditure because we have long-term contracts.

But if our clients decide not to follow the benchmark system and they decided to follow the short-term view, we will be very happy to do that. We will be very happy to do that, no problem at all. Why that? Because we truly believe that the iron ore market for the coming years will be very tight. It's going to be very tight. And as I've said, our competitors, they don't have room to maneuver because they are working. They are already working at the full capacity. And we have the market and the additional tons in the market. I think Vale is much more prepared to supply this additional market than the other competitors. So we are not in a hurry.

In nickel, we are in the same situation. We are finalizing two big, very big projects, Goro and Onca Puma. And the market just consumed all the stocks that they used to have in the last year. So today, the market, the nickel market is a little bit tight. And we have capacities to bring to the market and to take advantage of any recovery in the economy in the following months.

In copper, we are okay. We are working at full capacity. We are not really a big producer in the market. So we are following the market. In coal, we are full-stream ahead investing to be a player or, let's say, a significant player in the market. But we are not yet. But we will be a significant player in the market.

Logistics, we are still investing to repair or to restore our efficiency. And I think today we are working with a very good efficiency in the system. And we are increasing the capacity for the coming years. So we had a lot of homework to be done. We finished almost everything. Of course, we are keeping -- renegotiating our contracts with our suppliers. We are reshaping the volumes or the necessity of goods or materials for the coming years. I think we got a lot of cost reduction from our suppliers. They are our partners. And we are working together. And I think we are accommodating everything.

So in the point of view of the Company today, okay, the First Quarter I think was the bottom in terms of all kinds of problems that could have happened in a crisis like we are facing right now. I should say that in Europe, we are in weather that is minus 30 degrees centigrade. In China today, we are working at maybe 35, 40 degrees centigrade. So it's hot there. And it's very cold here and in Europe.

As a leverage, I think we are okay in a very placid weather because from minus 40 to plus 40. So we are in a very pleasant weather. So I think we are -- I believe that we are prepared to take advantage of any recovery in the market. I feel that we are right now in a situation that we can at least see what's going to happen in the next six or seven or 10 months that was completely impossible to see three, four, five months ago.

My feeling's that the whole market is not getting worse, is not recovering yet, but is not getting worse. But at least, nobody has stocks anymore, even ourselves. We don't have stocks. We have a little bit in the nickel. But Tito is going to take care of that. But it is a very, very, very low inventory there.

But the point is -- any recovery, I think we are prepared. We are open to face any challenge in the market. Financially speaking, we are very sound. We are very strong. We are -- we don't have any constraints. We don't have any pressure to generate cash flow to pay debts or whatever. So we are very comfortable in this regard.

So again, I can't say that we are unhappy with the results or I'm very happy with the current situation because I'm not. I think nobody is really happy. But at least I should say that compared to others I think we are in a very good situation. And we should be very, very happy.

Looking forward, I think we are much stronger than any other main competitor in the market. So we can increase production. We can increase shipment to China. We can increase shipment to Europe. We can sell more nickel. We can sell whatever is necessary to sell. The course is -- I think we have room to improve a little bit more.

And you are going to see that in the Second Quarter of this year because some measures that we took in the past is maturing right now. The level of goods in our warehouses are going down from April on because, of course, last year, we were working with a lack of everything. And we increased our inventories or our spare parts inventories, et cetera, et cetera, and right now is accommodating, is starting to reduce. So those are the comments that I should give to you. And I think Vale is in a very good position. I'm very confident that we are going to deliver very good results, even these very tough situations that we are facing in the market.

Regarding iron ore, everybody's betting if the benchmark will buy or if the benchmark will survive or the spot market will be the market for everybody. What I would like to say is that, listen, if it's benchmarked, great. If it's spot, it's great also. It's great also. Our plants are going to decide. They have to decide. And now is the time to decide what they want. If they want the benchmarks, okay, they should pay for the guarantee of supply. They should pay for the quality. They should pay for the local activity that we are bringing to the chain.

If they decide to go for spot, I'll be very happy because we are going to have upsides. I don't see that we are going to have downsides because the price in the market is a little bit tight right now, that I can tell you. If they wanted to have or to see the benchmark below the spot, I'd prefer to go to spot.

If they wanted to keep the guarantees, they wanted to keep the comfortable situation to have a very reliable supply with a price that they can't control, they can't see how it's going to be their cost in the future and how they will sign their contracts with their clients, okay. Say for that, it's luck. It's okay for us. It's okay for us. We are now prepared to do whatever what our clients decide to do. If it's benchmark, good. If it's spot, good.

The only thing is benchmark, guaranteed investments for long term, visibility, et cetera. This is something that costs. And we are going to charge. If it's the spot, okay, let's go and play in the spot. And I think it's -- I like that also. It's not bad. It's good also.

That's it. Thank you very much.

Questions And Answers

Operator

Thank you. We will now begin the question-and-answer session. (Operator Instructions)

Our first question comes from Mr. Felipe Hirai from Bank of America.

Q - Felipe Hirai {BIO 15071781 <GO>}

Hello. Good morning, everyone. My two questions are related to iron ore. So in the last conference call, you said that the First Quarter you would ship about 50 million tons. And it was pretty much what you did in the First Quarter. What kind of numbers are you looking for the Second Quarter of the year in terms of shipments and for the whole year in 2009?

And my second question on prices would be -- could you give us an idea what's going on with the benchmark price negotiations, if we should assume that it's 20% provisional pricing should be the price for the remainder of the year or if you see any kind of risk that prices could be actually lower than this 20%? Thank you.

A - Fabio Barbosa {BIO 21197136 <GO>}

Felipe, this is Fabio Barbosa speaking. For the first question, we are not providing any guidance of volumes moving forward. So as the year evolves, we will let you know what happens in our shipments.

And I'll pass the floor to Martins for the second question. Thank you.

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

Yes, I think as far as the price is concerned, look in the figures we presented and the volumes sold. And comparing our sales performance against competitors' performance, it's clear that Vale was a very disciplined company during this period. We didn't reduce price to get the market. And the volumes we locked in are clear. It's a clear demonstration that we were not the first to drive the prices down, like it happened.

From now on, as we told before, we are applying a more flexible policy. And also, we are considering other forms of selling. During the First Quarter, we didn't sell a ton in this quarter. All our sales are based in long-term contracts with some flexibility, it's true. But all our sales, including China, was done based on long-term contracts. We sold near 50 million tons of new sales in China for new customers at the benchmark price. So when you look forward from April 1st, we start developing a price flexibility that is according to the market situation.

And another issue is, as we told before and Roger stressed, considering that all our competitors are operating full capacity, our flexibility probably will bring us additional volumes. We face in Western world a huge distorting process that in the First Quarter amounted above 10 million tons of iron ore that was consumed based on the stocked inventories that the customer has.

We also have some impact of captive mines from some of our customers, which amounted near 5 million tons in the first half. So we lost almost (15) million tons based on inventories and based on captive production. But I think this is the cap. They cannot go above it. And from now on, even if they continue to consume the same quantities of iron ore they consumed in the First Quarter, they need to buy more ore.

So besides that, everybody knows what's going on in China with the present spot price in China. A huge quantity of local ore is being displaced. And everyday, we have more and more customers looking for imported ore. And the only company that has capacity available to sell more is Vale. So it's a good perspective, not only for volumes but also for quantities and for price.

Why you think that? If you look in the last three months, China bought almost 50 million tons per month in the seaborne market. This is almost 20% above their best figures in the last year. So even with this huge quantity, spot price in China stopped going down and showing some signs of recovery. So we think that going forward, considering our flexibility to work in this market on not only quantity but also in price, we see good perspective for Vale.

Seaborne market as a whole has a huge impact in this First Quarter. According to our calculations, consumption was down 40 million tons. But above that, we have this destocking. And also, we have this captive mine production, which together brought this seaborne market down near 55 million tons in this quarter. That could be around 220 million in a yearly base.

And part of this 55 million tons was offset by the increase in seaborne imports from China in this quarter, which accounts for 25 million tons of additional ore being imported from China in dispute. So as general, seaborne markets went down 30 million tons in this quarter. And by the figures, you can see that we took almost all the brunt. So we don't think that situation can be worse than that. And from now on, we really believe that all the odds are for a good upside for Vale, not only based on volumes, but also in price.

A - Fabio Barbosa {BIO 21197136 <GO>}

Thank you, Martins. Thank you, Felipe.

Q - Felipe Hirai {BIO 15071781 <GO>}

Thank you.

Operator

(Operator Instructions)

Our next question comes from Mr. Marcos Assumpcao from Itau Bank.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Hi. Good morning, everyone. First question is regarding iron ore as well. What percentage of total volumes sold also in the Second Quarter do you believe are going to be on the provisional discounts, just like in the First Quarter 55% of total volumes were sold with the 20% discount? How much do you think in the Second Quarter will be?

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

As I told you before, we continue to work in this flexible price policy. And as far as the provisional price, from April 1st, all our sales based on long-term contracts are subjected to provisional price policy, okay.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

All right. And the second question is regarding the -- what level of premium do you think Vale can charge on the spot prices for the higher quality, the guarantee of supply, and the more stable quality of iron ore when compared to other players?

A - Fabio Barbosa {BIO 21197136 <GO>}

Marcos, we are not going to provide any guidance about future price performance. We will disclose the results as we end the quarter. And you'll see how much we managed to achieve every quarter.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Okay. So if I can just -- a last question here on CapEx, Fabio, if you could comment that the maintenance CapEx was very low at $400 million in the First Quarter. If we annualize that number, it would be like $1.6 billion for the year. The previous CapEx guidance for maintenance was $2.5 billion. You think that for an extraordinary year, you could see a lower CapEx, even maintenance CapEx, in 2009, you could see room for reduction, even on maintenance CapEx? That's my point.

A - Fabio Barbosa {BIO 21197136 <GO>}

As we indicated and as it is, we are in the process of reviewing our investment program, as we commented in the last call. And this process is not over yet. What I could say about the First Quarter investment spending is that there is a seasonal pattern that usually execution of the budget in the First Quarter is lower than the average of the year. So it may not be a good sample to extrapolate for the whole year. Thank you.

Q - Marcos Assumpcao {BIO 7474402 <GO>}

Okay. Thank you.

Operator

(Operator Instructions)

Our next question comes from Mr. Carlos de Alba from Morgan Stanley.

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

Good morning, everyone. Thank you for taking the question. The first one is on China iron ore market. How much do you expect the total demand for iron ore in 2009 will be from China? And at what price do you think the domestic Chinese production stops declining? In other words, at what price do you assume that the substitution from imports stops?

And my second question would be at what -- in the First Quarter, the production at Carajas was around 20 million tons. That's down about 6 million tons from the peak in the Third Quarter of last year. How much can you produce from Carajas going forward as volumes picked up so that you continue to reduce your costs or maintain the very good cost of iron ore that you achieved in the First Quarter? My theory is that if volumes pick up, would you have to restart the southern system range and afford your cost of iron ore to go up a little bit? Those are my questions. Thank you very much.

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

As far as the Chinese market is concerned, in the First Quarter, China imported additional 25 million tons of ore, which means from last year we can guess that they'll buy at least 100 million tons more, which means this volume -- considering their production was almost the same as last year -- this volume will come from local production. I think to this price level that we have announced China, at least 100 million tons of iron ore will be displaced from local mines. So that's the situation we see in this moment.

As far as Carajas, I don't know if everybody is aware. But we've had one of the toughest rainy seasons in north of Brazil. And our production in the First Quarter was below the production that we could have done in normal situations. In the north of Brazil this year is running 20% above the last effort that was in the year of 2000. So this impacted our production. But the situation we have now, we can produce up to 100 million tons per year in Carajas. And the reason of 100 million tons per year is around 8 million tons per month.

In the southern system, although we've cut a lot of costs, we keep a lot of people in the Company prepared to restart production in these mines. Okay? Although we reduced production, we are prepared that any moment to recover production and if it was needed. So we have a lot of flexibility as production is concerned, not only in Carajas, which can increase a little bit more, but also in the southern system, where we have everything in place to restart production if it was needed.

And that's the importance of the cost reduction we reached in this First Quarter because we have some redundancy cost in the Company that we pay for it, but only to be prepared to resume production if the market -- if it's necessary according to our market sales.

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

Thank you.

Operator

Excuse me. Our next question comes from Mr. (Alex Simlert) from George Weiss.

Q - Alex Simlert

Yes. Good morning. A quick question in terms of the bench on the pricing -- I mean, you said that you don't really -- it doesn't really matter if it's benchmark or spot prices. You're fine with either one. But if everyone merges to go to spot prices, don't you think it's going to put a lot of pressure on spot prices because of the volume that's going to be thrown into the spot market?

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

By the contrary, I think the market today is tight. It's tight. Anything that can happen in Europe recover -- if the market recovers in Europe, of course, our sales to China will decrease a little bit. And our competitors there are working at full capacity. So I think any recovery in Europe means price increase.

What I could add to Roger's statement is we are a price-sensitive company. We manage -- we are in condition now more than before to manage volume and price. So we are going to do what is best for increasing our profitability. So we are not true in the market -- volume that could drive prices down for amounts bigger than the profit we can take from this additional volume. So we are going to manage it. What is different now is as everybody's operating full capacity, the only company that has the condition to manage the price volume game is Vale.

Q - Alex Simlert

I see. One second question if I may -- so if my interpretation's correct, you're saying that -- I mean, because China at one point is going to have to start defending a little bit their local producers. I mean, you've been gaining market share throughout the First Quarter. But don't you think at some point China would have to start defending a little bit the local producers and kind of step back a little bit in terms of importing iron ore? Then you'd be a lot more dependent on Europe.

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

I think that this is a possibility. But let's wait and see. I think we cannot anticipate -- we didn't anticipate what happened. And we cannot anticipate what will happen from now on. One thing is for sure. Local customers that never used Vale's ore are now using. And I can tell you they are like -- I think now they proved the good stuff that you can offer. They are becoming more and more interested in buying. So I cannot talk about what the local miners will do or what will happen in China. But we're happy to follow and to serve the market and do what is best for our company and for our shareholders.

A - Roger Agnelli {BIO 14016988 <GO>}

I think one point is very important. We shouldn't forget that the spot market price last year reached $200 per ton. At that time, a lot of low competitive, a lot of small miners were able to produce and to sell. And today, the market or the spot market varies $60, $65, $70 per ton. So they are not able to do that. So if the government decided to do something to increase the local production, I think that our clients in China will not be very happy with that because they are going to lose competitiveness in the world markets. So I think this is a possibility. But there is a tradeoff.

Q - Alex Simlert

Thank you.

Operator

Excuse me. Our next question comes from Mr. Jim Young from West Family Investments.

Q - Jim Young {BIO 20911202 <GO>}

Yes, hi. Could you talk a little bit more about your acquisition criteria and what you're looking for? I recognize you made an acquisition of some potash assets in the quarter along with some thermal assets. What types of return in invested capital do you expect to generate, given the prices paid? And it would seem that given your long-term nature and the strong balance sheet that you have that you would be a little bit more aggressive than you have been on the acquisition front. Could you address those issues, please?

A - Fabio Barbosa {BIO 21197136 <GO>}

Last year, we made some comments about our, let's say, guidance for M&A. We said that we were looking for small assets that could really increase our strength, our position in some specific markets. And we are following this kind of strategy. We bought, as you know, Corumba Insa from Rio Tinto that is a very good asset to be addition to our portfolio. We are very happy with that.

We bought this Rio Colorado potash project in Argentina that is right beside our other project there in Yukon. And it's a huge deposit of potash and a very good one. And we believe that the market is going to be very good for fertilizers or for potash and for sale. We acquired some good assets in Africa also, a small amount of money, but with a very big potential in terms of copper. So we are very happy with that.

We are analyzing several different opportunities. But we are not considering to move ahead with big or huge acquisitions. And we feel that even at the current price, our projects are much more competitive. So we don't need to acquire any other additional iron ore deposits because the deposit that we have in Carajas is much more competitive than any other possible acquisition.

In copper, we have several projects being developed, like Salobo in Carajas, that we don't need to go for a major acquisition. And to be honest with you, major acquisitions -- many acquisitions today, I think you can bring more liabilities than assets. So I think it's better to develop or to keep our eyes on the clean, very clean assets. And you do that when you buy a project or when you buy a small company because the big ones, I should say, not really completely out of liabilities. And this is not the right time to bring liabilities to our balance sheet.

Operator

Excuse me. Our next question comes from Mr. Leonardo Correa from Credit Suisse.

Q - Leonardo Correa {BIO 16441222 <GO>}

Hi. Good morning. And thanks for taking my questions. The first question is relating to Chinese domestic iron ore production. With the expectation that the ex-China market demand comes back in the second semester and spot price is recovering, do you see any risk that the Chinese domestic ore production that has been displaced during the First Quarter come back to the market, because in that case, basically, Chinese imports could be potentially driven down? So if you could please comment on that, please.

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

Well there is no free lunch. Okay? So for sure, if spot price -- the same mechanism that took those guys out of the market can bring them back if the price goes up. So but then again, it will depend on how much ore can be sent to China. We need -- we have to consider, for instance, that from now on a big quantity of Indian ore will be out of the Chinese market because of the monsoon. So I think there is a space for some price increase and some additional exports from, for instance, additional sales from Vale to China, even in this case because from now on probably we see a big volume of Indian ore getting out of this market.

A - Fabio Barbosa {BIO 21197136 <GO>}

And Martins, if I may, part of the consumption of the Chinese ore happened because there was no alternative. So the market was sold out. And they had to consume any ore they could find. And now clearly, Vale represents an alternative --

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

Yes.

A - Fabio Barbosa {BIO 21197136 <GO>}

-- moving forward.

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

I think it's the ore available.

A - Fabio Barbosa {BIO 21197136 <GO>}

Yes. Thank you.

Q - Leonardo Correa {BIO 16441222 <GO>}

Yes. Thank you very much. And the second question is relating to Vale's current market share to China. If you could provide, please, some more color on that if these current rates are sustainable or we should expect them trending down going forward.

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

What I see is we never in the past had iron ore available to test our market share in China because we always prefer to supply Europe and the western world. So for the first time in many, many years, we have iron ore available to test what would be our market share. So and we think that to reach 30% is something possible, considering quality, considering all of the aspects involved.

A - Fabio Barbosa {BIO 21197136 <GO>}

Just to clarify, we are not forecasting that we are going to reach. But it's possible.

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

Yes. It depends on a lot of factors.

A - Fabio Barbosa {BIO 21197136 <GO>}

Yes.

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

Okay?

A - Fabio Barbosa {BIO 21197136 <GO>}

Thank you.

Operator

Excuse me. Our next question comes from (Mr. Jim Richards) from (Netsky Capital).

Q - Jim Richards {BIO 17728740 <GO>}

Hi. In your release, you refer to the fact that although the Q1 unit cost in the iron ore division are very good that in fact most of what you've done over the last few months hasn't actually had effect yet and will affect Q2 through 4. I mean, is there any sort of quantification or further color you can give us on that?

A - Fabio Barbosa {BIO 21197136 <GO>}

We are not providing any guidance on the future performance of our costs. We indicated a measure that we adopted. We indicated -- we showed the results that we had in the First Quarter. Some of them have a permanent nature. So we'll release the results as they evolve.

Q - Jim Richards {BIO 17728740 <GO>}

Okay. Thank you.

Operator

Excuse me. Our next question comes from Mr. Tony Rizzuto from Dahlman Rose.

Q - Tony Rizzuto {BIO 1490590 <GO>}

Thank you very much for taking my questions. I've got two. First of all, gentlemen. on the iron ore side, I wonder if you could talk a little bit about how you see ore grades playing out within China. And I realize a portion of that is going to be determined by the mix and the internal supply-demand dynamics. But if you could talk generally about iron ore grades there, and then also what you think about the level of marginal capacity in China from an iron ore perspective.

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

If I understood your question, you want to know about the quality of iron ore being delivered in China. Exactly what the point you'd like to have our comments?

Q - Tony Rizzuto {BIO 1490590 <GO>}

Yes, really trying to get at what you see taking place with regard to ore grades over the medium term.

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

Well I think when you have a very low capacity utilization, normally customers accept work with not so good ore because they don't need too much productivity. Okay? But as they're increasing their capacity utilization, more and more, they demand good quality ore. And the good quality ore is not only important because of productivity but also because of carbon emission. High-quality ore normally demands less coal to produce (pigano). And so, you have a much lower carbon emission.

So if you look going forward as the market becomes more, I would say, sophisticated and as the market becomes more and more environmental conscious, the need of high-grade ore increases. And so that we see a very strong acceptability of our Carajas ore in China.

Normally, we didn't deliver too much Carajas ore in China because we were always delivering this ore in Europe and Japan, Korea, so and so. And we always deliver more southern system ore, which is not so good quality as Carajas ore. But from now on, we have more Carajas available because those markets, those traditional markets are not demanding. And so the acceptability of this high-quality ore is very good.

And also, considering that they are buying more low-quality ore, they needed more high-quality ore to blend it. So we have many mills that are only using in the past low-quality ore that now have the possibility to blend it with this Carajas or even southern system good-quality ore. I see the prospects for our ore in China are very positive as going forward. Okay?

A - Fabio Barbosa {BIO 21197136 <GO>}

Thank you.

Q - Tony Rizzuto {BIO 1490590 <GO>}

That's extremely helpful. And if I may, I have one more question. It's on nickel. And I was wondering if you could just update us on the labor negotiations at Sudbury (inaudible; technical difficulty) 31 expiry. But I wonder if you could talk about the major issues that you see going into these negotiations.

A - Unidentified Speaker

There's not much to say for now. Basically, we started the discussions last week. And so far, we are still sharing views about the future with the employees. Those negotiations, usually, they are done in a way that both sides they provide their views about the future of the business. So we're still discussing mostly of the forecast and the future of our business. We haven't really started the negotiations, not the process of negotiations. Usually, it happens in the last two weeks of the proper time.

Of course, I cannot comment anything else about that. But I think it's going to be a very interesting negotiation. We are optimists. Both sides understand that we are going through a very problematic time. We have -- the nickel business was very impacted by the drop in price last year. So I understand that the unions, they know that. And they understand that the future of our business depends on how they will react to what we will propose to them.

We need their support.

Yes. Absolutely.

We'll need their support to really to keep our operations in Canada competitive.

A - Fabio Barbosa {BIO 21197136 <GO>}

Yes. Thank you.

Operator

Thank you. Ladies and gentlemen. this concludes today's question and answer session. I would like to give the word back to Vale's executives for their closing remarks. Please go ahead.

A - Fabio Barbosa {BIO 21197136 <GO>}

I would like to thank you all for attending this conference call. And of course, as usual, we'll be available for any further questions you may have that myself or our team or the Investor Relations Department. Thank you very much.

Operator

That does conclude our Vale's First Quarter 2009 earnings conference call for today. Thank you very much for your participation. And have a nice day.