OVERVIEW:
X reported 3Q22 revenue of $5.2b and adjusted diluted EPS of $1.95.
CORPORATE PARTICIPANTS

David Boyd Burritt  United States Steel Corporation - President, CEO & Director
Jessica T. Graziano  United States Steel Corporation - Senior VP & CFO
Kevin Lewis  United States Steel Corporation - VP of IR and Corporate FP&A
Richard L. Fruehauf  United States Steel Corporation - Senior VP and Chief Strategy & Sustainability Officer

CONFERENCE CALL PARTICIPANTS

Carlos De Alba  Morgan Stanley, Research Division - Equity Analyst
Curtis Rogers Woodworth  Crédit Suisse AG, Research Division - Director & Senior Analyst
David Francis Gagliano  BMO Capital Markets Equity Research - Co-Head of Metals & Mining Research and Metals & Mining Analyst
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Gordon Lee Johnson  GLJ Research, LLC - CEO & Founder
Karl Blunden  Goldman Sachs Group, Inc., Research Division - Senior Analyst
Tristan Gresser  BNP Paribas Exane, Research Division - Research Analyst

PRESENTATION

Operator

Good morning, everyone. And welcome to United States Steel Corporation’s Third Quarter 2022 Earnings Conference Call and Webcast. As a reminder, today’s call is being recorded. I'll now hand the call over to Ken Lewis Vice President, Investor Relations and Corporate at FP&A.

Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

Thank you, Tommy. Good morning, and thank you for joining our third quarter 2022 earnings call. Joining me on today’s call is U.S. Steel President and CEO, Dave Burritt; and Senior Vice President and Chief Strategy and Sustainability Officer, Rich Fruehauf. Also, a special welcome to our Senior Vice President and CFO, Jessica Graziano, joining us this morning for her first earnings call at U.S. Steel.

This morning, we posted slides to accompany today’s prepared remarks. These can be found on the U.S. Steel Investor page under the Events and Presentations section. Before we start, let me remind you that some information provided during this call may include forward-looking statements that are based on certain assumptions and are subject to a number of risks and uncertainties as described in our SEC filings, and actual future results may vary materially. Forward-looking statements in the press release that we issued yesterday, along with our remarks today, are made as of today, and we undertake no duty to update them as actual events unfold.

I would now like to turn the conference call over to U.S. Steel President and CEO, Dave Burritt, who will begin on Slide 4.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Thank you, Kevin, and good morning to everyone joining us today. We appreciate your continued support of U.S. Steel. We delivered another strong performance in the third quarter. Most importantly, we did it safely. We had one of the safest summers in our history and are on track for a third consecutive year of record safety performance. While we certainly don’t focus on safety for awards, we are pleased that our industry-leading safety performance was recently recognized, not once but twice.
Both the National Safety Council and World Steel awarded U.S. Steel safety programs with Safety Excellence Awards, further validating our leadership role in placing safety first. At U.S. Steel, we have a culture of caring that extends through our facilities. Exceptional safety means exceptional operations. Thank you to my U.S. Steel colleagues for doing your job safely for yourself, for your co-workers and for your families.

We’ll spend the next 15 minutes or so providing you with a business and strategy update. There’s a lot of noise out there, but one thing is clear, we are confident in our ability to execute our best for all future. I remain bullish on U.S. Steel’s future. We are better positioned now more than ever to confront market uncertainty and to prove the foundational strength of our business. The challenges we face today remain transitioning to a less carbon and less capital-intensive business model while becoming the best steel competitor. Our strategy creates a path to achieve these goals and reach our best for all future.

To become the best, you have to outperform the best. That’s why we’re expanding our competitive advantages and expanding our low CapEx low GHG emission EAF steelmaking and value-added capabilities to meet customer demand. For example, we are leveraging our unique raw materials advantage to support our growing electric arc furnace fleet. Earlier this month, we were joined by Governor Walz in Minnesota at the ground-breaking ceremony for our DR-grade pellet upgrades at Keetac. The excitement from the team and from the community was invigorating, and everyone involved appreciates the importance of this investment as an integral part of our Best for All strategy.

We are another quarter closer to the earnings and free cash flow growth our strategic projects will generate. Each project remains on time and on budget. This means we’ll be -- we’ll continue to have a balanced approach to capital allocation, focused on driving long-term stockholder value. We’re also pleased to see the recent reinforcement of trade policies by the U.S. government. These policies are critical to ensuring national and economic security and ensuring a level playing field for American steelmakers. We are also optimistic that the CHIPS and Science Act, Inflation Reduction Act and Infrastructure Bill will positively impact steel demand in 2023 and beyond.

Our country is the leader in sustainable steelmaking, and we are encouraged the administration continues to support the role American manufacturing plays in the global economy. This gives us the confidence to deliver our Best for All strategy for our employees, our customers and most importantly, our stockholders. Let’s get into this morning’s materials on Slide 5. I’ll focus on 3 key areas that are helping to advance our best for all future. First, we’re operating from a position of strength. While we’re facing the same economic and geopolitical uncertainties as everyone else, the steps we’ve already taken have us well positioned to execute our strategy with confidence. We are closer to our customers and continue to add the capabilities to expand our offerings of steel solutions.

Second, we’re safely navigating current headwinds. We’ve taken steps to optimize our footprint and remain disciplined on cost. We also remain on track to generate higher and more stable through-cycle earnings and free cash flow as we execute our strategy. Our future is extremely bright. Finally, we’re returning capital to stockholders. As we’ve demonstrated through our progress against our stock repurchase program. We continue to invest in strategic projects that will grow earnings and free cash flow and reward stockholders with direct returns.

Our balance sheet is strong, which allows us to sustain the actions that drive long-term stockholder value, even as markets are volatile. Slide 6 details how our improved business model has us operating from a position of strength. We have redefined steelmaking for U.S. Steel since the last cycle, strengthening our business model in the process, and we will only get stronger as we complete our strategic projects. We are a more innovative company, and continue to add differentiated capabilities.

Since the last cycle, we’ve invested to revitalize and strengthen our North American flat-rolled assets, enabling record safety, record quality and record reliability. We also continue to build our position in flexible sustainable mini-mill steelmaking. Our customers are less than a year away from benefiting from the 200,000 ton per year state-of-the-art electrical steel line nearing completion at Big River. We will be uniquely positioned with products ranging from 0.25 millimeter to 0.5 millimeter gauge to serve high-end electric vehicle grades of steel. Consumers want electric vehicles that are more efficient and effective and U.S. Steel is helping to unlock that potential.

With the completion of Big River 2 including a differentiated portfolio of downstream finishing lines to serve the automotive and paint markets, our mini mill segment is expected to deliver $1.3 billion of annual through-cycle EBITDA, supported by only $100 million of annual sustaining CapEx. That will be a new source of significant cash flow generation for our business, cash flow that earns a premium for our investors.
We expect to improve the financial performance of the business by lowering our capital intensity. We’re also lowering our carbon intensity to achieve our bold 2030 and 2050 goals. These factors encourage us to move faster on our transformative strategy. On Slide 7, you can see our balance sheet has already been transformed. We have record cash and record liquidity. We have no meaningful near-term debt maturities. 80% of our total debt is due in 2029 and beyond, and we have overfunded pension and OPEB plans.

On Slide 8, our transformed balance sheet prefunds our strategic investments with record cash and liquidity. Our strategic investments remain on time and on budget. By year-end, we will be nearly 40% completed on our prefunded strategic projects. Looking forward to 2023, we expect total CapEx spending of approximately $2.5 billion. Jess will provide more details on next year’s CapEx plan shortly.

Turning now to Slide 9. We are safely navigating current headwinds with decisive management actions. Across North American flat roll, we responded quickly to softened demand and cautious buying. We accelerated planned outages and temporarily idled integrated assets to better align supply with demand across our diverse end markets. In our Mini Mill segment, we foreshadowed the negative impact, higher raw material prices would have on Big River in the third quarter.

We were prudent and moved quickly to secure additional raw materials as the Ukraine war intensified to protect our customers and our operations. These types of supply shocks reinforce the rationale for the metallic strategy we have underway. Our low-cost iron ore advantage in Minnesota will protect our electric arc furnaces for market price fluctuations as our Gary pig operation begins production in early 2023.

Temporary headwinds aside, we remain confident in the strategic and financial impact of the Big River Steel operating model, and we look forward to demonstrating the through cycle value of the segment in 2023 and beyond. Moving next to our European segment. The prolonged and tragic conflict in Ukraine has continued to pressure our European business on costs for both raw materials and energy. The uncertain outlook for the global economy and Europe’s manufacturing sector is also contributing to softer demand and lower prices, which compounds the impact of normal seasonal buying patterns.

While we don’t believe these are permanent impacts, we do expect these pressures to persist. In response, we are executing management actions. In September, we pulled forward a planned 60-day outage on blast furnace #2 at Kosice to better align supply with customer demand. We’ve also reduced our overhead costs in response to lower production. We’re focused on the things we can control to balance supply with customer demand and improve our cost position heading into 2023.

Our Tubular segment remains an outperformer, benefiting not only from solid energy market fundamentals, but the strategic investment we made in electric arc furnace rounds production. We continue to run at high levels of utilization to support robust customer demand for seamless OCTG products. We’re further benefiting from the $100 million of annual savings from the in-sourced rounds substrate. Recent trade actions also provide important positive impacts on the segment.

Turning to Slide 10. I want to reinforce the importance of returning capital to stockholders as part of our previously shared capital allocation framework. Our balance sheet is strong. Our investments are on track. And most importantly, we continue to see significant value in direct returns to stockholders. U.S. Steel is uniquely positioned to deliver higher earnings and expand our multiple, which means we expect to continue repurchases under our existing authorization as we enter 2023.

With that, I’d like to welcome our new CFO, Jessica Graziano to her first earnings call with U.S. Steel. I’ll turn it over to Jess now to cover the financials. Jess?

Jessica T. Graziano - United States Steel Corporation - Senior VP & CFO

Thanks, Dave, and good morning, everyone. Thanks for joining us today. I’m so pleased to have joined U.S. Steel at this point in its history and to be a part of the transformation that’s underway. Our compelling Best for All strategy and the opportunity it creates to generate significant value are 2 key factors that attracted me to this role. I’d like to start by saying thank you to Christie Breves as she passes the baton. Not only am I grateful for Christi’s support and transition but I’m thrilled to inherit the pristine balance sheet she was so instrumental in building.
Our record level of cash on the balance sheet is a highlight for the third quarter where we’ve seen some demand softness and some expected transient cost headwinds. More on that in a moment. I’ll also provide some color on our guidance to finish the year. But let’s start on Slide 11 with the third quarter’s results. We delivered adjusted EBITDA of $848 million in the third quarter from revenues of over $5.2 billion. This represents an adjusted EBITDA margin of 16%. Our adjusted EPS in the quarter was $1.95 per share, which was at the high end of the guidance range we provided in our September 15 press release.

We generated nearly $600 million in free cash flow in the third quarter, and that’s after investing close to $500 million to support execution of our strategy. Taking a closer look at the balance sheet. Total liquidity on September 30 was a record $5.8 billion, including just under $3.4 billion in cash. Leverage at the end of the quarter was 0.7x, significantly below our target range of 3 to 3.5x adjusted debt to trailing 12-month EBITDA.

In Treasury, we issued $290 million of low coupon 30-year environmental revenue bonds in support of our Big River 2 investment. This green bond commitment underscores our effort to use a high value of recycled scrap in our mini mill operations and the strong investor turnout demonstrates the market’s conviction for our Best for All strategy. We also successfully repurchased approximately $300 million of shorter dated higher coupon debt in the quarter. And together, these actions extended our maturity profile. They reduced our run rate cash interest expense by $5 million per year, and they maintained our strong leverage position and further enhanced the balance sheet.

Let’s take a closer look at each of our operating segments. North American flat-rolled EBITDA was $631 million, which reflects a healthy EBITDA margin of 19%. The segment continues to deliver solid earnings due in part to fixed contracts that make up a significant portion of its order book as well as quarterly market-based contracts. These fixed and longer-term contracts take some of the noise out of market price fluctuations. As a result, our average selling price remained resilient through the quarter, declining about 8% versus a spot market that declined 36%.

Shipment volumes declined 8% off their 2-year high watermark in the third quarter as broader economic concerns have some customers limiting their order exposure. We were quick to respond with footprint decisions as we started to see demand soften. In the quarter, we idled the blast furnace at each Gary and Mon Valley Works. Both blast furnaces remain temporarily idle today and will be brought back online when customer demand warrants it.

Moving to our mini mill segment, which experienced headwinds in the quarter that weighed on both EBITDA and margins. Notably, we foreshadowed the headwind Big River was facing to absorb higher-priced metallics costs, particularly pig iron, when we provided guidance in mid-September. The impact of those higher costs is temporary and we expect to work through them by year-end.

In the third quarter that impact was an 8-point drag on EBITDA margins for the segment. Not unlike what we experienced in North American flat-rolled, demand softening through the quarter was an additional challenge for Big River. This was especially the case in service centers and with distributors, where Big River has more exposure as a percentage of their total order book in the Flat-Rolled segment. Big River also has more exposure to spot business, which felt the impact of lower steel prices on its margins in the third quarter.

Similarly, higher raw material costs and commercial headwinds were at play in our European segment. This was compounded by the spike in energy costs across Europe, which pressured results for the third quarter and resulted in the significant EBITDA decline in the segment. Like we did in North American flat rolled, we took action in Europe to respond to these headwinds, which included overhead cost reductions. We also pulled forward a planned 60-day outage on blast furnace #2 from October into September. This furnace will stay offline until customer order activity improves.

Looking forward, a weak manufacturing outlook in Europe and persistent raw material and energy cost headwinds create a challenging backdrop for USSC for the remainder of 2022 and the start of 2023. Our Tubular segment remains a bright spot. EBITDA and margins in the segment are meaningfully increased sequentially behind strong customer demand and higher pricing. Now let’s move to the fourth quarter, and I’ll share some thoughts on each of our operating segments.

In our North American Flat-Rolled segment, we expect volume to remain stable throughout the fourth quarter. However, September volumes represented a low in the third quarter, so sequential shipments will be lower. We expect the pace of steel prices to decline similarly to what we experienced in the third quarter. And on net Fourth quarter EBITDA for the Flat-Rolled segment will be down sequentially.
In our mini mill segment, we expect EBITDA to decline in the fourth quarter as we continue to work through the higher cost metallics inventory. Lower steel prices will continue to impact margins for the fourth quarter, reducing our average selling price sequentially. In Europe, we expect lower sequential EBITDA from lower average selling prices a big headwind given half of Europe’s volumes are at spot rates. We also expect reduced shipment volumes and elevated raw material costs will continue to drag on segment EBITDA in the fourth quarter.

And lastly, in our Tubular segment, we expect this business will continue to generate robust results in response to strong demand. Prices will continue to be healthy across steady volumes. Our Fairfield EAF will operate at near maximum capacity for seamless pipe in the fourth quarter. And when you tally it up, we expect fourth quarter adjusted EBITDA for the company to be approximately $400 million delivering a full year of over $4.2 billion in adjusted EBITDA, the second best ever for U.S. Steel.

As Dave mentioned, we continue to see tremendous opportunity to create value through capital returns [and are pleased with the progress we’ve made so far in our share repurchase program, which is covered on Slide 12. Share repurchases] in the third quarter totalled $177 million bringing our total buyback activity to $850 million since the fourth quarter of 2021 and reducing our share count by 38 million shares or about 13% of our outstanding base. We expect to continue repurchases under our current $500 million program through year-end.

Before I hand the call back to Dave. Let me take a few moments to provide some additional detail on our 2022 and 2023 capital spending on Slide 13. We expect our 2022 total CapEx spending to be under $2 billion, which is about $300 million less than we originally forecasted. The projects remain on time and on budget with an unchanged scope and will be approximately 40% done by the end of the year. That $300 million spending update is all timing as we expect some of our construction payables will be paid in Q1 next year.

Looking forward to 2023, we expect capital spending to be in the neighborhood of $2.5 billion. As planned, we will invest a significant portion or about $1.7 billion for in-flight strategic projects. Notably, Big River 2 makes up about $1.4 billion of the total. While the level of strategic capital spend is material in 2023 for Big River 2 and our low-cost iron ore mini mill steelmaking and best-in-class finishing projects, we expect spending will ramp down in 2024 as we move towards commissioning and full operations of these projects.

As a matter of fact, 2 of these projects will achieve significant strategic milestones in 2023. First, our Gary Works pig machine is expected to commence operations in the first quarter, supplying Big River Steel with low-cost metallics. This will accelerate the competitive cost advantage gained by our using internally produced pig iron. In addition, we expect to begin operating our state-of-the-art non-grain-oriented electrical steel line in the third quarter. Trials have been successful and we expect to be well prepared to meet robust customer demand for electrical steels later next year.

Lastly, we are carefully managing investments across our existing operating footprint and we expect capital spending in those facilities to total about $650 million in 2023.

And with that, Dave, back to you.

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David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Thank you, Jess. Before we open the line for questions, let me summarize today’s prepared remarks on Slide 14. Our solid performance amid challenging conditions in the third quarter as a result of our continued focus on safe and reliable execution. It’s the product of some heavy lifting over the past few years, and I’m pleased but not satisfied with where we are today. We are operating from a position of strength with a historically strong balance sheet that put us in a position to execute with confidence.

We are safely navigating the current headwinds. We are operating our footprint to match demand and remain disciplined on cost. We are on our way to becoming a more capable, more agile and increasingly differentiated producer of innovative and sustainable steel solutions. We are also returning capital to stockholders. We look forward to delivering on our earnings and cash flow commitments so that we can continue to reward stockholders with direct returns. As I said, I remain bullish about our future, we are better positioned than ever, and we are confident in our ability to execute.

Kevin, let's move to Q&A.
QUESTIONS AND ANSWERS

Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

Thank you, Dave. Our first question comes from, Say technologies. We received a few questions on our demand outlook and growth strategies. Dave, can you share your thoughts on outlook and growth, please?

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Yes. Thanks. I think that's an important question, and it's kind of a boil-the-ocean question. So I hope you're sitting down because I'm probably running through a bit of a stream of consciousness here as we think about the remainder of the year and then 2023 and beyond. But to be clear, on the remainder of 2022, we've got near-term challenges. There's no doubt. And as we think about considerations for 2023 and then beyond the future is very bright, as I said, bullish.

So the remainder of the year, demand headwinds likely persist into the fourth quarter. Automotive has been more resilient. We expect flat to maybe slightly up shipments in the fourth quarter versus the third quarter. For appliance, impacted by consumer sentiment, and we saw some slowdown in shipments in the third quarter. Service centers and industrial and construction, they're cautious buying, saw shipment growth in industrial machinery and containers in the third quarter. There's a resilient demand from construction. Energy -- energy, it's a unique exposure and strong market for us today. Energy shipments increased over 10% in the third quarter for both flat-rolled and Big River. And so as we think about the remainder of the year, yes, there's the near-term challenges. But as we get into 2023 and beyond, things get better.

Expect to see growth in steel demand in 2023. Recently, you probably saw the growth forecast from World Steel, which is up and modestly pockets of demand. We're uniquely positioned to serve in that uptrend. Energy is expected to remain strong. We think there's opportunities for us to grow share in appliance. And I think you know appliance is a strategic market for us, and we're a key supplier on several of popular appliances. We're encouraged by feedback from the automotive negotiations and optimistic there's pent-up automotive demand and build rates will be higher next year. Automotive customers already signalling higher steel consumption in 2023. So that's all good news.

We're uniquely positioned, we believe, to sell a portfolio of differentiated -- differentiated automotive products, advanced high-strength steel exposed to automotive steel solutions. verdeX Steels, our green steel and of course, now non-grain-oriented electrical steels that we're finishing up at Big River. Beyond the market-specific considerations, demand catalysts and CHIPS and Inflation Reduction Acts and Infrastructure, and there's some really good news coming, but that's probably longer term. Strategic market growth to outpace overall market growth, demand for green steel, rapid electrification, infrastructure, that kind of list goes on.

One of the key things that we've learned from the pandemic and the conflicts that we see geopolitically, is that there's onshoring and strengthening of regional supply chain should also positively impact demand. Well, the things we think about is where we must win are advanced high-strength steel automotive and nonautomotive applications. Electrical steels we feel great about this. We'll have the world-class NGL line this next year. And green steel with our verdeX line of sustainable steels this gives us important reductions in GHG.

So to win, as you think about us in the future, we're building differentiated capability. We're not trying to be the biggest, what we want to be is the best. So we're building capabilities. We're focused on product and process innovation and the things we're doing in that space, we should be able to have some breakthroughs over time, and we're getting some top talent in the organization. We're working differently. We're more nimble. We're more flexible. We allow folks to work from wherever and we're attracting talent, we never would have had access to because we are so much more flexible in our work from wherever design. So our goal, basically, over this horizon, the future is profitable growth in the markets we serve. And as I said, near-term challenges, longer term, very bright.
Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

Okay. Thanks so much, Dave. Tommy, you may now queue the phone line for questions. (Operator Instructions)

Operator

(Operator Instructions) And we’ll get to our first question on the line from David Gagliano with BMO Capital Markets.

David Francis Gagliano - BMO Capital Markets Equity Research - Co-Head of Metals & Mining Research and Metals & Mining Analyst

First, I just wanted to ask a little bit about Europe and Kosice in particular, obviously. You've got 1 or 3 blast furnaces idled there. Given the operating headwinds that you flagged, what are your plans for the other 2 blast furnaces?

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Well, David, thanks for that question. And there’s no doubt that it’s an increasingly challenged market backdrop over there. The broader macro considerations are clearly impacting the steel markets and buyers have been focused on destocking, limiting deal making, and that continues across, frankly, all of Europe. We got the continued raw material prices, elevated energy costs and the big wildcard there, the Ukraine war. We have, I love a furnace there. And as we say, we will be nimble and adjust to whatever it takes to make sure that we continue to keep those operations robust and strong.

But I have to pivot a bit here because at some point in time, there’s going to be a great opportunity for that facility to expand and grow with the steel shut off from Russia and the damaged mills in Ukraine and U.S. Steel just 60 kilometers away from the border.

We’re uniquely positioned to provide value to that construction market. So as far as shutting off another blast furnace, we’ll see what the demand holds and what that looks like. But longer term, we should be in good shape. We’re going to adjust and be as nimble as we can in the short term, manage these headwinds. But at some point, things turn around. And then it will be so robust our heads will probably snap back as we start to build -- rebuild Ukraine and the surrounding area there.

David Francis Gagliano - BMO Capital Markets Equity Research - Co-Head of Metals & Mining Research and Metals & Mining Analyst

Okay. And then I just have a two-part follow-up here. On capital returns, obviously, we’ve got elevated spending. We’ve got a stormy outlook near term. Part 1 is why not pause the capital returns to focus on making sure that balance sheet stays robust. And then the other part of my question, I was wondering if you could comment on the negotiations with the unions in the U.S.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Yes, David, I’m not sure I completely understood the stock buybacks. We’re committed to the stock buyback program and making sure, maybe, Jess, you can fill in the gap.

Jessica T. Graziano - United States Steel Corporation - Senior VP & CFO

Sure. Sure.
David Boyd Burritt - United States Steel Corporation - President, CEO & Director

You heard her say earlier, the 38 million that we reduced so far. We are committed to this. This is part of our program. This is what we're doing. We're making sure we're rewarding stockholder. So Jess?

Jessica T. Graziano - United States Steel Corporation - Senior VP & CFO

Great. Thanks, Dave. Yes, I think you can think about it as against a backdrop of a balance sheet that is, dare I say, strong as steel, against the opportunity that we have as we even think about looking forward into 2023 to continue to generate cash flow even in an environment where we are going to be spending frankly, the bulk of cash towards our strategic investments in 2023. We don't want to get ahead of ourselves as we go through the 2023 planning process, and we certainly don't want to get ahead of our Board. But we feel very comfortable that, listen, this is an and strategy. There is strength in the business and strength in the cash flow enough for us to feel very comfortable to continue to underwrite continued share repurchases at a minimum through the end of the year.

And then as I mentioned, not getting ahead of the Board and not getting ahead of our planning process. But as we look forward into 2023, we feel very comfortable that we can continue to, frankly, afford our strategic initiatives without any trouble and be able to return excess cash to our shareholders. It's a very strong place to be.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

And David, your second question was an update on the labor agreement. Is it -- did I hear that right?

David Francis Gagliano - BMO Capital Markets Equity Research - Co-Head of Metals & Mining Research and Metals & Mining Analyst

Yes.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Okay. Yes. Well, we continue to bargain in good faith. I'll just say I'm optimistic about the framework being developed, and we're confident that we'll reach an agreement that is best for all, best for our employees, best for our customers and best for our stockholders which that enables us to make sure we fulfill our commitments on getting these strategic investments completed. We've made good progress so far. And we're taking the necessary time to make sure we get an appropriate agreement that is best for all. We'll give you an update as soon as we have an agreement.

Operator

We'll proceed to our next question on the line from Tristan Gresser PNB Paribas Exane.

Tristan Gresser - BNP Paribas Exane, Research Division - Research Analyst

Yes. The first one is in Europe. The European Commission has recently approved, I think, under EU state aid rules 2 Slovakian schemes for a budget of above EUR 1 billion to help company decarbonize in the country. So my question is, have you applied or do you plan to apply to those schemes? And if so, for what type of project facilities? And how confident are you to receive public funding there?
David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Yes. Thanks for the question. I'm going to turn it over to Rich Fruehauf here. One of the keys to our strategy is to make sure that we have a lot of optionality. That's why we have so much cash and so much liquidity. And so that's a key ingredient to the way we look at all things. Maybe, Rich, you could talk a little bit about the opportunity in Slovakia.

Richard L. Fruehauf - United States Steel Corporation - Senior VP and Chief Strategy & Sustainability Officer

Yes. Thanks, Dave. So yes, you're absolutely right. The EU Commission did recently approve the Slovak schemes. Obviously, USSK is a major employer and source of CO2 in Slovakia. So we've been watching that process very carefully. There is an allocation towards decarbonizing heavy industry in Slovakia that we would anticipate being part of the scheme when the government of Slovakia issues the call for projects. We're pleased with the support towards decarbonization we've seen so far in Europe and in Slovakia.

I think it's part of a comprehensive approach to decarbonizing these energy-intensive industries. And as I mentioned, USSK is a significant portion of the CO2 emissions that Slovakia needs to address. So we look forward to doing our part there. And we're looking at what's the best path forward for our Slovak operations. And obviously, we would look at any opportunity to see what's available to help that path forward from the government of Slovakia.

So we're evaluating that right now, and we'll let you know where we head as we complete that evaluation.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Yes. I think again, it's back to -- we want to make sure we preserve as much optionality as possible and that's the way we look at all these things that come our way.

Tristan Gresser - BNP Paribas Exane, Research Division - Research Analyst

All right. That's very helpful. And just maybe a follow-up. Do you have any timeline regarding the approval process in Slovakia?

Richard L. Fruehauf - United States Steel Corporation - Senior VP and Chief Strategy & Sustainability Officer

Well, I think that's really something that's up to the Slovakian government. Again, they have to issue as I understand their process, a call for projects. So really, that's the next step is how the Slovakian government moves forward with its process. And as I said, we'll be watching that very carefully. And as Dave said, evaluating the options under that call process from the Slovak government.

Operator

I will now proceed to our next question on the line from Emily Chieng with Goldman Sachs.

Emily Christine Chieng - Goldman Sachs Group, Inc., Research Division - Associate

Dave and Jess. My first is just a follow-up around sort of the cash flow questions that was heard so far this morning. Could you please help us with how you're expecting to see the working capital release perhaps in the fourth quarter and into 2023 and how that could help to support free cash flow generation?
Sure. Emily, I’ll take that one. So we are seeing some amount of working capital release, particularly in AR and through inventory as we move into the fourth quarter. We do expect to have positive cash flow through the fourth quarter. And when you think about -- or I should say positive working capital through the fourth quarter. When you think about the continued spend, that will ramp up on the strategic projects, right? We feel very comfortable that the pace of that spend is something that we’ve planned for, something that we’ve prefunded frankly with the cash position that we have on the balance sheet.

And even as we look forward into 2023, right? Very comfortable that consistent with our capital allocation framework, right, our cash balances will remain robust even as we continue to spend what’s necessary to move those strategic projects forward and closer to completion with 40% already behind us.

Emily Christine Chieng - Goldman Sachs Group, Inc., Research Division - Associate

Great. That’s helpful, Jess. And just one follow-up, if I may. I wanted to dig deeper into the mini mill segment and the profitability during this segment. I know you did mention that a lot of the cost increases related to high-cost inventory. But perhaps are you able to share of the $200 a ton sequential increase in costs there, how much of that was related to the high cost material and how quickly should we expect that to reverse through the next couple of quarters?

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Yes. Thanks for the question. I’d answer it this way. We definitely have some challenges here as we highlighted in the third quarter. That will continue into the fourth quarter and likely bleed into the first quarter of next year as we work it off. I mean, the good news is that’s a temporary situation, and we’ll work through that over time. And we’ll have a lot better result.

Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

Yes. And Emily, just to add to Dave’s comments there. If you think sequentially, total metallics costs of the furnace, we probably saw up somewhere in the range of $50 to $60 a ton in the third quarter versus the second quarter. I would say in total of our total kind of HRC cost at Big River, about $650-or-so was related to metallics. So certainly at elevated levels, and we would look to, with maybe 6 to 7 weeks of metallics inventory on hand with more of a long-term target of 3 to 4 weeks. We’ll have to work that off through year-end.

I think we remain selective in our buys for metallics and as we turn the page to 2023, we expect to be in a much more normalized position related to inventory levels and unit costs.

Operator

We'll get to our next question on the line from Curt Woodworth with Credit Suisse.

Curtis Rogers Woodworth - Crédit Suisse AG, Research Division - Director & Senior Analyst

David and Jess. I just wanted to drill down more into, I guess, (inaudible). Historically, we always kind of view that facility as being among the lowest cost in Europe and generally speaking, fairly advantaged from an energy perspective. And you still have kind of the benefit of some of the semi-annual contracts that were repriced over the summer. So I guess, question one is just what is the path do you think to get to profitability there? And then with respect to the guidance, you outlined $450 million of sequential EBITDA decline. Can you help break that out a little bit by segment? How much of that should we think about incremental decline into Europe sequentially?
Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

Yes. So Curt, this is Kevin. I appreciate the question. When it comes to USSK, certainly, historically, it’s been a low-cost facility on a favorable side of the cost curve there in Europe, really advantaged by its streamlined access to raw materials coming out of Russia and Ukraine. But as we know, that dynamic has changed as a result of the conflict. So we’ve seen challenges related to sourcing and resulting impacts on transportation costs and raw materials.

And then just broader energy headwinds have certainly impacted margins as well. So I think we’re more optimistic that we’ll be working our way through some of the raw material impacts through year-end, and we’ll continue to monitor broader energy headwinds that I think are impacting our facility as well as many others in the region.

Shifting to the fourth quarter, if you think about sequential declines, I mean, you should expect the pace of decline in our North American flat-rolled business to be the sharpest. We would see some step down from the mini mill segment, as Jess alluded to and then some strength, some sequential strength in our Tubular business, maybe order of magnitude, 15% to 20% up quarter-over-quarter, potentially approaching $200 million in the fourth quarter for the segment.

So definitely not for given the flow-through of prices, as Jess described in her remarks, with some more modest step backs in other segments and then strength in Tubular.

Curtis Rogers Woodworth - Crédit Suisse AG, Research Division - Director & Senior Analyst

And then just respect to the cash flow outlook, I believe Jessica you had a comment regarding 2023 that you do see still, I think, positive free cash flow, where you talked about generating free cash flow. So can you just confirm that. In the event that you would be free cash flow negative given the strength of the balance sheet, do you still feel like you could continue capital return. I know that’s kind of a Board level decision, but if you can just speak to your confidence level on those issues?

Jessica T. Graziano - United States Steel Corporation - Senior VP & CFO

Sure. Sure. So I really don’t want to get ahead of the planning process for 2023 right now. I mean we’re really knee-deep in that. So I don’t want to go too far just in terms of getting specific around what that free cash flow could look like. What I will say is if the challenges continue and we’re in a position where we look to be unfavorable from or have negative free cash flow, if you will.

The -- I think you said it best, there is confidence in our continuing without delay our strategic initiatives because of the opportunity we’ve had to prefund the balance sheet. So for sure, we know that 2023 cash flow for those strategic projects is going to be heavy, right? I mentioned in detail that we’ll have about $1.7 billion of the $2.5 billion specific -- specifically spent towards those projects. So to the extent that we have obviously offsetting cash from the operations of the business, time will tell and we’ll update you in January as we pull that budget together. But I think the bigger takeaway on cash flow and the bigger takeaway on the balance sheet is that we are very comfortable to keep going in the strategic processes that we know are going to enable that future of lower cost intensity, lower capital intensity, higher cash flow.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Curt, we’ve laid out the capital allocation process. We’re following that capital allocation process, and we’re going to get through these strategic investments and direct returns are a part of that. We have a lot of optionality. We’ve got a lot of cash. There’s a lot of things that we can do with this. We can -- need to get through the planning process. And see -- have a better view of the future. There’s massive uncertainty, as you know, related to geopolitical issues, macroeconomic issues. We’re very fortunate to have the optionality that we do, but direct returns should be a part of our normal way that we reward our stockholders.
**Operator**

We'll now proceed to our next question from the line of Carlos De Alba with Morgan Stanley.

**Carlos De Alba - Morgan Stanley, Research Division - Equity Analyst**

Some of my questions have been answered already. But just on sustaining CapEx or the CapEx on your existing footprint. I think, Jess, you mentioned around $650 million in 2023. How should we think about this going forward, given the investments in the strategic projects that you have, the renewal, if you will, to some extent or a shift in your asset base? How should we think about this number going forward? And I understand that it might be early, but just maybe just a path that would be useful?

**David Boyd Burritt - United States Steel Corporation - President, CEO & Director**

I think in basic, we have challenges we're doing our best to overcome. We're too cost intense, we're too capital intense, we're too carbon intense. And so over time, the problems we're trying to say at (inaudible) does it become less cost intensive and less capital intensive? So over time, those numbers will come down as we implement our strategic projects over the horizon here over the next 2 to 3 years so that the future is going to be a lot less capital intensity.

**Operator**

[We're going to turn the next] question on the line is with Karl Blunden of Goldman Sachs.

**Karl Blunden - Goldman Sachs Group, Inc., Research Division - Senior Analyst**

Thanks very much for the time. Just a question on the footprint. You commented on recently idling some blast furnace operations in Gary and Mon Valley and an intent to bring them up back online. Depending on customer demand, are there specific signals you're looking at to bring those back? Is it a volume that customers want? Is it a price signal? Just some kind of visibility into how that will evolve would be very helpful?

**David Boyd Burritt - United States Steel Corporation - President, CEO & Director**

It's obviously a multi-variant analysis, but we're always staying very close to the customers. And the priority is to make sure that we have the steel on time, high-quality, delivered safely to them. So the signals are pretty basic. We take a look at what their needs are, and we do our best to fill them. And when they tell us it looks like it's ramping up, we'll ramp up as well. And we're looking for those signals. We're working closely with them. We have ongoing daily conversations. And when they place the orders, we fill the book.

**Karl Blunden - Goldman Sachs Group, Inc., Research Division - Senior Analyst**

Should I just -- on the balance sheet. You recently extended some maturities and at a pretty attractive interest cost by using -- by accessing different parts of the debt market. Is there more opportunity for that? You don't have a lot of debt that's due near term, but a little bit of '29 debt that you could extend. Is there a goal to do some more of those kind of extensions when you think about liability management?

**Jessica T. Graziano - United States Steel Corporation - Senior VP & CFO**

We're always looking at opportunities. I mean we have a fantastic treasury team that is always communicating with the market looking at opportunities to continue to tighten and strengthen our balance sheet going forward. There's nothing that I'd speak to specifically now in terms of looking for
a near-term action on the balance sheet. But I guess the takeaway is we're always looking, we're always talking to the market, have very close relationships with the banks. And we'll take advantage of opportunities as they arise for us to, again, continue to strengthen that balance sheet.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Will preserve optionality and we'll be opportunistic.

Operator

We'll get to our next question on the line from Gordon Johnson with GLJ Research.

Gordon Lee Johnson - GLJ Research, LLC - CEO & Founder

A lot of my questions have been answered. I know you talked about BRS, but can you talk a little bit about -- more about -- it seems like you guys are guiding to EBITDA there to roughly $40 million down -- I'm sorry that the result was $40 million, it was down again in Q4. Can you talk a little bit about -- I know there's higher costs associated, but can you talk a little bit about the underperformance there? And what should we expect looking into 2023? And then I have a follow-up.

Jessica T. Graziano - United States Steel Corporation - Senior VP & CFO

I'm sorry, were you talking about BRS specifically? We couldn't hear parts of your question. Do you mind just repeating? We want to make sure we're answering you right on. Is the BRS you're asking about?

Gordon Lee Johnson - GLJ Research, LLC - CEO & Founder

Yes. BRS specifically.

Jessica T. Graziano - United States Steel Corporation - Senior VP & CFO

And your question was about cost pressures or what we're looking BRS going forward into '23?

Gordon Lee Johnson - GLJ Research, LLC - CEO & Founder

Yes. I guess just overall, a bit of underperformance this quarter and the guidance was a bit weaker than we expected. I wanted to get your thoughts on kind of what's driving that beyond cost pressures? Is it just cost pressures? And what you expect in 2023? And then I have a follow-up.

Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

Sure. Thanks, Gordon. This is Kevin. So as Jess articulated in the prepared remarks, right, the raw material headwinds certainly believe to be temporary, really persisting through year-end, but resetting towards the beginning parts of 2023. That had about an 800 basis point impact on margins. So if you add that back to the 6% of third quarter performance, that gets us back more towards the mid-teens goal that we've set for the business before executing projects like the nongrain-oriented electrical steel line and the additional galvanizing capabilities.

So what we saw in the third quarter, I think, was also impacted by just the mix there at Big River as we continue to mature that facility and increase its capabilities. Product mix in the third quarter was certainly more skewed towards HRC, which is about 60% to 65% of the book in the quarter. As
we bring on projects like the NGO line, that will add additional volume, 200,000 tons of electrical steel as we add capabilities related to the galvanizing facility, which is another 300-plus thousand tons of downstream value-added product. We would see that mix really rebalancing to something more -- certainly more diversified, maybe 50% of the book being more hot-rolled with the remainder being downstream, value-added product, including 10% of the book being an NGO Steel going forward.

So to Dave and Jess’s comments, we remain very, very confident in that business is financial and strategic impact on the enterprise. And as we continue to complete these projects on time and on budget, we see tremendous opportunity to continue to enhance the mix and drive margins even higher into the low 20% after the completion of those projects. So the fourth quarter, as you mentioned, we’ll continue to be, I think, burdened by some of the high-cost raw materials. But as we turn the page into 2023, we’re confident the business will be more normalized from a cost perspective and really, really excited for the second half of next year as the NGO line comes on, and we expect to meet really robust demand quite quickly.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Yes. There’s no doubt there are the short-term challenges here, and this temporary impact of the high cost raw material. But to Kevin’s point there, we should be well into the mid- to high teens on Big River and then a low 20 percentile as we get the NGO and galvalume. We’ve got to get a better balanced book. We need to make sure we fill the mill. We need to make sure that we get this thing back on track. And I don’t think there’s any question the best days are ahead for this facility. We got great talent down there. We got great operations, and it’s got a great future.

Gordon Lee Johnson - GLJ Research, LLC - CEO & Founder

And then just one last one on my end. Looking at imports, is it fair to assume that import prices are somewhat negatively affecting things now and if things shift there we could see a positive impact. And then you guys have done great with respect to capital allocation, in my view. But it seems like you guys are going full steam ahead with CapEx and share repurchases. Is there an HRC price at which you guys would accelerate that and/or decelerate that?

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

For our top priority, of course here, is to make sure that we're pleasing these stockholders, right? And the way we do that is do it over the longer term. We've got to get this next mini mill in place. We've got to get the NGO line, the galvalume, these strategic projects on budget, on time. And those are really important for us to deliver the value that our stockholders expect and deserve. And along that path, we want to give them some direct returns. So that's what we're headed for. We're not setting a specific target on HRC or things like that. We let the marketplace, we let the economic environment, we let our customers tell us how good we are going to be here in the short term. But longer term, again, I'm just over the top bullish.

Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

Yes. And then Gordon, I think on imports, right, we've seen the global price gap continue to narrow, and we think that's going to have a positive impact on import penetration into the ...
Kevin Lewis - United States Steel Corporation - VP of IR and Corporate FP&A

And we continue to be very, very encouraged with various trade actions, reconfirmations of various policies that we talked about in our prepared remarks. So we’re optimistic from that perspective.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

And these trade cases, it’s great to see this administration carry forward with understanding the #1 priority for any sovereign state is safety and security. And when you get that right and you have a strong manufacturing base, I’m bullish on the countries that understand that. So I’m bullish on the U.S.A. for sure.

Operator

Thank you very much. And there are no further questions at this time. I’ll now turn the call back to U.S. Steel’s CEO, David Burritt for closing comments.

David Boyd Burritt - United States Steel Corporation - President, CEO & Director

Thank you again for joining us this morning. We are on pace for the second best year in U.S. Steel history and are set up for success in 2023 and beyond. Thank you to our employees who come to work every day to make the steel our customers depend upon. When we do well, you do well, and we’re demonstrating that again with another quarter of significant profit sharing. We are working towards a common goal to make U.S. Steel the best steel company and to provide our customers with profitable steel solutions for people and planet.

We are pleased to safely and reliably provide high-quality steels to our customers. My thanks to each and every customer for your continued partnership. Thank you also to our investors. We are generating value by investing in the future, while rewarding you along the way with direct returns. We’ve already delivered record results in 2021 and 2022, and we’re confident this business is better positioned than ever before to create long-term value for stockholders.

We look forward to proving the value of our Best for All strategy today and tomorrow. Now let’s get back to work safely.

Operator

Thank you very much. That does conclude the conference call for today. We thank you for your participation and ask you to disconnect your lines. Have a good day, everyone.