Cleveland-Cliffs, Inc.
First-Quarter 2024 Earnings Conference Call
April 23, 2024

Presenters
Lourenco Goncalves, Chairman, President & Chief Executive Officer
Celso Goncalves, Executive Vice President & Chief Financial Officer

Q&A Participants
Lucas Pipes - B. Riley Securities
Bill Peterson - JPMorgan
Phil Gibbs - KeyBanc Capital Markets
Alex Hacking - Citi
Tristan Gresser - BNP Parabas
Lawson Winder - Bank of America

Operator
Good morning, ladies and gentlemen. My name is Rob, and I am your conference facilitator, today. I would like to welcome everyone to Cleveland-Cliffs First Quarter 2024 Earnings Conference Call.

All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session.

The company reminds you that certain comments made on today's call will include predictive statements that are intended to be made as forward-looking within the Safe Harbor protections of the Private Securities Litigation Reform Act of 1995. Although the company believes that its forward-looking statements are based on reasonable assumptions, such statements are subject to risks and uncertainties that could cause actual results to differ materially.

Important factors that could cause results to differ materially are set forth in reports on Forms 10-K and 10-Q and news release filed with the SEC, which are available on the company's website. Today's conference call is also available and being broadcast at clevelandcliffs.com.
At the conclusion of the call, it will be archived on the website and available for replay. The company will also discuss results, excluding certain special items. Reconciliation for Regulation G purposes can be found in the earnings release, which was published yesterday.

At this time, I would like to introduce Celso Goncalves, Executive Vice President and Chief Financial Officer.

Celso Goncalves
Good morning, everyone. As I did on the last conference call, I'm going to start, today, by providing an update on capital allocation and M&A.

On our last call in February, I indicated that we would be much more aggressive with returning capital to shareholders and made it very clear that share buybacks are now the number one capital allocation priority for Cleveland-Cliffs.

Consistent with what we said we would do, we bought back more than 30 million CLF shares during Q1 by utilizing the remaining $608 million from our prior $1 billion share buyback program, announced in 2022.

In the last couple of years, we have reduced our diluted share count by over 100 million shares, or 17%, realizing an average purchase price of $18.79 per share on open market repurchases, significantly below where we are trading, today.

Going forward, given our strong free cash flow outlook and healthy liquidity, we are introducing a new $1.5 billion share repurchase program that we plan to deploy immediately and aggressively during open windows.

This new buyback program is also supported by the fact that we are no longer compelled to preserve as much dry powder for M&A, given the limited number of possible outcomes for U.S. Steel.

It's now clear that their “strategic alternatives review process” was only “robust” and “competitive” because the company and their financial advisers at Barclays and Goldman Sachs invited foreign buyers, creative consortiums and companies with no support from the USW.

As we explained to U.S. Steel, to their advisers, and to the entire market early in the process last year, there is no way to close the sale of U.S. Steel without agreement and full support from the USW. We discussed publicly in August that the USW has de-facto veto power in the outcome of this process, but U.S. Steel denied it. Back then, Cliffs was right and U.S. Steel was wrong. Today, we continue to be right and they continue to be wrong.

There's no denying reality anymore. The USW has said from the very beginning that they would not endorse any other buyer, only Cleveland-Cliffs. Union leaders do not go back on their word. And now after President Biden has clearly expressed his position, unequivocally, against foreign ownership of U.S. Steel, the list of real buyers for the company is even more evidently a party of one. Cliffs is the only union friendly American solution for U.S. Steel. The Nippon deal is dead and other buyers stand no chance to close a deal involving U.S. Steel union assets.

In terms of value, the inflated bids resulting from the blind auction process that included unrealistic buyers don't represent a meaningful proxy for real valuation and neither do the standalone price targets coming from research firms pandering to the arbs. A company is only worth what a real buyer or investor is willing to pay for it, and everything else is just an opinion.

The last time that real steel industry investors owned U.S. Steel, the stock was valued at $22.72. The valuation reset lower is far from over. We will have to reassess everything, including value, once we have the chance to reengage in M&A due diligence, as everything we saw last year is now stale.

Obviously, there is no assurance that U.S. Steel will even want to sell to Cliffs. The company can always stick around as a standalone entity and the arbs holding the stock can always sell their shares back to the real investors in the $20's. In the meantime, Cliffs will continue to buy back our own CLF stock, hand over fist like we did in Q1.

Buying our own stock and returning dollars to our Cliffs shareholders, who are real investors, is a much better use of capital than any M&A opportunities at current valuations.

From a leverage standpoint, we are implementing a more shareholder-friendly leverage target of 2.5 times net debt to last 12 months Adjusted EBITDA, allowing ourselves even more flexibility for aggressive shareholder returns.

We have made a lot of progress on the balance sheet over the past few years. As of the end of 2023, we outperformed our prior net debt target level of $3 billion, but the rating agencies gave us no credit for the massive debt reduction last year and kept our ratings unchanged. If the agencies are just going to keep our ratings where they are now, we might as well give ourselves the flexibility to buy back more stock.

At 2.5 times net debt to EBITDA, there is also no risk of a ratings downgrade from where we currently are. We have flexibility up to 3 or 3.5 times, before risking any downgrade. By self-imposing the 2.5 times threshold on ourselves, we are just allowing for more flexibility, while remaining comfortably within the spectrum of our existing ratings category.

This new leverage target just gives us the ability to continue to execute open market share buybacks. And even if we deploy the entire $1.5 billion program throughout this year, our net leverage would still be comfortably well below 2.5 times.

This new leverage target also applies in the context of M&A. Any acquisition situation would also be limited to pro forma net leverage at the same self-imposed 2.5 times target level.

Obviously, any M&A that we do will come with meaningful EBITDA contribution, significant synergy realization and increased scale that will be viewed by the rating agencies and bond investors as a credit positive.

For the avoidance of doubt, we are not currently performing due diligence on any M&A opportunity that would prohibit us from buying back stock today. And even if the U.S. Steel situation were to resurface at some point in the future, we would need to refresh our due diligence at that point and reset valuation expectations from current levels.

Our balance sheet continues to be in great shape with near record liquidity and no secured bonds in our capital structure for the first time since 2017.

During the quarter, we launched the redemption of our final tranche of secured debt that was also our nearest dated bond maturity. With no debt maturities until 2027, we now have a 3-year maturity runway that gives us even further comfort with our new target level. This is the best shape our capital structure has been in since Lourenco took over the company ten years ago.

As a result of higher automotive sales during the quarter, our Q1 adjusted EBITDA of $414 million marked a rebound in profitability from the latest trough in Q4. With production and sales of cars, trucks and SUVs remaining healthy in the U.S. throughout Q1, our average sales pricing came in much better than expected, due to a greater participation of automotive in our Q1 steel sales mix. Conversely, in January and February, service centers went on a typical buyers' strike, which led to reduced sales to the distribution sector.

The net result of this dynamic of more sales to automotive and fewer tons delivered to service centers led to a reduced sales output of 3.9 million net tons. Now that the distributors and service centers have come off the sidelines and steel pricing is on an upward trend, we expect to again exceed the 4 million ton shipment level in the second quarter.

Unit costs were, of course, impacted by the heavy automotive mix in Q1, as well as the overall lower production volumes, though we maintain our previous guidance of an approximately $30 per net ton reduction in unit cost in 2024, compared to 2023. That will begin here in Q2 with an expected $20 per ton drop in costs, quarter-over-quarter.

The lower production volume in Q1 and heavier automotive mix impact on unit cost, have been offset by lower natural gas prices. As is typical in the first quarter, working capital represented a use of cash, which we expect to recover in the second quarter.

Also during Q1, as widely publicized by the U.S. government, we were selected for award negotiations related to two decarbonization projects for a total of $575 million worth of DOE grants. These projects should not impact our capital spend expectations for this year. And in the case of the Middletown DRI EMF project, the new investment will, significantly, mitigate future expenditures related to the Middletown blast furnace and other infrastructure.

Our investment expectation related to the two projects is that our net capital expenditures will hover around $1 billion from 2025 through 2028 with the ultimate outcome of $550 million in annual cost savings starting in 2029, with virtually no impact to production.

With that, I will turn it over to Lourenco for his remarks.

Lourenco Goncalves
Thank you, Celso, and good morning, everyone. Cleveland-Cliffs has a very simple, yet somehow unique way of conducting business in corporate America. We respect our workforce.

There is nothing special or particularly complex beyond that. Our employees drive our performance and our profitability. Our workforce is the reason why we're here, and they are treated accordingly. Of course, this has always been the case during the last 10 years I have been running Cliffs. But the events of the past year have, obviously, shed a brighter light on this.

Our relationship with all workers and, particularly, with the union represented workers, is a function of the long view we have taken with respect to our labor force and not something that can be outshined by empty promises from outsiders written on worthless pieces of paper.

Nippon Steel, the unsuccessful attempted acquirer of U.S. Steel, has failed to understand this. It still baffles me to this day that the clueless individuals representing Nippon Steel in this embarrassing event felt that they could do this, without union support. You just cannot do it with a USW represented workforce.

This historic M&A fiasco was a direct consequence of the goals the U.S. Steel CEO and his fellow Board members had in mind. First, to do good for the stockholders only, ignoring everyone else; and second, to break the back of the USW. Therefore, for them, it was necessary not to sell to Cleveland-Cliffs.

To give a sense of the enormous prejudice against Cliffs and against the USW, despite all we have clearly demonstrated to them, the U.S. Steel directors and their advisers from Milbank, Wachtel, Goldman Sachs and Barclays, still chose a buyer that cannot close the deal.

We are grateful that the U.S. government shares the same view we have always had about the importance of union jobs for a thriving middle class in America. The Biden Administration has different ways to terminate the Nippon transaction, and we believe that will be done sooner rather than later.

Before the President of the United States had expressed his clear position, we attempted to offer a solution to Nippon Steel, where we would acquire the union represented assets of U.S. Steel, and Nippon would keep the assets they wanted in the first place, the non-union Big River steel facility.

Nippon did not accept that. And now after President Biden has spoken, this option is no longer available to them. Nippon is now saying they actually value the blast furnaces because they can apply their great technology.

Let me be clear; this talking point on technology is complete hogwash. There is nothing special about the Japanese blast furnace technology. We are far ahead of them on everything blast furnace related. The use of iron ore pellets and no sinter, direct reduction, the charging of HBI in blast furnaces, the injection of natural gas and hydrogen, we already have all that in the United States at Cleveland-Cliffs, and they do not have any of that in Japan.

Their so-called superior technology is not even remotely based on facts. But one thing that's good about Nippon Steel now being hell-bent on owning blast furnaces and BOFs in the United States is that people that used to say that blast furnaces and BOFs are bad don't know what to say, anymore. They are now on mute.

Thanks, Nippon Steel, for validating my point. You have to pay the breakup fee of $565 million just to prove my point, and I appreciate that. Your money will be well spent.

Another relevant point ignored by the U.S. Steel board, Nippon still has been a perpetual violator of our trade laws, probably the worst actor in the international steel trade over the past several decades among all. In my view, Nippon Steel is actually worse than the Chinese. And they also have significant interest in China, which they love to downplay. Unfortunately, for them, Nippon Steel cannot hide their deep ties with the Chinese, and that has also been completely exposed.

Nippon's existence in the U.S. is also bad for customers. By the way, in order to obtain a price increase back in Japan, Nippon Steel has recently sued the largest Japanese automotive manufacturer, Toyota. Cleveland-Cliffs has never done that here in the United States and for the record, Toyota here in the United States is our largest automotive client.

When this thing ultimately ends, we are in a whole new world. If the feelings of U.S. Steel directors are hurt, but by what I have said or done and they still don't want to sell the company to Cleveland-Cliffs, that's their prerogative. At the end of the day, they don't have to sell themselves to Cliffs, and there is no easy way to force them to do so. But their only other alternative after they collect the breakup fee from Nippon is to continue as a standalone company. If that's going to be the case, good luck running the assets that you hate with the workers you don't respect.

From our side, Cliffs has several other opportunities, with or without M&A. The most relevant example of that, right now, is our share repurchases. We were overdue in Q1 and with our new reauthorization we are still buyers of our stock at today's price. We also just displayed our ability to grow profits organically, with the two projects we are initiating with support of the U.S. government.

The $1.3 billion investment at Middletown Works replacing our blast furnaces with a DRI facility and two electrical melting furnaces is a game changer for our company and for our industry. The $500 million co-investment we will receive makes this project the largest federally supported de-carbonization initiative in U.S. history.

The government took note of our investment in direct reduction made seven years ago, as well as our 30% reduction in CO_2 emissions over a six-year period and our technological advances on hydrogen utilization.

In our recently published Sustainability Report, we reported another reduction in integrated emissions intensity to 1.54 metric tons of CO_2 per metric ton of steel, down from 1.82 in 2020 and, significantly, below the current global average of 2.15. When the Middletown project is in full operation, Middletown Works will be the lowest cost steel producing facility in the United States.

To illustrate the cost savings, our current cost to produce pig iron in Middletown is about $470 per net ton, and our current cost to produce DRI is less than $200 per net ton.

Hot DRI will be fed into a melting furnace, a very simple process to melt solid DRI into liquid, creating a pig iron equivalent that can be fed into our existing BOFs and process it further, downstream.

Knowing that scrap will become scarce, expensive and more contaminated over time, we will avoid any increase in our scrap intake, maintaining our ability to serve the highest quality demand in end markets, like the automotive, market by using pure iron. That's technology, American technology, not Japanese hogwash PR.

At Butler Works, we were awarded $75 million by the DOE to replace our natural gas fired slab reheat furnaces with electrified slab furnaces. That will reduce emissions, improve productivity and enhance our production of GOES, grain-oriented electrical steel, critical to our country's electrical grid.

The future of our production of GOES was at risk under the initial draft of the DOE's new emissions standard as proposed, last year. If adopted as initially proposed, the new standard would have effectively replaced the use of GOES in all transformers used in the United States with made in Japan amorphous metal.

Fortunately, the DOE heard what Cliffs and our American clients, the company is producing transformers in the United States, we're telling them. And with great help from elected officials like Senator Sherrod Brown of Ohio, Senator Bob Casey of Pennsylvania, and Governor Josh

Shapiro of Pennsylvania, as well as Representative Mike Kelly from Butler County in Pennsylvania and Representative Chris Deluzio of Pittsburgh, Pennsylvania, just to name a few, a more reasonable standard was adopted.

With that, our customers will continue to be in business, and they will continue to use GOES to produce the transformers our country needs.

By the way, there is pent-up demand for transformers in the United States, and that's a great opportunity to produce more transformers and to generate more jobs for American workers.

We expect to see significant investment from our customers in this important piece of infrastructure, and we must produce more made in USA transformers. That's totally viable because Cliffs already has enough additional steel producing capacity for GOES to deploy in Butler, Pennsylvania and Zanesville, Ohio.

Our other major move this quarter, was announcing the indefinite idle of our Weirton facility, which officially ceased production on April 11th. Over the past three years, Weirton's average annual contribution to our EBITDA was a negative $100 million, due largely to unfairly traded imports of tinplate products.

In January, the Department of Commerce recommended antidumping and countervailing duties on some of these imports, which would have mitigated this issue. But in February, the International Trade Commission, in a totally surprising decision, reversed the Department of Commerce recommendation, allowing for low-priced imports to continue to flow into the United States.

As a result, we had no choice but to exit the tinplate market, leaving more than 900 Weirton employees without a job. Some of these employees elected to retire, and we were able to offer the impacted workers employment at other Cliffs facilities. As of today, we have been able to relocate over 100 employees to other Cliffs locations.

Our GAAP loss in Q1 is primarily driven by the approximately $170 million in one-time charges taken at Weirton, mainly employee support costs, along with asset impairments and other expenses.

Clearly, this was an eventful quarter for us. Our automotive business carried the day for us, once again, as the automotive sector in the US continues to improve, growing for the fourth consecutive year.

Our customers need us for our best-in-class quality, delivery performance, customer service and technical expertise. Buying steel from other suppliers is just a price-driven decision for each one of the individual car manufacturers, but not all car manufacturers are willing to bet their performance on less competent suppliers just to save a few bucks per ton. Some are willing to do so and these ones will be treated by Cleveland-Cliffs, accordingly. Message delivered.

On the flip side, service center business lagged on both volume and price during the past quarter, impacting our production volume. Demand has since returned, and we have had success in implementing our recent price increase. This should support prices and shipments above the 4 million-ton level in Q2.

With that, I will turn it over to Rob for Q&A.

Operator
Thank you. We will now be conducting a question-and-answer session. If you would like to ask a question, today, you may press "*", "1" from your telephone keypad, and a confirmation tone will indicate your line is in the question queue. You may press "*", "2" if you would like to remove your question from the queue. For participants that are using speaker equipment, it may be necessary to pick up your handset, before pressing the star keys.

One moment, please, while we pull for questions. Once again, that's "*", "1". Thank you.

Our first question, today is from the line of Lucas Pipes with B. Riley Securities. Please proceed with your question.

Lucas Pipes
Thank you very much, Rob. Good morning, everyone. Lourenco, you said the option that Nippon essentially acquires the non-union assets and you acquire the union assets is dead. And I wondered, is there anything that could revive that option? Any thoughts on that? Thank you very much.

Lourenco Goncalves
Thank you for the question, Lucas, and good morning to you. By the way, I said that I offered this option, but I'm assuming that between Citibank and the bank representing Nippon Steel and Ropes & Gray, the law firm representing Nippon Steel, they were able to at least deliver the message to Nippon Steel because Nippon Steel never had the courtesy to reply to my offer, to sit down and discuss.

So, I'm just assuming that they said what the--they did what they said they had done to deliver the proposal to Nippon Steel. That said, yeah, the proposal is gone because at this point, the President of the United States already said what he's going to do. He's not a dictator. He needs to wait for the process to run.

And then he will do what he already promised, publicly, to the workers of the USW, to the President of the USW, Dave McCall, and he has repeated in public situations. So it's game over.

I cannot go against the word of the President of the United States. So, therefore, my option is totally 100% off the table.

Lucas Pipes
That's very clear. Thank you. Thank you for that. And so, I think in the prepared remarks, you mentioned cost reduction in Q2. Could you remind me, or us, of those? And also, what would be the impact on margins in the current steel environment in Q2 and also for the rest of the year? And as you think about free cash flow, any portion that would go towards deleveraging off the kid of higher Q1 levels or 100% towards the buyback? Thank you very much.

Celso Goncalves
Yeah, sure. Hey, Lucas. Good morning. As it relates to costs, we indicated that from 2023 to 2024, we're going to achieve a $30 per ton decrease, which equates to kind of a $500 million savings on an annualized basis. And that's going to come from, primarily, lower cost coal. We negotiated our coal contracts very well, lower natural gas, lower alloy costs. So these are the three primary drivers that are going to help our costs.

As it relates to Q2, specifically, costs are going to be down $20 a ton. You'll start to see the full benefit from these lower coal contracts. Natural gas has also been lower than we expected, and the mix is going to be slightly less value-add here in Q2, which is going to help costs.

As it relates to your other question, I believe you asked in terms of free cash flow and deleveraging. I think we made it pretty clear that share buybacks would be the number one priority. I made that abundantly clear in the last call. But obviously, if we do see opportunities to buy back bonds in the open market, we'll look to do that as well. We didn't have that opportunity during Q1, because our bonds were, essentially, all trading above par, and we had already paid down the entire balance of the ABL.

We're giving ourselves this flexibility to use a little bit more leverage within our existing rating category to buy back more stock. But if there are opportunities to buy back bonds in the open market, we'll look to do that, as well.

Lucas Pipes
Sounds good. Thank you very much for all the color, Lourenco and team. Continued best of luck. Thank you.

Lourenco Goncalves
Thank you, Lucas. Appreciate it.

Operator
Our next question is from the line of Bill Peterson with JPMorgan. Please proceed with your questions.

Bill Peterson
Yeah. Hi. Good morning, Lourenco, Celso and team. Thanks for taking the questions. I wanted to follow up on that, and you said--you answered a little bit on the prior question, but how should we think about the product mix and then as that impacts the trajectory of pricing into the second quarter? And maybe related to that, if we think about the negotiations you've had with the auto contract negotiations, how do they play out, especially with the Japan headquarter companies, given their fiscal year timing?

Lourenco Goncalves
Good morning, Bill. The auto negotiations for this period are the ones related to the clients that have an April 1 renewal time. And those are basically the Asians, Japanese, Korean transplants because their fiscal year is April 1 in their respective countries. And I'm glad to inform that these negotiations are completely uneventful, and everything went totally smooth. And we accomplished what we are asking for. And I'm sure that they are happy because the tonnages delivered to each one of these guys are growing on each one of them.

So consolidating, for example, one of the Asians above Stellantis as a bigger client for Cleveland-Cliffs. So, this specific client is now much bigger than Stellantis. Stellantis, for us, became like another part of the pack. It's no longer a top priority for me and for Cleveland-Cliffs. They are now treated here as a second-class citizen, and we are going to continue to do that for the ones that are price driven, like Stellantis.

So, April was great, it was fantastic. And keep in mind, we continue to grow tonnage for automotive. The only difference is that we are concentrating more on the--some of the clients and selling less for other clients. This will be reflected on the quality of the cars. It's a matter of time. When you're only hitting for low cost, at the end of the day, you end up building a car that sucks. And that's what I expect to happen, and we are going to help differentiate the good ones from the bad ones. I would say that the April crowd was, in its totality, part of the good one block.

Bill Peterson
Yeah. Maybe you can also--maybe speak to the product mix and trajectory of pricing into the second quarter, please?

Lourenco Goncalves
Let me take the product mix, as well. Second quarter will be a lot more normal, Bill, than the first quarter because if you recall, January and February, we had kind of a buyer's strike among service centers. They're all expecting price to go down and not buying, uncertainty and waiting for the Fed and waiting for this, waiting for that and nobody was buying. And that was a very complicated period for us at the beginning of the first quarter. And that's also why we had so much more concentration on automotive.

It’s not like automotive was buying a lot more, it’s because service centers were buying a lot less. But then things resolved after we announced the first price increase, first price increase went through, very well. Then we announced the second price increase, then our competitor announced a price that became kind of a reference in the marketplace just to bring a different perspective, their intentions.

But at the end of the day, that is still playing out in the marketplace, and we are still working through the consequences of that event. But all in all, I see Q2 returning to a more, much more normal mix between service center and distribution and automotive. So automotive will continue to be good. Service center and distribution will become bigger, and that will bring the mix back to where the mix normally is.

Celso Goncalves
Yeah, Bill, and just to answer your question on selling price, which I believe is what you were focused on. Obviously, this mix--the mix will have an impact on pricing, obviously, in Q2. And I think we've given enough in terms of bread crumbs that you can kind of calculate what the impact might be.

But just to kind of refresh for everyone in terms of what the contract lags are related to our index-linked contracts, we're about 40% to 45% fixed with full year price. And then we have 20%, which are on CRU month lags, about 10% of the volumes are slab on a 2-month lag. 10% are CRU quarter lags and the rest, call it, 10% to 15% is true spot. So when you think about Q2, the monthly lag is down from Q1, the quarter lag is up from Q1. But overall, you can kind of expect Q2 average selling price to be down around $40 a ton.

Bill Peterson
That's super helpful. Thanks for that, all that insight. Second one is on CapEx. And I guess, thinking about the company on a stand-alone basis with net CapEx, excluding awards and so forth. You talked about like, I guess, $1 billion normalized over the next four years, after this year. Can you provide a little more granularity on 2025, in particular, with assuming you have better visibility or maybe even the '26? Just a lot of questions we've been getting is how to think about your free cash flow generation ability, beyond this year.

Celso Goncalves
Yah,. I think it's a little too early to go into the granularity of 2025. I think the easiest way to think about it is just stick to that $700 million for this year, which we're very confident with. 2025 probably won't even get to $1 billion, and then you're only exceeding $1 billion when you get to 2026. But as we get closer, we'll be able to share more detail related to '25 and '26.

Bill Peterson
Thanks, Celso.

Celso Goncalves

Thank you.

Operator
Our next question comes from the line of Phil Gibbs with KeyBanc Capital Markets. Please proceed with your questions.

Phil Gibbs
Hey, good morning.

Lourenco Goncalves
Good morning, Phil.

Phil Gibbs
I have a question just on the timing of the DOE grant. You obviously have two very substantial CapEx projects, over '25 to '28 timeframe. Do those DOE grants get let as you spend the capital on the project, or is that kind of a lump sum fund that you get upfront, before you start spending?

Lourenco Goncalves
I'll let Celso take that.

Celso Goncalves
Yeah-no, Phil, you're right, they're paid out pro rata with the spend. That's the easiest way to think about it.

Phil Gibbs
Thank you. And then maybe with the Middletown project, given that it's so substantial in timing and scope, can you give us kind of the time line of or the pockets of phases, as you all are looking at it? And what more do you need to complete in terms of due diligence or design?

You've given this as relatively new technology, at least to the states. I think people would just be interested in hearing that.

Lourenco Goncalves
Yeah. No, look, it's a brand-new facility there but it's not, by any stretch, new technology because it's the combination of a direct reduction plant that instead of producing DRI, we will be producing--I'm sorry, instead of producing HBI like our plant in Toledo, we'll be producing hot DRI, and that hot DRI will be fed in on-site through two EMFs.

And what's an EMF? It's just electric arc furnace to melt iron ore, to melt, to melt, in the case of this facility iron ore metallic, because it will be sponge iron, hot DRI from the direct reduction plant. So it's a simple setup. There's nothing really complex.

And these are two things that we do extremely well. We have electric arc furnaces, so we dominate this operation. And we absolutely have the best-in-class direct reduction plant, as far as I know, in the world. So, we are going to be hydrogen ready, and we are hydrogen ready in Toledo. We have been using hydrogen.

So hopefully, by 2029, when this plant goes into operation, we are able to start with the hydrogen or we'll start just for the start up with the natural gas and then, immediately, go to syngas and in the short-term, be 100% hydrogen, by the early 30s.

So, this is real game changing in terms of the technology to produce steel, in particular to produce automotive grade steel. But it's a combination of a lot of things that; one, we have full knowledge and full operational capability; and second, we are operational proven in terms of how to use all these things. So it's no big deal.

Phil Gibbs
Thanks Lourenco. And then just lastly on the mix. You mentioned auto carried the day in Q1, the service centers took a step back. Are we expecting or are you expecting rather, auto to be relatively stable in Q2, and then service centers to be the driver of the increased volume, or is automotive improving, as well?

Lourenco Goncalves
Phil, automotive continues to do very well, particularly now that they are no longer all pursuing to be the next Tesla. They are not as hell-bent on going all into electric vehicles as they were even six months or 12 months ago. They are now talking turkey. The cars that are selling are the ICE and now the hybrids. So the ones that are moving faster to hybrids are the ones that are winning the day.

And because we are so big and supporting pretty much all of them, except one that only buys cheap stuff, we are going to really continue to support the ones that are growing. And we don't have a problem picking winners and losers among the car manufacturers.

For example, yesterday, I announced that I'm no longer selling steel to Volkswagen in Mexico because there is no point in selling steel from the United States to Mexico, just to have Volkswagen then sending back cars to the United States just to pay cheaper wages to workers in Mexico.

I'm not going to support that, particularly now that the UAW was able to unionize the plant in Chattanooga, Tennessee, for Volkswagen. I would rather sell to Chattanooga, Tennessee. So, we are going to start to be a lot more selective among our automotive clients.

But make no mistake, automotive is a good business for us. But the only innovation that the alliance for American innovation can come up with this we need to sell to lower price. So we are not going to do that. And we are going to continue to play the Cleveland-Cliffs game.

We don't need to grow our size in automotive through M&A. We are big enough, but we can be smaller but be smarter. And that's what we are going to do, and that will bear fruit for Cleveland Cliffs, going forward.

Phil Gibbs
And lastly, Lourenco and team, on the grain oriented electrical steel market, I think your comments over the next several years are very bullish, particularly as it relates to grid spend and the timing of around when that is going to take place.

But what's your outlook in the shorter term, maybe in the next six months to 12 months in terms of volumes? And then within that question, you also mentioned in your prepared remarks that you expected some reshoring perhaps after this space we saw in the last 10 years of offshoring into Canada and Mexico on the transformer side. Maybe shed some light on that aspect, too. Appreciate it. Thanks.

Lourenco Goncalves
Look, this situation of reshoring only happens because for a while, we allowed the thing to go away from us. But we have been working very hard, since the Trump Administration, to stop this bleeding. If you recall, during the last couple of years of the Trump Administration, we worked very hard to put a Section 232 on cores and laminations. And the main reason was the distribution with Mexico that was allowing that to happen.

We were able to fix that without the Section 232 which, by the way, was never signed by President Trump, despite the great efforts from the USTR ambassador, Bob Lighthizer. For some reason, President Trump never signed that thing. But this is water under the bridge. We fixed the thing with the clients. And the clients are not doing that in Mexico anymore, at least not to a major scale.

On the other hand, we still have the importation of transformers into this country. And that was discussed in that situation, yesterday, with Secretary Jennifer Granholm about the risk we are taking, when we import transformers. Among other things, we don't even know what's inside the transformer, when you import the entire transformers. So, we need to stop that and that's for national security reasons.

So, we will continue to work with the Biden Administration. And whoever is the president after the election, we will continue to work on that. We need to stop importing transformers. We can't allow that to happen. We need to build more transformers in the United States.

The good thing is that our dialogue with these clients that produce transformers in the United States is fantastic. We are working on a solution for Weirton that will resolve a lot of the situation with the transformers, will allow us to produce more GOES. We have spare capacity.

With minor investments, we can increase 50% to 70% of our throughput in Butler just to produce more GOES, grain-oriented the electrical steels for transformers.

So, we want to put up a new factory in Weirton, West Virginia, using our workforce there to produce transformers. We can co-invest; we can just support with the steel. We can do whatever it takes, but we need to increase the throughput and the availability of transformers for the supply chain, mainly in USA transformers and, hopefully, with the union workers. That's what we are working on, and we believe we're going to be successful.

Phil Gibbs
Thank you so much.

Lourenco Goncalves
Thank you.

Operator
Our next question is from the line of Alex Hacking with Citi. Please proceed with your questions.

Alex Hacking
Yeah, morning Lourenco and Celso. Just coming back to the DOE awards. It sounds like the negotiations there are somewhat of a formality, and you're very confident that that money will be awarded. Is that assumption, am I correct in that assumption? And then what would be the timing there, the expected timing of when those awards would be confirmed? Thank you.

Lourenco Goncalves
Good morning, Alex. I don't believe it's a formality because they are asking a lot of good questions, and we are providing with what we believe a lot of good answers. And the timeframe for the negotiation or the discussions over whatever you call, is basically, we are going to use the rest of this year to finalize this negotiation.

But we are fairly confident that we're going to be successful. But I don't think it's a formality. I believe that they are doing a good job. They are doing the due diligence that they need to do. At the end of the day, they are going to be giving us $575 million, $500 million for Middletown and $75 million for Butler. So, it's a lot of money, and it's at the end of the day, tax payer’s money, and we take this very seriously.

But it's not a formality. We are doing the work. And in the process, the most important part that in the process, we are having the ability to educate the government on what we do, instead of having them only reading what is in the trade press or in the report from research analysts, they are learning from the ones that really know what they're talking about.

Alex Hacking
Okay. Thanks.

Lourenco Goncalves
Yeah, that includes you in the crowd that don't know what you're talking about. You're right about that. But that's just me, you know me, Alex. So yes, what's next?

Alex Hacking
What's next? Let's say the money wasn't awarded. It sounds like for whatever reason, it sounds like the economics of the electric melt furnace would be compelling, even without the award. But is that a project that you would still move ahead with in that circumstance? Or you can't really say it, until you reach that point?

Lourenco Goncalves
Alex, I'm very confident that I will get the money. And we, of course, will run the projections with and without. But with the money coming from the DOE, it's a no-brainer. It's a very, very compelling case of return on investment, it's money well spent. It's a real game changer. We are going to be reducing our costs to produce the same ton of liquid steel by more than $250 per ton. That's super significant, so we want that project.

And, yes, the ROI without the grant is still okay, but the ROI with the grant is unbelievable. And I believe that so far, based on what Cleveland-Cliffs is doing in terms of, among other things, working together with the government and working together with our workforce, we deserve to get the money.

Alex Hacking
And I guess just finally, I mean, you mentioned that the $250 number, earlier. I mean, is that really like the direct savings from shifting the technology because that would, obviously, provide a massive uplift, right, in EBITDA per ton.

Lourenco Goncalves Exactly right.

Alex Hacking
An apples to apples comparison.

Lourenco Goncalves
Exactly right. Because I'm a metallurgist, I like technology. It would be so easy to shut down blast furnaces and BOFs and put EAFs and not be able to produce all kinds of steel that are produced today and producing massive unemployment. Europe is doing that. The UK is doing that. When I was--when I had a conversation with then Minister of the Economy of Slovakia, he said that there was £600 million granted money for Kosice just to shut down the blast furnace and replace with the EAFs.

And I said, do you know that two-thirds of your personnel will be let go? He said yes, unfortunately, that's the consequence of decarbonizing. I said, Mr. Minister, you don't know what you're talking about, with all due respect. So, we've got to see the big picture. We've got to understand where cost is.

If you believe that cost is saving, saving by cutting 20 bucks per ton today and 30 bucks per ton tomorrow, you end up with what we created here in the United States. And then you decimate a steel industry that was the envy of the world, four years ago, and you create China, and then you realize that China is an enemy to be beaten.

And yes, so we got to see the big picture, and it takes a lot of education and a lot of technology and a lot of engineering to do things the way we are doing here at Cleveland-Cliffs. We are very happy that we found a willing counterpart in several cabinet members of the Biden Administration, and we are happy with that.

Alex Hacking
Okay. Thanks. Best of luck.

Celso Goncalves
Thank you. Same to you.

Operator
Thank you. Our next question is from the line of Tristan Gresser with BNP Parabas. Please proceed with your question.

Tristan Gresser
Yes. Hi, good morning and thank you for taking my questions. Just maybe a follow-up on the decarbonization project. Can you please maybe split the gross CapEx elements of the project in Middletown and give us a sense on, not on a net CapEx basis, but on a gross basis, what the normalized CapEx would look like 2024, 2025, 2026, 2027. Would it be close to 1.2 billion? That's my first question.

Lourenco Goncalves
Yeah, I'll let Celso take that. Celso, please.

Celso Goncalves
Yeah, sure. Hey, Tristan. Like I said, there's no impact to CapEx from these DOE projects in 2024, just to be abundantly clear, everything starts in 2025. And if you want to break that down, in 2025, the Cliffs portion of the Middletown spend is about $250 million. And the total CapEx related to everything is about $985 million.

So, that's why I said in '25, we don't even crack above the $1 billion market. And then when you go to '26, Middletown steps up to about $400 million and the total goes to about $1.2 million. So, that's the breakdown for the next couple of years.

Tristan Gresser
All right. That's helpful. And that's a net number, right, the $1.2 billion, so removing the reline and the grant.

Celso Goncalves
Correct, yeah.

Tristan Gresser
All right. And then the second question, should we think as Middletown project as the way forward for the rest of the footprint, given the carbon benefits you mentioned that can translate into selling premiums, but also the cost benefits?

I think you mentioned in the past that there was a next reline at Burns Harbor in 2026. So, basically, does it make sense to gradually convert your BF footprint to this kind of, this DRI melting unit setups. And if that's the case, would more funding be available, should you decide to go this way?

Lourenco Goncalves
Yeah, it's a very good question. But let's go, piece by piece, on where my cost savings are, the numbers that I just gave to you. The biggest problem for us in Middletown is our very punitive contract that we have with SunCoke. That contract is absolutely horrible. And our cost of coke in Middletown is one of the reasons why we started studying this project, in the first place. So, that situation is going to change, no matter what. We are not going to be keeping ourselves penalized by SunCoke with that horrible contract that we have.

So, for Middletown, the numbers are the numbers I mentioned to you. And we are going to go in that direction coming hell or high water. I'm going to get the grant. But the project there is our response to the contract we have with SunCoke.

When we go to a company like--to a plant like, for example, Burns Harbor, the switch is not as clear as that because we have been improving a lot our ability to produce coke at a reasonable cost. Burns Harbor is because of that--among other things, but because of that, mainly, it's our lowest cost production plant in the entire footprint. So, I don't see us going to Burns Harbor, so quickly.

But of course, the new configuration that we are implementing in Middletown will be our first in the company, like we did with our plant, our direct reduction plant in Toledo.

And with that, we were able to now easily go to Middletown with a new direct reduction plant because we know we dominate the technology. So, it's a first. I don't know, if we are going to continue in that route but there's a possibility, and we have our priorities in terms of who would be next and who will be next, if that's the case.

Tristan Gresser
All right. That's very clear. Maybe one final question. Maybe if you can discuss a little bit the situation at Calvert, you have a slab supply agreement. The facility there is ramping up its upstream, could go with the second year. So, I think the contract is up for renewal next year, but what are the solution if, let's say, well, Calvert decide, well, to go with upstream or some other slab supply? Do you have options? Is that already a topic of discussion or negotiation? So if you could share some thoughts on that, that would be helpful.

Lourenco Goncalves
Yeah, the negotiation has just started. And of course, I'm not going to give you--I can't give you details of how the negotiation is going, but I will tell you what the outcome will be. We will end up with a much better contract for us, or no contract. Either one is good for Cleveland-Cliffs. No contract is good, and a better contract might be good. The contract we have was the last piece of the puzzle for us to close the deal and acquire ArcelorMittal USA, and that was in December of 2020, we closed.

So that negotiation happened September 2020. So that was almost four years ago. I knew exactly where I was walking us into. And now it's the time of expiration. And it's like any situation with the contract. We prepared Cleveland-Cliffs to be without that contract, we're going to be okay.

And if that contract improves, we still can work with our friends at ArcelorMittal. Otherwise, we continue to be friends, but they'll have to find slab somewhere else. That's the deal.

Tristan Gresser
All right. Thank you very much.

Lourenco Goncalves
Thank you.

Operator
Our next question is from the line of Lawson Winder with Bank of America. Please proceed with your questions.

Lawson Winder
Thanks very much, Operator, and also good morning Celso and Lourenco. Thank you for taking my question. I would like to ask about the NOES expansion at Zanesville. Has that started to ship to customers? And how is that ramping up?

Lourenco Goncalves
The NOES expansion in Zanesville is in operation and mission accomplished. We always believed that we would have more use for non-oriented electrical steels, particularly for motors of

electrical vehicles. And we created a modest increase in our capacity by investing a relatively small amount of money in CapEx. So we're good.

The project was executed as planned. We are selling oriented electrical steels. We continue to develop applications with our, mainly with our automotive clients, and we are fine with that and we have no intention to expand beyond what we already have for NOES.

Lawson Winder
Okay. Thank you for that. And can I also ask about the base price that you set at $900 per short ton. So, I mean the price reporters are still indicating prices in the lower 800s. Are you guys realizing pricing in that $900 per short ton range? And what's your thinking on pricing, over the next month or two?

Lourenco Goncalves
I never give public predictions on price. We announced our price increase, and we are working to get that price increase. We are not on an island. In the meantime, that we announced our price increase, and everything was actually going in the right direction. We're still selling for $900, for that matter; we are. So the answer to your question is yes. But other clients--I'm sorry, other clients--other competitors came with different price points.

And we live in a world of pricing competition, particularly in a world that everybody reads every single line that comes out of the trade press. And you just said what would you like to hit. So, the prices are $800 and low $800s. Yeah, they will take that to the--like the Bible. But I'm telling you, we're selling for $900. But is that easy right now to get there? No. It was easier before things that happened during the latter part of the quarter. But these are always--it's an always changing environment.

And at the end of the day, we will see what's going to happen. And we expect to sell more, particularly for service centers that are completely depleted in terms of inventory because not buying seems to be the only diet that they can do when they want to lose weight on their inventory. I suggest Mounjaro or Ozempic, that would be a lot more effective. All right. With that, I think we're done, right, Rob?

Operator
Yes, that's correct. Would you like to make some closing comments?

Lourenco Goncalves
Done. Mounjaro, Ozempic. You'll lose weight with that and pair with exercise. But as far as inventory, service centers are supposed to carry inventory. For a service center, you don't carry inventory, you are setting yourself up for a disgrace. So, but be my guest. Good luck.

Thank you, everybody. I'll talk to you soon. Bye now.

Operator
Thank you, everyone, for joining us, today. This will conclude today's call. You may disconnect your lines at this time, and thank you for your participation.