Cleveland-Cliffs, Inc.
Second Quarter 2022 Earnings Conference Call
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Presenters
Lourenco Goncalves - CEO
Celso Goncalves - CFO

Q&A Participants
Curt Woodworth - Credit Suisse
Lucas Pipes - B. Riley Securities
Michael Glick - JPMorgan
Emily Chieng - Goldman Sachs
Timna Tanners - Wolfe Research
Seth Rosenfeld - BNP Paribas
Carlos De Alba - Morgan Stanley
Karl Blunden - Goldman Sachs

Operator

Good morning, ladies and gentlemen. My name is Kevin, and I am your conference facilitator, today. I would like to welcome everyone to Cleveland-Cliffs Second Quarter 2022 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 protection 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 releases filed with the SEC, which are available on the company 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 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 this morning.

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

Celso Goncalves
Good morning, everyone. Our second quarter marked the continued execution of our key capital allocation objectives, including the largest free cash flow-driven debt reduction in company history.

During the quarter, we generated $633 million in free cash flow on $1.1 billion of adjusted EBITDA. This cash generation in Q2 is more than double of what we generated in Q1, even after paying around $300 million of cash taxes in the second quarter.

Consistent with our stated priorities, we used this cash to aggressively pay down debt and opportunistically buy back stock.

During the quarter, we fully redeemed the remaining $607 million of our most expensive secured notes, well in advance of its maturity, and took advantage of volatility in the debt markets to attack other tranches of bonds in the open market, repurchasing another $307 million in principal outstanding notes at an average discount of 8% to par.

These repurchases focused on our 2029 and 2031 guaranteed unsecured bonds, as well as our 2026 secured notes.

On the revenue front, our volumes and selling prices were both up sequentially from Q1 to Q2, leading to a record quarterly sales revenue of $6.3 billion.

Our Q2 steel selling price averaged $1,487 per net ton, representing an over $40 quarter-over-quarter increase, primarily driven by substantially higher slab prices sold to other steel mills and favorable April fixed price sales contract renewals, as well as continued robust spreads for cold rolled, coated and plate products sold on an index basis.

Looking ahead, in the third quarter, although pricing will likely be impacted by falling commodity index prices, lower spot prices will be heavily mitigated by our industry-leading use of fixed price contractual arrangements.

Our next round of fixed price contract resets will occur on October 1, with roughly 1.7 million annualized tons up for renewal.

Given our unique product offering and technical capabilities, we expect to see continued substantial increases in fixed contract prices in this upcoming renewal, even with the recent downtrend in commodity steel prices, as a backdrop.

From an operating standpoint, our Q2 adjusted EBITDA was down sequentially quarter-over-quarter, primarily due to the increased costs that we foreshadowed on our last earnings call.

With over $200 million MMBTUs of annual consumption, Cleveland-Cliffs is one of the largest direct consumers of natural gas in the U.S. Even though we're meaningfully hedged at all times, we still experienced a substantial impact from elevated natural gas prices, throughout the entire quarter.

Other rising input costs included electricity, scrap and alloys, as well as higher repair and maintenance spending. Cost increase was also driven by higher idle costs, up nearly $200 million from Q1, which was driven in large part by the expanded scope of the outage at our Cleveland Works facility.

Along with the reline of blast furnace # 5 in Cleveland, which is generally only done once every 20 years, we took advantage of the downtime to perform other important repairs and maintenance in related areas of Cleveland Works, including the wastewater treatment plant and the onsite powerhouse.

With the additional work being done, we now plan to have Cleveland Works back at full capacity in August, aligning with improved automotive steel demand.

With the bulk of the work behind us, we expect our excess and idle costs to decline, meaningfully, in the third quarter.

In terms of working capital, while our gross inventory values increased as a result of higher cost during Q2, our total steel inventory volumes were actually reduced by 230,000 tons in the second quarter and has declined about 400,000 tons, so far this year.

As costs for several of our primary inputs have declined recently since the end of Q2, and with Cleveland Works back in full operation in Q3, we expect working capital to be a meaningful source of cash in the second half of the year.

Even with the current lower price of commodity grade steel in the market, we expect to continue generating strong free cash flow for the remainder of the year. There are several factors that will continue to support our cash generation going forward, under the current environment.

One, the fixed price nature of nearly half of our order book will keep our average selling price elevated, despite lower spot prices.

Two, fixed price contract resets occurring on October first are going up, not down.

Three, lower operating, repair and maintenance and idle costs going forward.

Four, the expected release of working capital that we have built up over the past 18 months.

And five, lower CapEx spending, as we have no major capital projects on the horizon for the foreseeable future.

This will all allow for continued robust free cash flow generation, opportunistic share buybacks and aggressive debt reduction.

With net debt well below one time our last 12 months adjusted EBITDA, we continue to be focused on maintaining conservative leverage levels going forward.

With that, I'll now turn the call over to our CEO, Lourenco Goncalves.

Lourenco Goncalves
Thank you, Celso, and good morning, everyone. Cleveland-Cliffs became a steel company on March 13, 2020, the day we completed our acquisition of AK Steel.

Two of our favorite things about AK Steel were its industry-leading weighting toward the automotive end market and its leading capabilities in research and development. Automotive not only consumes a lot of highly customized flat-rolled steel, but also demand the strict specifications and a long approval process to qualify material.

There is no such a thing as commodity steel in automotive. That's true in Europe, in Japan, in South Korea and, obviously, here in the United States, as well.

That being said, the supplier base of steel to automotive clients everywhere in the entire world is limited to a few steel companies really able to support all the specs the car manufacturers need, usually one per country or geographic region.

That background aside, within a week of the completion of our AK Steel acquisition in March of 2020, the entire automotive production ecosystem shut down for the first time ever in its century-plus long history.

After a three-month long interruption, automotive production began to resume, but not nearly to the levels we had seen for the prior decade, despite a very strong demand for cars associated with the restrictions imposed by COVID-19.

While the automotive sector was slowly coming back to life, we acquired ArcelorMittal USA. They are the major steel player in the automotive space, making Cleveland-Cliffs, the largest supplier of automotive steel in North America, by a very wide margin.

Next, our wave of supply chain issues began to hit the sector with widespread shortage of microchips being the most visible problem. That reversed the initial pace of recovery and have hampered automotive production to this day.

In the six years leading up to 2020, North American light vehicle production averaged more than 17 million units, per year.

Comparably, in the past two years, the industry has only produced 13 million units per year, a 24% decline at a time when consumer's demand for cars was growing.

During this time period, other steel consuming markets have grown-most notably construction, and we have benefit from that, as evidenced by our record earnings results in 2021. That said, our mini-mill peers are much more leveraged to the construction market than we are, and they have benefitted from that more than we have, particularly, in their downstream businesses.

This is now about to change. As we read through the current economic conditions in the country, which include 40-year high inflation levels and rising interest rates, yet consistently low unemployment, we have all the ingredients for the dynamics of the past two years to shift in our favor.

It has been over two years of construction outpacing automotive, but that's no longer the case.

The North American automotive industry could have produced 8 million to 10 million more vehicles than they actually did, over the past two years. And as a result, a relentlessly growing pent-up demand for cars, trucks and SUVs have developed.

The best indicator of this trend is the manheim used car price index, which has nearly doubled in that time period and remains near all-time highs. On top of that, the average age of a light vehicle on the road in the U.S. has grown to 12.2 years, the highest it has ever been.

Also very importantly, the unemployment rate has remained low at 3.6%, about the lowest it has been in 53 years. This means that individuals not only have the income to buy a new car but, in most cases, they also need that car to commute to work.

A car is not a house and a loan to buy a car is less sensitive to interest rates than that of a mortgage. If you have a paycheck, you can buy or lease a car and make the monthly payments.

Unless the fight against inflation leads into high levels of unemployment, every car that can be produced over the next several years has a buyer. It's just a matter of having the materials needed to produce the cars.

The most prevalent material in a car is steel, which makes up roughly half the weight of the vehicle.

Over the past two years, we at Cleveland-Cliffs have made the investments necessary to meet this coming onslaught of demand and we are ready with the most advanced technical capabilities the industry can offer, including a brand-new blast furnace at our Cleveland Works operation.

All of our automotive customers have indicated to us that their supply chain issues are easing, and we are seeing tangible proof of this through our own channel checks. The production pace of the first half of this year has been nowhere near its full potential, let alone the prior decade average.

Starting in the second half of 2022, we expect to get more automotive volume and with more volume and base load for our mills, our costs should naturally improve.

The income volume improvement comes from both, internal combustion engine vehicles and electric vehicles. We are not only the largest supplier of steel to the automotive sector, but we're also the largest supplier of each one of the individual car manufacturers currently transitioning from ICE vehicles to EVs.

Higher fuel prices have only increased the consumers' appetite for EVs. If you, as an investor, believes in this EV transition, Cleveland-Cliffs is who you need to deal with. That's not just because of the long-standing quality products we have, historically, supplied for ICE vehicles, but also because our broad offerings of advanced high-strength steels is the perfect solution for battery-powered EVs.

In addition, we are the only domestic producer of non-oriented electric steel in the United States, where roughly 150 pounds are required, per vehicle, for using the motor. Because of the growing demand of these steels, we are investing $30 million in our Zanesville, Ohio, facility, a small investment to allow us to add another 70,000 tons of production of non-oriented electrical steels, NOES, effectively doubling our NOES capacity without impacting our industry-leading capability on gross grain-oriented electrical steels.

With that, we will also be generating another 100 good paying middle-class union jobs at Zanesville, when this addition comes online in 2023.

Going forward, these are the types of low dollar, high-impact capital projects we will be focused on. That's a clear differentiation between Cleveland-Cliffs and other companies in our space.

In their multiyear commitments to massive CapEx, each one of these other companies has announced several billions of dollars to build new mills--steel mills and even aluminum mills. Cleveland-Cliffs did not and will not announce any of these mega investments.

When we acquired ArcelorMittal USA and based on our experience immediately after we acquired AK Steel, we knew we would have to spend significant money to bring its assets to our own higher standards.

That has been done and done very well. By now, we have all the equipment and technology in place to meet the needs of our most demanding customers in automotive and other sectors. Actually, our capital spending in 2023 should decline, when compared to 2022.

Our last big capital project was the Cleveland Works revamp, and we do not have any other capital project of this magnitude, until at least 2025.

Outside of automotive, it's clear that destocking activity is underway at service centers. And they simply, will let their inventories go very low. Other steel consuming sectors have peaked for now, but automotive has not. A significant 45% of our sales are on fixed prices, and those prices are not directly correlated with the latest market prices.

We have the leading market share in automotive, not because of price but rather, because of our technical capabilities and ability to deliver on time.

This is why we expect more price increases in our upcoming renewal cycle, where we can get closer to a proper value for the full service and solution package we provide the automotive industry.

These fixed prices will keep our cash flow strong through the rest of the year, along with the release of, at least, a portion of the $2 billion in working capital we have built, over the past 18 months. This working capital release should come not just from lower input costs, but also from our own proactive management of raw materials.

For example, we are now extending the ongoing idle at our Northshore swing facility to, at least, April of next year. With the increased use of scrap company-wide in our steelmaking operations made possible by the acquisition of FPT last year, the pellets from Northshore are not needed at this time.

Rather than deplete this finite resource for the benefit of the Mesabi Trust and its so-called unitholders, we will keep Northshore idle until we decide, otherwise.

On a final note, we have begun our union negotiation with United Steel Workers to renew our current labor agreement. The agreement expires September 1st, and it covers approximately half of our company-wide workforce. We have always valued the relationship with our unions and made it clear that we appreciate working together with them.

Differently from others in our industry, we remain committed to our existing plant sites and to our unionized workforce. With all that, we expect the negotiation process to result in a fair and equitable agreement for both parties.

Cleveland-Cliffs is about more than just making steel. Our mission is deeper; to revitalize manufacturing in the United States and through that, support and enable a vibrant American middle class.

We are not a steel company of the past. We are the present and the future of our industry, and we have the right people, equipment and capabilities to prove that out, going forward.

I will now turn it back to the operator for Q&A.

Operator
Thank you. We'll now be conducting a question-and-answer session. If you'd like to be placed in the question queue, please press "*", "1" on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press "*", "2" if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset, before pressing the start keys.

One moment, please, while we pull for questions.

Our first question is coming from Curt Woodworth from Credit Suisse. Your line is now live.

Curt Woodworth
Yeah, thanks. Good morning, Lourenco and Celso. First question, just with respect to cost progression, going forward. You outlined a $200 million of costs for Cleveland this quarter, and it seems like the remaining $42 million was more on the energy side.

So, would you expect to get most of that $200 million back? And does that $200 million also include the implied loss of volume as well from the facility in the third quarter?

Lourenco Goncalves
Look, I'll give you a generic idea on the answer and then I'll let Celso handle the specifics, okay, Curt. We acquired assets, particularly, the set of assets came from ArcelorMittal that were not in great shape.

We knew that, coming in. That's why we paid a price that was much lower than the actual value of the assets. So, I'm sure you recognize that. So it's not like we did not know what was coming. So, this being said, all these big costs are behind us. Cleveland was the last one.

And when we shut down the blast plants, we saw the opportunity due to a market that was less than ideal, let's call it like that, to do things that are overdue like the powerhouse and the water

treatment we have at the Cuyahoga River and pretty close to Lake Erie. So, we need to be very careful with these things, and we take our environmental commitment very seriously, as you know.

But these are onetime things that don't happen, often. Like I said, our next big deal might come in 2025. Between now and then, we have nothing. Anyway, Celso, please go ahead and complement to the point that Curt was asking.

Celso Goncalves
No, I think you covered it. I mean when you shut down a facility like Cleveland, you have the opportunity to fix everything. So, we took advantage of that in Q2, and the fact that automotive has been slower here to start the year has given us time to catch up on maintenance. As you stated, the facilities we acquired needed to be brought up to our standard.

And then--so on top of that, we had some inflationary pressures like natural gas, as we all know, electricity, scrap and alloys. Those all spiked during the quarter but have since come down.

But I'd say that the biggest cost impacts are now behind us. You might have some flow-through in inventory in Q3, but we don't have any more of these major outages like Cleveland, until 2025.

Curt Woodworth
So, would you expect to recoup most of the $200 million this quarter? I'm just trying to kind of get a little bit more color on unit cost progression into the quarter.

Lourenco Goncalves
Yeah, this cost will run through inventory in Q3, if that's your question.

Curt Woodworth
Okay. And then maybe just on a couple of cash flow item questions. Could you--if we assume that fuel pricing stays roughly where it is, even though the forward curve has actually shifted back into contango, what would you expect for working capital release in the back half of the year?

And then if you can give us updates on your estimates for CapEx this year, next year, as well as cash taxes for this year?

Lourenco Goncalves
Yeah, I'll do the CapEx. Celso will do the working capital. CapEx next year will be no more than $800 million. And that should be a good guidance, going forward. So, we are not going to starve our mills for CapEx, like others did before. The Goncalves way is different.

We do maintenance. And we take care of our equipment, instead of being concerned about the specific quarter. We did what we had to do in Q2, period, full stop, that's good management.

Going forward, we are not going to do big CapEx things because we don't need any more, we already did. So, if you need a number, Curt, and I know you do to plug in your model, I would plug an 8-handle type--800 handle type of number for CapEx, something between $800--$850 million on a going forward basis. That's those for CapEx. Working capital, Celso, please.

Celso Goncalves
Yeah. In terms of working capital, we've built a lot of working capital since we acquired AM USA, and that's now starting to reverse. So, working capital is going to provide a tail, even as pricing falls. Receivables, for example, will accelerate. Q2 was probably the peak, in terms of inventory cost. We're replacing higher cost now with lower cost inventory.

So, this is all going to support healthy free cash flow generation going forward from this release of working capital.

Curt Woodworth
Okay. Thanks very much.

Lourenco Goncalves
Thank you, Curt.

Operator
Thank you. Our next question is coming from Lucas Pipes from B. Riley Securities. Your line is now live.

Lucas Pipes
Thank you very much, and good morning, everyone.

Lourenco Goncalves
Hi, Lucas.

Lucas Pipes
Lourenco, I believe in your prepared remarks, you commented on automotive volumes being up. And I wondered if you can maybe put some numbers around that for Q3 and Q4. And then also on total volumes, what you think might be a good ballpark for the remainder of the year. Thank you very much.

Lourenco Goncalves
I can't put out a number. Very bluntly, it's very difficult at this point to narrow down to a number. But I can see trends. The orders are starting to come more consistently. The--

unexpected shutdowns are gone. The announcements of new EVs from the likes of our clients, each one of them, you pick one, and we are there.

We are the biggest supplier of the one that you pick, are consistent with what they are ordering in terms of steel. There's a lot of development in the background in our R&D department to advance the high strength steels for enclosures of battery for EVs, as well as specification of materials for the skins and the structure of these same EVs.

So, things are really moving back where they should move. One short term indication is also that there's a big trend right now of car manufacturers being kind of--the reality sinking in, in Europe. It's clear that all this speak of the Europeans is just that, speech.

They don't have natural gas even to heat their houses. So, we are starting to see reallocation of microchips and other things from Europe to the United States. And we're also seeing the growth in orders, as a consequence of that. So, even though I'm not giving you a number, Lucas, I'm giving you a lot of good indications that things are starting to turn, and we are ready for that.

Lucas Pipes
That's very good to hear. Thank you for that color. Lourenco, it was great to hear that the October pricing is going to be up. And I--I'm sure there are a lot of different components to this negotiation and resetting these prices. But when I think back to late last summer pricing were at the record highs.

And so, you would think that led into the October pricing last year. So what's maybe the biggest factor, this year for the higher pricing reset? And can this carry forward into the Jan and April negotiations, as well?

Lourenco Goncalves
Because basically, Lucas, what people see on the spot price don't really bear a lot of contact points with what we are dealing on a daily basis with our car manufacturers. And by the way, pretty much also you talk about the automotive industry.

When I say that Cleveland-Cliffs is the largest, let me put numbers on that. Last year, we supplied 6.8 million tons of steel to the automotive industry and automotive industry produced 13 million cars. So 6.8 million is bigger than 6.5 million-that will be half.

So, we supply more than half of the steel that the automotive industry acquired. So, we are really affected by the automotive industry.

The results we have brought to this company since we built this company a couple of years ago are not short of a miracle, particularly, because we are going against the backdrop of our main markets that's not working properly. So, that's about to change, at this point.

So, they know that. They can't just try to negotiate the last penny in a moment that they are fighting for their own survival. They have one big competitor that came brand new to the sector and took over the electric vehicles chunk of the market. Now, they're playing catch up. I'm telling you they're playing catch up pretty fast, and we are helping them to play catch up.

And the price conversation exists, but it's not front and center when we are negotiating the bulk of their needs. Then they might for hot-rolled stuff that has less restrictions and things that's going in less critical parts of the car. They still have the ability to buy from others. But for the real deal, they buy from Cleveland-Cliffs. They know that. We know that. That's the negotiation that's going on.

Lucas Pipes
Great. Lourenco, really appreciate the color. Thank you very much. Best of luck. I'll turn it over for now.

Lourenco Goncalves
Thanks, Lucas.

Operator
Thank you. Your next question today is coming from Michael Glick from JPMorgan. Your line is now live.

Michael Glick
Hey, good morning. The market's obviously focused heavily on demand, right now. I mean, I guess, beyond auto, could you just talk about how the order book has been shaping up in recent weeks? And have you seen any pockets of weakness in demand in any of your non-automotive end markets?

Lourenco Goncalves
Yeah. Look, automotive is different. And I think I have spoken enough about automotive, at this time. So, let's move to the other sectors. Service centers, service centers like always, they are still in the destocking mode. So, it's not really bad, but it's opportunistic. It's just what they need.

Destocking has an end game. You end up with a low stock. So it's coming soon. And when the stock is really low, what they do next, they buy. So, my optimism for the latter part of Q3 is big like the other companies that preannounced said the same thing. So, that's service centers.

As far as manufacturing, that is a big broad sector, when we say manufacturing. There are parts of manufacturer that has red hot and buy a lot, and we will supply some of them. And there are others parts of the manufacturing spectrum that are much lower, particularly, things that are related to construction.

So, we are not a major player by any stretch, but we are starting to see things slowing down in construction.

So, it's a mixed bag. The good thing for us, Michael, is that automotive has less to do with recession and a lot more to do with employment.

Assuming that we don't go into a deep recession and we still keep employment at decent levels, even if unemployment increased a little bit, we still have enough middle-class type of buyers and above to continue to buy the cars they want.

You continue to see people that are really upset with higher fuel prices to try to move and buy their first electric vehicle. And these are all things that will benefit Cliffs, going forward.

So, I really encourage you to look going forward, instead of just looking right now at what you see in the results or the press or the negativity or the political football.

The fact of the matter that we are, at this point in the United States, in a moment of people really considering buying cars. If the cars are made available, you are going to see a wave of acquisitions of cars that's unprecedented. But the cars need to be available. It looks like they are becoming available.

Michael Glick
Understood. And maybe as we think about the balance sheet, how should we think about your net or maybe even absolute debt target in this environment?

Lourenco Goncalves
Look, I think we got to what we have to get. We are consistently below one time EBITDA. And we will continue to manage down this debt with cash flow. It's our--clearly, our main priority to continue to knock down debt. I don't know if you know, but $6.3 billion in revenues is a record quarter.

And our conversion to free cash flow was also outstanding. And we put the vast majority of the cash generated to pay down debt. We started to buy stock until the silly season started, and then we stopped buying stock and then we focus only on that.

We will continue to focus on that. Like Celso said, we're going to be very focused on paying down debt, as always. And we'll buy stock, if the opportunities arise. But I really believe that, at this point, my opportunities to buy stock, we will start to be verified. We want to be really focused on that.

Michael Glick`
Understood. Thank you very much.

Lourenco Goncalves
Thank you.

Operator
Thank you. The next question is coming from Emily Chieng from Goldman Sachs. Your line is now live.

Emily Chieng
Good morning, Lourenco and Celso, thanks for the update, this morning. My first question is just around the asset portfolio and following the closure of Indiana Harbor 4. And I know you did mention this in your prepared remarks, ongoing commitment to each of your assets.

But just to reconfirm, do you feel that the size of your portfolio is rightsized at this point with your assets now running more efficiently than they were before?

Lourenco Goncalves
Yeah, look, good morning, Emily. Look, first and foremost, the shutdown of Indiana Harbor 4 was driven by our commitment to reduce our carbon footprint. We can only do that because Indiana Harbor 7 is a massive consumer of HBI.

And we use much lower coke rate over there. We generate a lot less CO2, per ton of steel produced. And we are able to serve the entire Indiana Harbor complex plus Riverdale, just operating the Indiana Harbor 7 furnace. That's also because we melt a lot of scrap in Indiana Harbor and Riverdale. So ,that's basically adapting the hot end to the size of the market that has been there, and we will be there in the future and doing that in the most environmentally friendly way.

So, I believe that we are pretty optimized, at this point. We don't have any intentions to reduce our footprint or grow our footprint. That's the footprint to have. Gains will be margin like the one I just announced, this investment in Zanesville, just a $30 million investment to bring back a Zanesville mill to produce more NOES, non-oriented electrical steel. That's the one that goes on the engines of the electric vehicles.

So, we are doing that in Zanesville. So we are not doing that, we are preserving our ability to continue to produce growth in Butler because the market for transformers is also fantastic. So, these are markets that are extremely hot right now, and we're the sole supplier of this type of steels, electrical steels. So, we're good.

Emily Chieng
Great. That's very clear. And a follow up is just around gas and energy and electricity cost there. But this is clearly being elevated in the second quarter. How do you see that trending in the

third quarter? And maybe if you could share how you think about sort of the hedging program in place and what sort of spot exposures you might have there?

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

Celso Goncalves
Yeah, hey, Emily. So gas prices, I think, reached like a 14-year high, and they stayed at those levels throughout the entire--the three months during the quarter. So the Q2, I think market price for gas average was like $7.50 per MMBTU, compared to less than $5 in Q1.

We've seen those prices come down here in Q3. So that's a benefit to us. As I stated, we consume 200 million MMBTU across our footprint, per year. Our philosophy is to remain 50% hedged at all times.

So, if you look forward to the back half of this year, we're already 50% hedged at much lower levels than spot. We're not trying to speculate on price. We're not trying to make money off of hedging. We just want to kind of mute the impact of these swings in volatility.

So, that's kind of how we look at it. And then we're exposed on the other half, but at least we're mitigated on the half that we're hedged.

Emily Chieng
Right, thanks, Celso.

Lourenco Goncalves
Thanks, Emily.

Operator
Thank you. Our next question is coming from Timna Tanners from Wolfe Research. Your line is now live.

Timna Tanners
Hey, good morning.

Lourenco Goncalves
Good morning, Timna.

Timna Tanners
Good morning. I wanted to dial down a little bit more, if I could, on your utilization and your volume outlook for the second half. I know in the past, you had said that to get above 4-million-ton shipments per quarter, you need auto to come back.

So, with the restart of Cleveland, could we be at that run rate by the end of the year and into next year? And with Cleveland, do you also see a bit of continued outage costs, until those roll off into the fourth quarter?

Lourenco Goncalves
Yeah, the answer to the first question is yes. We are--one of the reasons why we revamped Cleveland Number 5 is automotive demand. We are seeing the demand shaping up. And Cleveland Works is one of--is the one, the flagship facility in the country to produce high strains of steels for structural portions of the vehicle.

So--and some exposed, as well. But we have other locations that are more dedicated to exposed parts. So automotive, volume, yes, 4 million tons, yes. What was the rest of the--utilization on these things are we don't deal with this thing.

These are our statistics, things that they are new to do with operational metrics. But volume, absolutely, you're absolutely right, and the 4 million tons is target. But I kind of missed the one portion of your--

Timna Tanners
--Oh, yeah, just the lingering outage cost, given you're talking about an August restart, so assumably perhaps some lingering inefficiencies into July, I guess?

Lourenco Goncalves
Yeah, we're going to have some. Celso may be able to give you a little more color, but the book has been gone through the tank. So I don't know if you –

Celso Goncalves
Yeah, it will be back up and running in August.

Lourenco Goncalves
No, but she's saying some of the lingering impact of the numbers flowing through to the quarter.

Celso Goncalves
Yeah, it will flow through here in Q3, but the biggest cost impacts are behind us.

Timna Tanners
Okay. Helpful. And if I could follow-up. I know last quarter, you talked a lot about the benefit of having your own raw materials. And I just love to get your perspective on kind of how quickly that prime scrap price seemed to have faded.

I mean, do you expect that that's temporary and that it will still be tough to get prime grade material and alternative iron units, going forward and that that can be an advantage, as some of this excess buildup in material and the panic time has rolled off?

Lourenco Goncalves
Yeah. Look, we are seeing a lot less competition for prime scrap. Our ability to do closed loops with automotive continues to increase. At the beginning, we had to really fight to get the deals done. But now apparently, the competition is not really looking for a prime scrap. They should have their reasons. To be honest with you, I don't care. For us, prime scrap is important. We prefer to use prime scrap.

Prime scrap allows me to use less coke and using less coke, I generate less CO_2, and that's a good thing. And prime scrap that I use coming from automotive to go back to automotive in the steel that I produce is great to create a closed loop solution with our clients, and there's a value in that.

And this value is being translated in our ability to renegotiate higher prices and the price that we are currently in negotiations or already negotiated with our automotive clients. So, that's all positive. That's good.

Timna Tanners
Okay, great. Thanks for the update.

Lourenco Goncalves
Thanks, Timna.

Operator
Thank you. Our next question is coming from Seth Rosenfeld from BNP Paribas. Your line is now live.

Seth Rosenfeld
Good morning. Thanks for taking our questions. Just one final one, please, with the outlook for electrical steel, please. I'd love to hear a bit more about investment in Zanesville. Going to be very low CapEx for meaningful expansion of your non-oriented capacity.

Can you give a bit more color with regard to the expected EBITDA contribution and ramp-up time line of that? Also thinking about that facility, is there opportunity for additional kind of debottlenecking or low-cost expansion, looking forward?

Lourenco Goncalves
Yeah, good morning, Seth. Look, Zanesville, Ohio, is the--currently the location that finishes some types of electrical steels. So, that was a case use way of doing business. They

concentrated production Butler and between supporting Butler itself and another portion in Zanesville.

So, what we are doing with this investment, we are bringing back to operation, the main piece is the ArcelorMittal to produce the steel in Zanesville and a few auxiliary equipment to finish the steel produced at the mill to make then you're pretty much independent for this type of those specs.

So, Zanesville will become s producing facility by bringing back of units there, and it was idle for, I don't know how many years. When we acquired the K2 was already idled. So we're bringing it back.

That's why the investment is not big. We are not building a mill. We are basically bringing back to life a mill that was there, but it was not being utilized. So--and I gave you the investment, and I gave you the tons, $30 million for 70,000 tons. It's a pretty damn good relation.

The next thing that's going to happen, we are going--as the demand for electrical steels continues to grow, we are going to do something similar in Mansfield to—Mansfield is our facility that produces stainless steel. We continue to like and do well with stainless.

But we are seeing more and more demand for electrical steels, and we might be able--not might--we are able to alleviate Butler even more by creating electrical steels capabilities in Mansfield. But we are talking again, a small investment and a big return.

So, but we are not done with that part yet. So Zanesville is reality. Mansfield, we're set.

Seth Rosenfeld
Thank you. Just one follow-up on that front for Mansfield. If you were to expand more into electrical steel, would that come at the expense of lower stainless volumes?

Lourenco Goncalves
No, that's the key because doing that would be easy. We are--like we did in Zanesville, we are creating capacity without giving away anything. That's where the science is.

Seth Rosenfeld
Great. Thank you very much.

Lourenco Goncalves
Thank you.

Operator
Thank you. Your next question is coming from Carlos De Alba from Morgan Stanley. Your line is now live.

Carlos De Alba
Yeah. Good morning, gentlemen. So, we discussed the fact that your CapEx is going to remain around $800 million. And cash flow generation should be quite robust, even if prices continue to go lower. You will buy back maybe shares.

Your net debt is already quite low. What about dividends? Is that anywhere in your plans for the foreseeable future?

Lourenco Goncalves
Good morning, Carlos. Look, of course, it's in our radar. But it's not priority. It's not a priority. From the investor standpoint, if they really want dividend, there are other companies in our space, great companies, by the way, that offer a consistent dividend.

And they have stable business, but I strongly recommend dividend hungry investors to go to these companies. They are good companies. You're going to do well there.

On the other hand, if you want growth, and if you believe in the electric vehicle revolution that's coming--and I'm talking about the names that everybody knows, General Motors, Ford, Toyota, Nissan, Honda, it keeps going. I am the biggest supplier of each one of these names that I just mentioned, by a lot.

And what I'm telling you, they are going towards electric vehicles, take it at face value. They are going towards electric vehicles. And we are working with them to go towards that.

So, that's growth, and we will continue to grow and we will continue to generate cash, and we will continue to marginally—I say marginally because when we're down to onetime EBITDA, you were there, you got it. I appreciate you recognize that our debt is low, right now.

And we will continue to buy back stock because not for a second, I believe that investors, as a whole, will all of a sudden, all become big fans of Cleveland-Cliffs understanding everything we are doing. So, our stock price will continue to be mistreated by the market. That's where the opportunities are. That's how I built this powerhouse here in the last two years.

Think about it. Think about where we were two years ago and where we are, right now. So, think about where we're going to be in two years. Is that a dividend that put me there? No. It's execution day in and day out in the business, commercially, operations and in the financial side. We are good in all that. What else, Carlos?

Carlos De Alba
Yeah. The other question is regarding your end markets, given that this is something that is going to become increasingly important. In the second quarter, around 26% of your sales went into infrastructure and manufacturing.

Could you break this down? How much was infrastructure and how much was manufacturing given the comment that you made earlier on infrastructure is trying to maybe slow down a little bit?

Lourenco Goncalves
Yeah, look, primarily, manufacturing because infrastructure, particularly, to relate infrastructure to the infrastructure bill, this thing is not really sticky yet. Plate is infrastructure, and we are doing well with plate. And that's a part of the business that we really appreciate.

But it's pretty much what we had before and things that we are conquering in our dealings with our clients. It's not the infrastructure deal, yet. We believe that this will come but hasn't hit yet. So, it's basically manufacturing.

Carlos De Alba
All right. And then finally, if I can, and listen, just maybe to address a little bit of the elephants in the room on the story. So when you said that you are not going to make a major investment until at least 2025, so that potential electrical furnace that you were discussing in the last quarter is not going to come before that?

Lourenco Goncalves
No, no. We are done. We already revamped. Since I acquired AK Steel, we already revamped 1-2-3-4 blast furnaces--four blast furnaces in two years, we are done through at least 2025. So we are in great shape, as far as a big investment.

And just because you are mentioning big investments, I want to make abundantly clear, we have no intention to build—electrical plants in Middletown. But you are working to gather permits? Yes, I have permits to mine stock in Minnesota going through 2050.

So that's our long-term mindset. That's how I manage stuff. I've been doing that way my entire life. But there's no EAF coming at Middletown. We are good with the footprint that we have. We are probably the most environmentally friendly blast furnace operator in the entire world.

And when I say blast furnace operators, I'm saying a major supplier of automotive. Major supplier of automotive equals blast furnace operators.

Keep this in mind. Think about Japan, think about Europe, think about South Korea, think about the United States. When you get to the United States, you get to Cleveland-Cliffs.

Carlos De Alba
All right, excellent. Thank you very much. Good luck, gentlemen.

Lourenco Goncalves

Thanks, Carlos.

Celso Goncalves
Thank you.

Operator
Thank you. Next question is coming from Karl Blunden from Goldman Sachs. Your line is now live.

Karl Blunden
Hi, good morning. Good to see the progress on debt reduction and the limited CapEx needs going forward. Just to be a bit more granular on the debt reduction front. Should we continue to expect full redemption of the '26 secured this year? Just going back to your comments from the 4Q call.

Or when you look at the lower dollar price bonds like the unsecured, could that be a better use of cash for you? And I guess, finally, maybe you don't have to choose, you have enough cash flow based on what you've outlined to do both.

Celso Goncalves
Yeah, hey, Karl, good question. So, my goal is to take out those 6.75% secured notes due 2026 at the earliest. But when we saw that our 29s and 31s, which are our largest and most liquid and unsecured bonds, were trading at such a discount, we sort of redirected dollars towards that in the open market.

And we were really successful at picking those off in aggregate $300 million plus of those at a pretty good discount.

So, if we continue to see things like that, the strategy can shift because we get more bang for our buck targeting those. But absent those opportunities, our 2026 secured notes remain our main priority for full redemption.

Karl Blunden
Got you. That makes sense. And then just with regard to the other senior debt in the structure or secured debt in the structure, at least. When you think about the ABL and reducing that balance there, where does that come into the list of priorities? Do you anticipate, over time, getting that to be largely undrawn? Any comments there would be helpful.

Celso Goncalves
Yeah. So the ABL is still pretty cheap. So, we use that as liquidity. And we have other bonds that are more expensive and that are already callable. So, to the extent that those are available to be picked off, we'll continue to do that, especially, if it's at a discount.

And then, we also manage our liquidity to keep our liquidity at least at $2 billion. So, those are sort of the--all the levers that we play with. But absent other opportunities to pick off bonds in the open market, we'll just use cash towards lowering the ABL amount.

Karl Blunden
Thanks for clarifying. Appreciate the time.

Celso Goncalves
Thank you.

Lourenco Goncalves
Thank you, Karl. Appreciate it.

Operator
Thank you. We reached the end of our question-and-answer session. I'd like to turn the floor back over to management for any further or closing comments.

Lourenco Goncalves
Just appreciate the continued interest about our company and about our business. Please remember that I don't manage this company to get to the quarter results and tell only good news. Sometimes that will happen when I have to report maintenance, we're going to have to report the expenses.

Thanks, God, I haven't had to report any accidents because we take care of our equipment. So, we don't have that. So that's a very predictable and boring company, but it's a very predictable and boring company that continues to be seen ahead of the curve and around the corner.

So right now, it's not even that difficult to see around the corner. The future is in automotive, and automotive is electric vehicles, and we are working on that. It's pretty much the entire industry going toward that, and they're all buying from us. So, things are getting exciting here at Cleveland-Cliffs. We'll talk again in three months. Thanks a lot. Bye now.

Operator
Thank you. That does conclude today's teleconference and webcast. You may disconnect your line at this time. And have a wonderful day. We thank you for your participation today.