

**Cleveland Cliffs, Inc.**  
**Third Quarter 2022 Earnings Conference Call**  
**October 25, 2022**

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**Presenters**

**Lourenco Goncalves – Chairman, President and Chief Executive Officer**  
**Celso Goncalves – Executive Vice President and Chief Financial Officer**

**Q&A Participants**

**Lucas Pipes - B. Riley Securities**  
**Emily Chieng - Goldman Sachs**  
**Tristan Gresser - BNP Paribas**  
**Curt Woodworth - Credit Suisse**  
**Alex Hacking - Citi**  
**Carlos De Alba - Morgan Stanley**  
**Timna Tanners - Wolfe Research**

**Operator**

Good morning, ladies and gentlemen. My name is Maria and I'm your conference facilitator, today.

I'd like to welcome everyone to Cleveland-Cliffs Third 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 harbors 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 Form 10-K and 10-Q and news releases filed with SEC, which are available on the Company website.

Today's conference call is also available and being broadcast at [Clevelandcliffs.com](http://Clevelandcliffs.com). At the conclusion of the call, it will be archived on the website and available for replay. The company will also discuss the 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**

Thank you, Maria. And thanks to everyone for joining us, this morning. Before going through our Q3 results, let me start by highlighting the \$1.8 billion improvement to our balance sheet that was outlined in our earnings release, this morning.

During the quarter, we signed two new labor agreements covering approximately 14,000 USW-represented employees, encompassing more than half of our workforce. These agreements also cover benefits for over 22,000 retirees.

The ratification of these labor agreements triggered a remeasurement for the associated pension and OPEB plans, essentially requiring a refresh to all assumptions that go into calculating the value of those liabilities, including primarily, interest rates, asset returns and most importantly, the premiums that we pay for retiree healthcare expenses.

With interest rates higher this year and asset returns lower, those two first factors effectively offset each other. But the third factor, the updated healthcare premiums, resulted in a significant reduction to our overall liabilities.

Using our size and scale to our advantage, we were able to, proactively, renegotiate significantly lower premiums with our health insurance providers at much lower costs. All in all, these updates reduce our net pension and OPEB liabilities on our books by \$1.8 billion relative to the end of 2021, a 63% reduction.

Our pro forma net liability for pension and OPEB is now only \$1.1 billion, compared to \$2.9 billion at the end of 2021 and \$4.2 billion at the end of 2020, after we acquired ArcelorMittal U.S.A. In less than two years, we have reduced this liability, by over \$3 billion.

As you may recall, the pension and OPEB liabilities we assumed were, by far, the largest piece of the enterprise value of the AM U.S.A. acquisition. And now, most of those liabilities have moved over to equity on our balance sheet.

Going forward, these changes will also reduce our OPEB cash funding obligations by more than \$100 million per year, cutting this use of cash, by more than half.

Since the larger of the two labor agreements was not ratified until October 12, meaning after the end of Q3, the full impact of this change was not reflected on the actual 9/30 balance sheet. That's why we provided the pro forma calculation in our press release, this morning.

Furthermore, the impact of these renegotiated healthcare premiums is also applicable to other plans that will not be remeasured until December 31. As a result, when we report the Q4 and

year-end 2022 financials, we expect these liabilities to be even lower on the 12/31 balance sheet.

Also, to be clear, the benefit we have gotten just comes from reduced premiums from healthcare providers and does not reflect any reduced benefits for our retirees. This was truly a win-win for both the company and the union, and we thank the USW for their partnership to make it happen.

Now, moving on to our results. In Q3, we generated \$5.7 billion of revenues, \$452 million of adjusted EBITDA and \$288 million of free cash flow. On the revenue front, steel sales volumes of 3.6 million net tons held roughly steady with the prior two quarters, as lower demand from service centers and distributors was offset by higher automotive volumes.

Very importantly, Q3 of 2022 was our best shipment quarter to the automotive market, since the semiconductor shortage began. But it is still well below what we would consider normalized, compared with the period from 2014 to 2019.

Going forward in Q4, we expect total volumes to increase, as a result of further improved automotive, service center and slab demand.

On the pricing side, our sequentially lower average selling price was driven by the index-linked portion of our business with declines in the hot rolled, cold-rolled and slab indices. We also had declines in EBITDA for our third-party pellet and scrap businesses, as a result of lower pricing.

Looking into the fourth quarter, the improvements we achieved on the contractual fixed prices that reset in October will help to mitigate the lagged impact of continued falling index prices, but a product mix heavier in slabs and HRC will be a negative factor on our realized price.

Our adjusted EBITDA performance was also impacted by higher reported operating costs, which on a unit basis, trended upward in Q3, due to the lagged effects of higher cost inventory that we foreshadowed on our previous call.

Compared to 2021, our 2022 costs have been up meaningfully, due to inflationary pressures on input and energy costs, as well as lower production volume and higher repair and maintenance spending.

From a cash cost standpoint though, these costs peaked in Q2, but the impact on our results was not fully flushed through EBITDA, until Q3, a dynamic that can be seen, when comparing the Q3 and Q2 cash flow statements.

With all big repairs behind us, our repair and maintenance expenses have begun to decline rapidly here in Q4. Going forward, increased production volumes will also further dilute our fixed costs.

From a free cash flow standpoint, we generated almost \$300 million of free cash flow in Q3, largely driven by a significant amount of working capital released during the quarter.

Price declines, combined with lower cost of inventory, should lead to continued release of working capital in Q4 and into next year, supporting strong free cash flow generation, and partially offsetting the cash flow impact of declining EBITDA.

Also, our capital expenditures should decline in Q4 and even further into next year, where we expect total CapEx to be between \$700 million and \$800 million in 2023.

We also expect cash taxes to be negligible for the rest of this year, with a substantial refund coming in early 2023.

And of course, pension and OPEB cash needs will decline, substantially, as discussed earlier.

Consistent with our previously stated capital allocation priorities, we continue to use the majority of our free cash flow to pay down debt. During Q3, we reduced that debt by \$200 million.

And on a year-to-date basis through today, we have reduced our net debt by \$1 billion, bringing our current net debt level below where it was before we completed the acquisition of ArcelorMittal U.S.A.

Our capital allocation priority remains to continue reducing our overall debt. And beyond that, we still have around \$800 million remaining, under our current share repurchase authorization.

With almost \$2.5 billion of liquidity, a much cleaner balance sheet with meaningfully reduced pension and OPEB obligations, lower operating costs going forward, less CapEx next year, minimal cash taxes for the remainder of this year, cash coming in from working capital and no major bond maturities until 2026, we are in great shape to navigate any potential recessionary environment.

Very importantly, our automotive shipment levels in Q3 have indicated that our largest end market has been counter cyclical, due to the massive backlog from lower production, over the past two years.

The strength of our automotive franchise with our unique product offering and ability to lock in fixed price contracts will reduce volatility, especially now that our major maintenance, repair and capital expenditures are behind us, and costs begin to trend meaningfully lower.

I will now turn the call over to our CEO, Lourenco Goncalves.

## **Lourenco Goncalves**

Thank you, Celso, and good morning, everyone. Throughout my several years with Cliffs, our company has transformed and adapted to several different challenges. But two elements have remained constant throughout. Our commitment and full support to manufacturing in the United States is one; and the importance we placed on our people is the other.

This is not just a speech. We have backed this up with actions. Our latest labor agreement with our USW represented workforce is the most recent demonstration of that. The deal provides increased wages, offers better insurance, gives improved pension benefits, and enhances vacation holiday provisions.

We also agreed to continue to invest in our facilities at \$4 billion, over four years, combining CapEx and OpEx, which is consistent with typical spending on this type of investment for our footprint.

We also kept the retiree benefits strong and were able to negotiate lower rates across the board, as Celso has already explained.

Together with our union partners, we have integrated four standalone companies in a span of just two years, where we overcame a difficult pandemic, completed the construction of a state-of-the-art direct reduction plant, invested to keep our mills at an automotive level standard, paid down a significant amount of debt and drastically reduced our pension and OPEB liabilities, which we assumed two years ago, in order to make the entire transformation possible.

Our third quarter results were unique in that they reflect abnormally elevated costs, the largest portion of which was incurred in the second quarter but did not flow all the way through, until Q3.

We have been very open since day one that the set of assets we acquired, particularly those from AM USA, were a bit under invested and at some point, would need some catch up repair and maintenance.

We got great value on these assets on these two acquisitions and in fact, over the past two years, we have already paid ourselves back with profits from the business, even with the persistent underperformance of the automotive industry, during that timeframe.

That said, embedded in the low acquisition price was an implied catch-up repair and maintenance cost; that is now behind us. As a major supplier to the automotive sector, the quality standard for our equipment must be pristine.

We wrapped up repairs, beginning in the fourth quarter of last year, reinvesting a portion of our record profits earned throughout the year.

It was around that time that we're assigning new fixed contracts with our automotive customers at higher prices. So, it was even more important that our equipment capability was taken care of.

As our spending picked up, both CapEx and OpEx, in many cases, we found more work to do than we initially anticipated. The best example of this was the outage of our Cleveland works facility, which lasted from March through August.

The original scope of the blast furnace reline expanded to effectively include the rebuild of the wastewater treatment plant and the power house located on site, as well as several other smaller jobs.

Fast forward to the present moment, we are now at the point where the major maintenance cycle has been concluded. Due to the work we have done, our equipment is in great shape, and we are primed to meet the unique needs of our customers, particularly, in automotive.

The most common feedback we consistently hear from these automotive customers is about our perfect steel quality and our ability to keep them in steel during a time that the entire automotive sector has been deeply affected by underperformance from several suppliers, throughout their supply chain. Not the case with what they buy from Cleveland-Cliffs, and these clients know that.

Throughout this year, and particularly during the big repairs, we have seen the negative impact of lower production volume, reducing our ability to dilute our fixed costs. In the first nine months of 2021, we sold 12.5 million tons of finished steel, compared to 10.9 million tons of finished steel, so far this year.

That being said, automotive steel demand has started to improve in Q3, and we expect our volumes to increase further in Q4. That will result in improved costs, going forward.

The remaining drivers of higher costs, including increasing natural gas, electricity and alloys, are not unique to us. And we have also seen some relief in these areas.

All in, based on our inventory status and current outlook for input costs, we expect our reported unit cost in Q4 to fall at least \$80 per ton, compared to Q3, with further reductions into the first half of 2023, even after factoring the increased wages in the USW double labor agreements that were recently ratified.

As for demand, we were encouraged by the 100,000 ton volume improvement from our automotive customers, from Q2 to Q3. And while they're still not back to normalized levels, the worst impact of the chip shortage seems to be behind us. In our view, automotive is now in position to carry the market.

Despite the Fed's best efforts to damage the job market, unemployment at 3.5% is at a 50-year low, and that means people both need cars to go to work and can qualify to buy cars because they have jobs and paychecks.

Inventory levels at car dealers remain so remarkably low that even if there is a consumer slowdown at the end user level, there will still be a lag acting as a buffer until the slowdown in the production of cars, SUVs and trucks eventually falls. The current average age of light vehicles on the road of over 12 years is the highest on record.

Also, for those of you that have rented a car in the past year, there's clear evidence that fleet inventories need to be replenished as well, a meaningful 20% of the light vehicle market with a healthy backlog.

Our October fixed contract renewals were another success, and the weighted average of the price increase we achieved would represent the second-best October renewal cycle in our legacy company's history, only behind last year.

As we come to the table for our renewal cycle in January, our customers are being reminded that what we offer them cannot be compared to a CRU spot price. The difference between what makes up a CRU price and how we do business in automotive is night and day.

We manage our production schedule, based on our OEMs needs. We have to reserve our available capacity to align with their production forecasts, as we hold their inventory if they have production issues which, by the way, happens a lot.

We have a fully dedicated customer service group that manages this complicated just in time inventory system to the point that our customers don't even have to think about steel. It's there, when they need, automatic.

And this is all before we even consider the constant technical support, research and development and, of course, quality of materials that we provide them. In sum, in the United States, automotive steel means Cliffs.

Now that they have microchips, we want each one of our automotive clients to be successful in 2023. They have a unique opportunity in 2023, as automotive may be the only sector with pent-up demand to taken care of.

The last thing they need now is not having access to all the specs of steel they need to produce cars. That can be a lot more devastating than not having microchips.

On the distributor and service center portion of the business, customers have been following the typical herd mentality and buying hand-to-mouth in recent months. The strengthening of

the dollar has not helped price either, but the economics of overseas imports no longer makes sense, supporting demand from domestic suppliers, as we close out the year.

Our August price increase announcement brought some buyers off the sidelines, and we secured additional Q4 orders, as a result. As long as underlying demand stays this way in the coming quarters, a restock will need to happen.

Our grain-oriented and non-oriented electrical steels continue to see very strong demand, as we anticipate rapid price increases in the fixed price for those products.

We have an infrastructure build that should finally started to drive steel demand in the next year. We expect automotive taking up more steel share, and we have manufacturing being re-shored. When this thing turns around, it will turn around, sharply.

With an ongoing war, multi decade-high rising inflation, rapidly rising interest rates and a focus on mitigating climate change, we're living in a difficult time, as a world in transition. But we have already proven that Cleveland-Cliffs is capable of overcoming difficulties. The key to that is having the right people.

People is the foundation of ESG. You cannot pretend to care about the environment, if you neglect your people. And Cleveland-Cliffs will never do that.

Several companies, the vast majority actually, fight to their ESG challenges with MOUs, letters of intent and press releases, while Cleveland-Cliffs and very few others take concrete action.

We built a direct reduction plant, before it was trending. We adopt HBI using blast furnaces, and we will remain on the cutting edge.

Next for us will be the use of hydrogen, first, in our direct reduction plant and then in our blast furnaces. Blast furnaces have always been on the forefront of technological innovation in iron making and steelmaking and our current utilization of HBI as part of the burden in our blast furnaces is further confirmation of that.

The future use of hydrogen and carbon capture will be the next examples of American blast furnaces in the vanguard of CO2 emissions reduction.

Other companies in the United States and abroad are building new plants, and new plants add CO2 emissions, regardless of the process utilized. Cleveland-Cliffs is not adding capacity, and we will not add capacity.

We are reducing emissions within our existing installed capacity, and that will be the ultimate goal. After we completed two years ago, a transformational, once in a generation consolidation



of the American steel industry, some outsiders were fixated on the resulting pension and OPEB liabilities.

Fast forward, in less than two years, those liabilities have been made irrelevant.

With our major repair and maintenance impacts behind us, no ongoing or planned new construction project, an improving automotive sector and, most importantly, labor peace throughout our organization, we are ready to continue to execute, like we have been doing for eight years.

With that, I'll turn it over to Maria for Q&A.

### **Operator**

Thank you. We will now be conducting a question-and-answer session. If you would like to ask a question, please press “\*”, “1” on your telephone keypad. A confirmation tone will indicate that your line is in the question queue. You may press “\*”, “2”, if you would 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 star keys.

One moment, please, while we pull for questions.

Our first question comes from Lucas Pipes with B. Riley Securities. Please go ahead.

### **Lucas Pipes**

Hey, good morning, everyone. Congratulations on the OPEB obligation reduction. Lourenco, I remember, during COVID, you used some common-sense incentives to drive vaccination participation. And I imagine that maybe you'd use similar common-sense approaches to drive this really significant reduction in healthcare premiums, now.

Would appreciate if you could comment on some of the factors that drove that. Thank you very much.

### **Lourenco Goncalves**

Thanks, Lucas. Look, this is a negotiation that is extremely complex. It's not just the scale we go and we pose, because that actually takes cooperation with the unions, in order to get accomplished.

The vast majority of the USW, which we consider partners, and we consider that we are better because we have them with us. All the unions know our company. And that gives us the ability to include the non-union personnel, as well.

So, we present a very unified front, when we negotiate with these healthcare monsters. So, I think it's a first in a lifetime, that a company of our size was able to accomplish what we got. It's a cost per person that was cut in half.

And I'm not talking about steel company, I'm talking about companies, in general. This is a unique thing; this is called management. And of course, I know that everybody is looking to the quarter results, and I'm looking too, and I don't like it, but costs are necessary, and prices we fight with the weapons we have.

And we accomplish the best we can get. And eventually, we're going to have a quarter like Q3 that was not fantastic in terms of profitability.

But if you take one step back and see what we have accomplished, not just having the contract done with the union, but using the fact that we have a ratification to accomplish a much bigger picture type of thing that will kind of change the landscape, in terms of how healthcare is taking care at this point at Cliffs. I think that's how investors, really investors, should look into this thing.

#### **Lucas Pipes**

That's very, very good to hear. Lourenco, switching topic, and you touched on pricing. Three months ago, you were able to comment on the October contract resets with the auto customers. For January, do you have an indication at this point what direction pricing might take on the fixed portion? Thank you very much for your perspective.

#### **Lourenco Goncalves**

Thanks, Lucas, for the question. But as you know, October, the result of our October negotiations are not reflected into the numbers just yet because we are reporting Q3. Of course, you know that.

But what we are going to have, going forward, is a much better number coming from our October tranche that we negotiated, and the accomplishment is good. Of course, I'm not going to give any numbers, but we are in good shape.

Remember, we're the only ones--only ones-- supplying exposed parts, for example. We know that; they know that. We compete very little with the ones that can produce the more plain vanilla type of grades.

But we also keep reminding the car manufacturer that the car is a complicated puzzle, and we are the only ones that have all the pieces of the puzzle. So, that gives us leverage in the negotiation. I can't stress that enough.

In the past, we had Bethlehem, LTV, AK, Armco, Inland, keep going. They are all Cleveland-Cliffs, now. So, car manufactures know that. And that's a very important part of our negotiation. I think I have given enough color to you to see the picture.

**Lucas Pipes**

Lourenco, I appreciate the color very much. I'll turn it over for now. But continued best of luck. Thank you.

**Lourenco Goncalves**

Thanks.

**Operator**

Our next question comes from Emily Chieng with Goldman Sachs. Please proceed with your question.

**Emily Chieng**

Good morning, Lourenco and Celso. And thank you for taking my questions. My first question is just around--my first question is just around costs. And understandably, you're looking at \$80 a ton lower costs into the fourth quarter. But perhaps could you share maybe what you're seeing the moving pieces to be that would drive 2023 costs below that mark, as well?

**Lourenco Goncalves**

Yeah. I'll let Celso answer this one. Celso, please go ahead.

**Celso Goncalves**

Yeah, sure, hey, Emily. As we stated in our prepared remarks, there was a lot of repair and maintenance that we had to do here in 2022. And as we look to next year, a lot of those repairs and maintenance costs are going to come down, significantly. You can expect them to be down in the area of \$400 million for next year.

We'll have a lot lower idle costs next year, relative to this year. We don't have any major outages, like we did this year. So, there's a lot of tailwinds that are going to start dropping our costs here, rapidly.

And as we increase our volumes, this year, we've been kind of at that 3.6-million-ton level every quarter, and we're really pushing to get up to 3.8 million, 4 million tons again, and that's going to further dilute our fixed costs going forward, as well.

And then you have other things like energy cost, natural gas has come down a lot and things like that, that are also going to be a tailwind, next year.

**Emily Chieng**

Great. Thanks, Celso. And just a follow-up. Can you remind us on your gas and coal costs. On the gas side, you're still hedging 50% of that and the remaining 50% is spot. And with the coal piece of it, how should we think about the upcoming contract renegotiations there? Thank you.

**Celso Goncalves**

Yeah. On natural gas, you're correct, we're hedged 50% through the end of next year, at this point. And if you look at the futures curve for gas, it's around \$5 per MBTU, compared to almost \$7 that we're realizing here, this year.

So, those costs are coming down. And then on the met coal side, you can probably model coal cost to be up, call it, 5% to 7%, next year. So, it's still not meaningful.

**Emily Chieng**

Great. Thank you.

**Operator**

Our next question is from Tristan Gresser with BNP Paribas. Please proceed with your question.

**Tristan Gresser**

Yes, hi. Thank you for taking my question. The first one is on the plate market. Can you discuss a bit the market dynamics there, the premium elevated compared to HRC, but also the sustainability of that.

And moving forward with Nucor, a competitor wrapping up capacity, how do you prepare for the arrival of increased competition in the market and how strategic plate shipments are in Cliffs? Thank you.

**Lourenco Goncalves**

Tristan, the sustainability in pricing of the plate market is just about fewer participants and all of them responsible.

In the light flat rolled, we have at least one in the United States that is totally irresponsible and two in Canada that are completely irresponsible. So, irresponsible players destroy the market. The market destruction affects everybody. And in situations like that, management matters.

So, don't believe that we are here in the receiving end of this bad behavior from--compared that we know well. And we are not going to do the same thing and retaliate and create issues for them. And the plate market don't have that because everybody is in the market to make money, everybody is in the market to do their best for their companies and for their shareholders.

That's why we have a much better market in plate than in light plate roll.

As far as new capacity, the new capacity that's come is overdue. Plate has been a playground for imports for a long, long time, and I'm happy that Nucor put the capital to deploy capacity--where capacity is needed and push imports out. That's a good mentality.

One sector that will be good for us, Cleveland-Cliffs, as far as plate going forward, is military. And it's not just U.S. military. Of course, U.S. military goes without saying. But we are receiving orders from lots of countries that are friends of the United States.

They are all stepping up their expenditures on plate-related business. And we are the ones in the United States out of Coatesville, mainly out of Coatesville, but also out of Burns Harbor, that can produce quality military level plate. That has--we'll be one of the superstars of 2023. I hope I gave you the picture you're asking for.

**Tristan Gresser**

Yeah, that's very interesting. Thank you. My second question is a bit more on something you touched on in your remarks and about decarbonization, in general. We're starting to see steelmakers in Europe getting large sums of money to decarbonize and build DRI capacity and electric arc furnace capacity, as well.

How do you view that in a global perspective, as those steelmakers can be competitors, sometimes? Is that a signal for you to go to U.S. government and also do the same? Or do you believe that there may be room for more aggressive maybe trade actions, regarding Europe?

**Lourenco Goncalves**

Yeah, decarbonization in the United States is not, at least so far, has not been done through subsidies. It has been done through action and a couple of responsible companies that are doing very serious things.

As you may know, we built an HBI plant, and we use our HBI in our blast furnaces. And because we use our HBI in our blast furnace, our coke rate is 50% of the coke rates in Europe.

So, 50% coke rate, less coke usage means 50% less CO2 from coke. It's one to one in the psychometric relation. So, we are really decarbonizing in the United States.

In Europe, there's a lot of talk about decarbonization. But I think that the problem in Europe right now is currency, heating homes, finding a way around the lack of gas from Russia. I think Europe, right now, has a lot more important fish to fry. Decarbonization will be left for the oil that can do it. That's United States, we are doing, and we'll continue to do our own way.

**Tristan Gresser**

All right. Thank you.

**Lourenco Goncalves**

No question about pension OPEB? Your institute--financial institution out of Europe is the most concerned about pension OPEB and then we knock it off, and you don't even ask me a question?

**Tristan Gresser**

Well, it's pretty clear. So, we take note and of course we just--thank you.

**Lourenco Goncalves**

Good. All right.

**Operator**

Our next question is from Curt Woodworth with Credit Suisse. Please proceed with your question.

**Curtis Woodworth**

Thank you. good morning. So, I just wanted to follow up with respect to the cost guidance for next year, around the \$400 million. Because I think this year, you outlined \$200 million of reline cost. I think there was other kind of inventory absorption issues and high-cost inventory. In fact, in the P&L, I believe of another 100 to 150.

So, is the apples-to-apples kind of comparison for next year, would that be more like 100 million down? I just want to make sure I'm understanding kind of the cadence of costs, relative to this year.

**Celso Goncalves**

Yeah, so let me add some more color there, Curt. Thanks for the question. So, as we tried to explain in the prepared remarks, costs that we're seeing here in Q3 were largely a function of elevated spend from Q2. I think everyone kind of understands that, right. You could see in our cash flow statement that inventory was a 250 million inflow this time, and it was a 250 million outflow, last time.

But almost everything that drove costs up this year is coming down. Like I said, not only the kind of inflationary pressures that we're seeing on input costs, but also repairs and maintenance, as I stated, are expected to be lower by 400 million, next year.

So, everything that has driven costs up this year is starting to materially come off a Cliff. So, we're going to see the benefit of that in the quarters to come. I don't know if I specifically answered your question, but happy to add more color, if needed.

**Curtis Woodworth**

Okay, so MRO, apples-to-apples, will be down 400. And then should we assume then because of--I don't think you have a major reline next year that that would give you another two to three hundred. So, kind of the total cost down potential of 700 for next year. Is that correct?

**Celso Goncalves**

That's correct. Yes.

**Curtis Woodworth**

Okay. And then just a follow-up on trade policy in the United States. There's still Russian pig iron coming into the country. And just kind of curious just in general, what communications you've been having with maybe the Department of Commerce? And just kind of any updates on how you see trade policy in the U.S. Thank you.

**Lourenco Goncalves**

Yeah, look, Curt, Lourenco here. We communicate with them. But this pig iron that comes into the country, directly or indirectly through rerouting and transshipment, it doesn't happen in a vacuum. It happened because the ones that import pig iron are importing pig iron, and they know what they are doing.

So, we are not cops. We can inform and we inform, but that's pretty much it.,

And if a company imports pig iron from Russia, don't play the nice guy. You are supporting a dictator. You are supporting a butcher that 50 years from now will be put at the same level as Hitler.

So, that companies in Germany that still as of today pay the price for supporting the Nazi regime. And the ones that import pig iron are setting themselves up for future scrutiny. It might look good for the quarter; it might not look good in five to 10 or 20 years.

**Curtis Woodworth**

Understood. Thank you.

**Operator**

Our next question is from Alex Hacking with Citi. Please proceed with your question.

**Alex Hacking**

Yeah, thanks. Good morning, Lourenco and Celso. So, on the automotive side, if I look at the U.S. auto, what I saw, it seems like it's been running maybe 20% below where it should, 13 million versus 16 million to 17 million.

Is that how we should think about the impacts on your volume? Because if I sort of run it through your auto volumes, it would seem like you've been shipping 300,000 to 350,000 tons below what you would normally expect to. And so, that would be the amount of volume that we could potentially see recover every quarter as the automotive market recovers. Is my math there kind of correct?

**Lourenco Goncalves**

You are directionally correct, yeah. We are still in the 13 to 14--less than 14. We did the 13s in automotive. And it was kind of expected by now that this level would be a lot closer to what was the normalized level between 14 and 19 and would like that. So, we are still running behind. They are still running behind.

This being said, it's encouraging to see a quarter that was concrete. We have a concrete number to show and say, look, we're a 100,000 tons ahead. It's not anything to throw a party of but is encouraging. It's a step in the right direction.

Car prices are increasing to the end user. So, the car manufacturers are making money. So, the biggest supplier of steel to the car manufacturers is making money as well on that--on those sales and plans to continue to make money on those sales.

We might have too many car manufacturers in the United States. That's another thing that we need to think about. We are taking that into consideration in our strategic analysis.

**Alex Hacking**

Okay. Thank you. And then, Celso, I think you mentioned in your remarks that you would not be paying cash taxes for the rest of the year. Would you expect to pay full cash taxes in 2023? Thank you.

**Celso Goncalves**

Yeah. I mean that's right. In Q4, cash taxes are going to be minimal. And then for 2023, obviously, it's going to depend on profitability. But depending on how things play out, we could even have a big tax refund coming. So, that could be a source of cash early in '23, as well.

**Alex Hacking**

Thanks, and what would be the driver of the tax refund? I apologize for asking another one.

**Celso Goncalves**

Yeah, I mean we've made some overpayments here, this year. So, some of that would be reversed back and we'd get some cash inflow from that.

**Alex Hacking**

Got it. Thank you very much.

**Celso Goncalves**

Yeah, no problem.

**Operator**

Our next question comes from Carlos De Alba with Morgan Stanley. Please proceed with your question.



**Carlos De Alba**

Yeah. Thank you very much. Good morning. So regarding prices, I know that you don't want to give us a number, and it's understandable. But maybe just talking about the outlook for January reset of your contracts, if I'm not mistaken, that is a bigger chunk of renegotiation for you guys.

So, how is that progressing, given the trend that we have seen in the spot market down but the recovery in auto sector volumes that should potentially offset that, maybe more than offset that. So, any color for the January reset of contracts, that will be great.

**Lourenco Goncalves**

Yeah, look, the trend will be the same. We are just starting, actually. So, there's not a lot of details available on the automotive contract renegotiation on specifics like we have for October.

But you're right, Carlos, it's the vast majority. But the threat has been put in place. Our conversations with the January crowd should be even more facilitated by, one, the fact that these clients that we deal with in January tend to be a little more reasonable.

And second, because they are seeing what we are doing with others because it's funny, all these prices are extremely confidential. But they know a lot more than we release because we respect our NDA's.

So, at this point, they know that we are not bluffing. They know that we're real. At the beginning, it was kind of, who's this new Cleveland-Cliffs thinking, who is this Lourenco guy? Now they know. So, I believe it to be easing.

**Carlos De Alba**

All right. And in terms of volumes, just to clarify, so it's clear that production in the fourth quarter is going to improve. Shipments in the--to the automotive--like sales volumes to the automotive sector will also increase. But just to double check, the overall volumes, shipment sales volumes in the fourth quarter, do you also expect them to move higher?

**Lourenco Goncalves**

Yeah, we are. Look, we no longer have repair, big repairs in place. So, we are expecting to recover our usual 4 million tons of shipments a quarter, 3.9 to 4 million tons a quarter. It all depends on how much slabs we are going to add to the mix. And so, that's why saying 3.9 to 4.

But actually, more slabs, even though they help dilute the fixed costs, they are not exactly our best money maker, if you will, because it's lower value added than hot-dip galvanized for exposed part or ultra-loom or anything like that. There's a play between the mix and the volume. The higher volume helps cost but, eventually, the higher volume comes from products that have a lower margin impact.

**Carlos De Alba**

Right. No, that's clear. Okay. And then if I may, just one final question. With the cost coming down, CapEx in the \$700 million to \$800 million range next year, even contemplating lower steel prices, it seems that your free cash flow generation is going to be quite interesting, quite good.

Any changes on the capital allocation front? Or you continue to prioritize debt reduction and maybe some share buybacks and not dividends yet?

**Lourenco Goncalves**

Look, the priority continues to be paying down debt. We continue to do that, quarter after quarter after quarter after quarter. And even though the underlying EBITDA was lower, cash flow was not. Because remember the priority. The priority is not to impress the Street. The priority is not to add a number of subscribers like these unicorns.

Our priority is to pay down debt. So, that generates cash. So, we did not renegotiate with our healthcare contracts because we would like to be nice. It was because we'd like to reduce costs to generate cash to pay down debt.

So, we are doing exactly what we told you guys that we will be doing. And the investors that understand that will stay with us. Actually, they will take the opportunity of the shares on sales to buy more.

If we are going to be able to buy more, we have the authorization. But what's my priority, Carlos? My priority is to pay down debt; not to pay a dividend. To pay down debt. When we get to a point to say yeah, that's good.

That's the level that I feel like is sustainable, going forward. There is no inflation. The Fed is no longer crazy. They are not trying to destroy the economy. They are not trying to generate unemployment, because that's what they're doing.

And we are in a much more stable world, then we can do whatever we need to do to continue to grow toward returning capital to the shareholders. But don't neglect the fact that we bought a lot of stock, so far. We did, and that's returning money to the shareholders.

**Carlos De Alba**

All right, excellent. Thank you very much, Lourenco.

**Lourenco Goncalves**

Thanks, Carlos.

**Operator**

Our next question is from Timna Tanners with Wolfe Research. Please proceed with your question.

**Timna Tanners**

Yeah, hey, good morning. I really like Lourenco's point about all new mills add carbon emissions. That's fun. I wanted to just ask a follow-up on the volume side, if I could. Looking ahead, we've seen a mix of philosophies out there. Some mills are adding capacity and running it. Some are cutting capacity and shedding.

Cliffs obviously benefits, as you point out, from running more volumes. And you have Cleveland back running, you have automotive improving, but yet your steel production is still below year ago levels. And I'm just wondering, how do we think into next year on the mix of your potential volume and how that can help continue to cut your average cost? Thanks.

**Lourenco Goncalves**

Thanks for the question. Look, we will continue to explore, to maximize the utilization of the assets that we have. And we are not going to take equipment down just to implement discipline in the market, if others are completely undisciplined.

If the others feel like their business model is predicated on destroying the marketplace, just because they feel that they can put the scrap price whatever they want. They might be right, but we just don't agree with that type of approach. But we run our assets to minimize our costs. As long as we can make money, we will run. And I think that it's a good balance because we can generate cash that way.

So, don't count on me to take my capacity out to make the life of others better. That happened in Q2 and a portion of Q3 because we had to make a big repair at Cleveland Works. When Cleveland Works was done, we came back. But also, remember, Cleveland Works, I don't know if you know that, but it's the biggest producer of advanced high-strength use for automotive exposed users.

So, the one reason that we fixed that thing is because we have a lot of confidence that automotive will pick up and the orders that come to Cleveland Works will start to pile up. And actually, we are seeing that, as we speak.

Others cannot do that. That's why our capacity can come back, because it's serving markets that I believe in 2023 might be the only ones that will be exciting, automotive being the biggest one.

**Timna Tanners**

Got it. So is it reasonable to assume that continued progress in automotive recovery can result in Cliffs producing over 4 million tons again per quarter? And can that mix still be kind of swayed to automotive or is it going to be also shipping into some of those other businesses?

Because I think we've seen a bit of mix deterioration into the fourth quarter. Just how do you see that, going forward?

**Lourenco Goncalves**

Yeah. Let me-I think I already explained this mix deterioration. Automotive is the reason why we are back to 4 million tons, a quarter. And it will be that, going forward. So, that's automotive. Automotive is supporting this growth.

**Timna Tanners**

Okay. I'll leave it there.

**Timna Tanners**

Thank you.

**Operator**

Ladies and gentlemen, there are no further questions at this time. This concludes today's presentation. You may disconnect your lines at this time. Thank you for your participation.