VALE

Transcript of conference call on

2012 3rd Quarter Report

October 25

Portuguese: 10:00 a.m. (RJ time)

Introduction

Operator: Good morning ladies and gentlemen. Welcome to the Vale conference call, during which we will discuss the results for the third quarter of 2012.

At this time, all participants are connected only as listeners. Later on, we will hold a question and answer session, when you will be given instructions to attend this session. If you require the assistance from an operator during the call please press star zero.

Please note that the conference call is being recorded. The recording will be available on the company's website at the address, www.vale.com, section investors. The replay of this call will be available by telephone (55 11) 4688-6312, access code: 4704575#. This conference call is being simultaneously broadcasted over the internet, and access is also through the company's website www.vale.com, section investors. Or on the website www.prnewswire.com.br.

Before we move forward, I would like to clarify that any statements that may be made during this conference call regarding the perspectives and the business of the Company, as well as projections, are forecasts based on the management' expectations regarding the future of Vale. These expectations are subject to macroeconomic conditions, market risks and other factors.

The following persons are attending this call:

- Mr. Luciano Siani Pires – Executive Officer of Finances and Relations with Investors;
- Mr. José Carlos Martins - Executive Officer of Ferrous and Strategy;
- Mr. Peter Popinga - Executive Officer of Base Metals and IT, and
- Mr. Galib Chaim - Executive Officer of Capital Projects Implementation.

To begin with, Mr. Luciano Pires will make some comments about Vale's performance during the third quarter of 2012, soon after he shall be available to answer questions that may be asked.

Now I would like to turn the call over to Mr. Luciano Pires. Please go ahead.

Luciano Siani: Good morning to all. Thank you very much for joining us. As you know, the third quarter was a period of many challenges and a lot of volatility. Especially in our main product market. But, I hope to convey to you the idea that, within our principles of management, Vale responded well to these challenges. I would like, for those who have the presentation that was made available on our website, I will follow approximately the structure that is defined in the presentation. I will start by reaffirming some principles that have guided the new strategic decisions of Vale. After that, I will make some more specific comments about our statement of income and balance sheet. And finally, we would like to pass some information on how we see the main market for our products, which is China. We understand that you all have opinions about this, but we can contribute with some elements to help form this opinion.

Well, as far as the overall context is concerned, I would like to say that Vale will continue to prioritize only investments and operation of world-class assets. In order to maximize the return to our shareholders. That is, we are no longer pursuing the growth or the generation of volume without creating value. In this sense, the diversification of our business is more a consequence of having world-class assets in different commodities, than an objective per se to be pursued. In this context of reduced revenues as well, due to lower prices. We have stated that we will adjust our cash flow, our investment program to our cash flow. And as we will demonstrate later on, this is being done. 2012 will probably represent the peak of our investment plan. And we are making efforts to reduce the total investment in comparison to what was predicted last year, as to know $21 billion. And in 2013, of course, the value will also be lower than the number that we will reach in 2012. Also in terms of our capital discipline, as we already have a quite diverse and varied set of growth options, we are reducing expenses with research and development. We believe that research and development are used to create future options. Since these future options are already available, many of them, it makes no sense to keep the same pace of investments in research and development.

Cash management, as I said, shall prioritize the adjustment of investments and cash generation, as well as the maintenance of the investment rate. We believe that market volatility requires a more conservative and careful approach from the Company. In this sense, we are moving all our planning forward, based on more conservative assumptions, we expect positive surprises regarding our assumptions. This will allow us to deleverage the Company or limit the leverage, or even offer a greater return to our shareholders.

In this sense also, everything that does not fit this philosophy is being reevaluated. We are reassessing our entire non-core assets portfolio. And we intend, and you may expect, over the next 6, 12, 18 months, continued asset sales initiatives. During this quarter you have seen, for example, the sale of ships to release capital from our balance sheet.

One important issue I would also like to point out is that a central leverage for managing our investment program, so that we do not fail to pursue opportunities because of cash restrictions. We will try to establish, whenever possible, partnerships to develop many of our projects. This is also something that we are looking for on a more widely basis in comparison with last year, to seek for project development partners. We will even provide details on Vale Day; we will describe, in details, how we concretely intend to deploy these partnerships in various emblematic projects of our company that you know.

With respect to the investment program, we had already stated last year that our top priority would be S11D. To regain our position, our *market share*. It is a very low cost operation. We have already announced our expectation that ore be shipped at a cost of $15.00 per ton. It is a world-class asset. Therefore, we can recover the levels of quality that have always characterized our products. And besides iron ore, there is Moatize. It is a very important world-class asset and its implementation is our absolute priority.

Obviously we need to spend resources to complete projects that are underway. As an example, Tubarão VIII, Salobo II, Long Harbour, and, therefore, besides completing the projects that are underway. To pursue world-class projects; we are being very cautious and we are not, at this time; we are being very cautious to start new projects apart from that partnerships that I mentioned.

I have also mentioned in some meetings with investors that we expect to have good news to tell you in the coming years regarding the company's main business, which is iron ore. We recognize that Vale could not keep up, lost *market share* in recent years, for failing to increase output. We are now, at this moment, working with a much better licensing process. We had about 72 licenses already issued this year against slightly over 20 last year. This allows us to open new pits; this allows us to move forward with projects, this allows us to recover our production levels. Projects like +40, Serra Leste, will ensure capacity increases especially in the second half of 2013. So you can expect, after 2016, in the second half of 2017, with the beginning of Serra Sul, we can expect, then, a growth profile in the core business of Vale, regaining the market share that was lost. And that growth will be profitable, like I said, because even with lower prices, operations to come will be very low cost.

We are also adapting our sales and business strategy to new market circumstances. Notably the preponderance of Asia and the strong importance that the spot market has been gaining. Our philosophy is to be closer to clients. We are building a distribution center in Malaysia. But you have already noticed some impacts of this strategy to be more commercially close to clients, including in the results of the quarter with an improved price realization, which we shall comment below.

We have also given another emphasis to capital discipline; except for the iron ore business, we are being very strict in assessing the prospects of the other businesses of the company. A business that we know is a major concern of investors and shareholders is the Base Metals business. You recently saw some news about mines closing in Canada, the Frood Mine which is part of the Stobie complex, and the Birchtree Mine in Thompson. There are two mines that marginally were not adding value to our portfolio's current prices, and therefore, they are being placed under care and maintenance. We are reviewing all of our Base Metals assets. We are slightly optimistic in relation to the New Caledonia assets, Peter Popinga will take about this later on. We are doing well in the Salobo ramp-up, and we have already reached 40% of our capacity, line two has kicked off. There already is a little bit of the copper production of Salobo in the production report, it already appears on the line of others. The production of gold, Salobo, has the potential, Salobo I and II, of producing more than 300,000 oz of gold per year. So current prices, it is a very interesting by-product. You can now also expect a continued rise in Vale's gold production in the future.

We are committed to the nickel business, because it is a core business, we need to generate value with it. But it is not a priority for expansion right now. And even within the nickel and copper business, assets that are not adding value will be divested.

Okay, let's now talk specifically about results. As far as income is concerned, I will first talk about volumes and then prices.

In relation to volumes, you saw in the production report that, despite the increase in the iron ore production in relation to the second quarter of 2012, it has decreased in comparison to the same period last year. Traditionally the third quarter is a very good period. But we could not keep the same pace of production, mainly in the northern system.

However, it is very important that you have in mind that, in view of its extended chain operation, Vale currently has an extended supply chain up to its customer in Asia; our inventories, including finished products, allow us to absorb production variations without any impact on sales. And thus, the volume of sales in the quarter can relatively be within the forecast and we continue, in relation to the end of the year, to aim at the achievement of both production and sales volumes that we have set at the beginning of the year. This means that we have the capacity; a loss of production in a quarter does not necessarily mean a loss of sales. We can recover production levels later on, since we have these inventories. So, this is what you need to have in mind.

We are adjusting the production of pellets to the market, this has already been reported with the closing of the provisional plants I and II in Tubarão, and with the closing of the plant in São Luís It is important to note, as you probably already have, as far as prices are concerned, that the price of pellets in relation to the price of iron ore is much higher since the sale of pellets takes place through contracts and primarily to customers in Europe and Japan, therefore, it was still strongly impacted by the prices of the previous quarter, due to our contract terms. This explains much of the difference that some of you may be wondering about, if with a premium of this magnitude, it makes sense to close the plants. No, we reaffirm that premiums are not enough to compensate, for example, the operation of these plants, so we are closing them temporarily.

As far as coal is concerned, despite the fall in production in the quarter, it is important to note that Carborough Downs is closed. We also managed to recover production; we are operating the mine in a certain way now, recovering again the capacity of the Carborough Downs mine. We have a new long-wall in Integra; we are approaching favorable geological formations in Carborough Downs. Thus, the estimate that our coal production in Australia will recover. With regard to Mozambique, our ramp-up in the mine is doing very well. We have some temporary issues on the railway, which are not allowing our product to be delivered. We hope to solve these issues and to have a better result in the fourth quarter. So, right now, our production in the Moatize mine is being limited by logistics capacity. Unlike iron ore, coal is a product that can not be stocked so well, so it makes no sense to produce to stock in the Moatize mine. But there are no operational restrictions in the Moatize mine on our ability to grow production at this point.

In the case of copper, I already mentioned Salobo; the copper production was also impacted by production decrease in Sudbury. We made a planned shutdown in the third quarter of this year.

When we look at the accumulated figures over the year, the biggest impact in production was mainly in Ontario, it was the safety shutdown we did in the second quarter in view of some security issues and except for that maintenance shutdown that was already planned.

I would also like to draw your attention to the beginning of concentrate production in the Lubambe mine in Zambia. What can also, from the standpoint of copper, bring us an additional important volume as the ramp-up continues.

And finally for the fertilizer business, it is important to note the continued positive performance of the Bayóvar mine where we still break records in phosphate rock production during the quarter.

In relation to prices, there was a decrease in iron ore prices in the market of approximately $29.00. We have already talked on other occasions about, there is a different relationship between dry and wet basis prices, which are the prices performed by Vale. So, even after making all these adjustments, we actually had a better price realization in the quarter of approximately $8.00 or $9.00, which was possible thanks to various business strategies adopted as the spot market gained importance, as the lead time gained importance. We are adjusting to these new market circumstances, the destocking that took place and our business strategies were successful. Therefore, in relation to the market, we had an important gain in prices and the difference between Vale's realization price and the platts price was reduced. Obviously, the price of nickel has also followed the falling trend of commodity prices in the quarter. Now, in the case of fertilizers, showing that we have, this is really a more anti-cyclical business, some of our products have a good price performance, and we even made some changes in the mix of phosphates to work on that higher profitability segment.

When we look at the translation of these volume and price performance in the income statement, we see that the revenue decrease was of approximately $1.2 billion and it is transferred almost entirely to the fall in EBITDA. EBITDA is of $3.7 billion in the quarter. Taking into account the provision for CFEM about which I will talk later. But it is important to say that this immediate transfer of revenue to EBITDA is due to the relative stability of deductions from income for the composition of EBITDA. That is, our costs had several factors influencing several of its components up and down. But anyway, these are small variations that somehow are offset. Costs are relatively stable. We still do not want to say that we are in a downward trend in costs, but I think we can easily say that although we are still in an escalating cost environment, operating costs are under control.

Moreover, from the standpoint of research and development, which is also a deduction to EBITDA, we are sure and can already tell you that you will see a downward trend in the costs of research and development. In this quarter, we are still stable at $360 million, but traditionally there is seasonality, the third quarter is very strong in CAPEX, research and development expenditures at Vale, third and fourth quarter. If you compare nine months to the third quarter of 2011, there is a significant reduction. We had estimated, at the end of last year, that $2.1 billion would be spent on research and development and this year, we are at a pace that you can see is much lower than that, and will still be reduced. We, for example, closed some mineral exploration offices which added value, in our opinion, no longer corresponded with the business plan. So those costs with the closing of some offices in some countries will, in future, correspond to a decrease in research and development costs. General administrative expenses have also showed some stability and also are an account which you may expect to be reduced in the coming quarters as the company has recently set up an infrastructure in order to prepare for growth, an investment plan that is, as you know, being adjusted to the Company's cash flow and more focused on world-class assets. And, therefore, the administrative and support infrastructure will be adjusted accordingly. I highlight the stability of these costs, but also briefly suggest a downward trend.

Another important point affecting EBITDA, as we already reported, is the provision for the payment of CFEM, R$1.2 billion reais more, $540 million. Because our loss assessment regarding that specific segment has become probable. So we made this provision, and that impacted the EBITDA. Moreover, you can also see that we are making provisions for the payment of TFRM fees both in the states of Minas Gerais and Pará. In the specific case of Pará, we recently managed a reduction of the TFRM value. This means that expenses with this item, with the fee in Pará, will fall significantly from now, as of October. And Vale, which was only provisioning amounts, but was not making deposits, will then make the payments because it believes this is an appropriate value, which was agreed with the government of Pará.

As I mentioned, EBITDA, you can see on page 17, some drivers that impacted the reduction of EBITDA in the second quarter, compared to the third quarter. And the effects on volumes, costs and expenses, as I mentioned, are marginal, and the main effect is CFEM, that’s it.

I would like to call the attention to page 18 specifically, and for those who do not have the presentation, I will describe what we have here. We had a cash generation over the past nine months that was very compatible with the uses of our cash, and the sources of resources are fairly balanced. Our cash flow from operations was of $13.3 billion. We did some net divestitures and acquisitions, such as some portions of the MBR we had not yet acquired. We had divestitures, assets in Colombia, manganese assets and ships. So we had a net amount, a net source of resources from divestitures. And we had a relatively small increase in net debt, of approximately $1 billion this year. Why? Because we managed to control expenses with current investments and projects. And, in a reasonable manner, we spent $11.2 billion in the first nine months of the year with capital projects and current investments. This value does not include research and development. Because research and development already causes EBITDA deduction. We managed to return in the first half $3 billion of capital to shareholders. We also had a net variation of other accounts, for example, working capital consumed a little cash. But the important message here is that in a period of quite visible falling prices, we managed to get through it with a very moderate increase of our debt.

Well, I believe we will have the opportunity to talk, perhaps, about the high profit of China further along, during the questions and answers session. That said, I would like to turn the call to those who are already attending the conference, so that questions can be made.

Questions and Answers session

Operator: Ladies and gentlemen, we shall now begin our questions and answers session. To ask a question, please press asterisk (*) one (1). To take your question from the line, press asterisk (*) two (2). Only two questions can be made at a time.

Operator: Our first question is from Mr. Rodolfo de Angele from JP Morgan.

Rodolfo de Angele: Good morning, my two questions are first regarding working capital, we saw that the company has greatly reduced its working capital in the quarter. I was wondering if you could talk a little bit about this. And, if this is a trend, what can we expect for the future? Is this one of the leverages that management should use to face this new scenario? And second, in relation to CAPEX, we know that the budget is of $21.4 and you have said that it will be below that. If we take the number so far and annualize it, the result is $16.4 billion for the year. But also looking back, in the fourth quarter, CAPEX is usually higher. So I wanted to ask if you could talk a little bit about what to expect especially for the next quarter, if you could also talk a little bit about next year too, I think it would be very interesting. That's it, thanks.

Luciano Siani: Well, first of all, I would like to say that our CEO, Murilo Ferreira, apologizes for not being here. He had an emergency and could not attend.

But addressing the issue of working capital first, in fact when you look at the numbers on the cash flow statement or balance, there was a release of working capital. It was influenced by several factors, some of which are under management control, and others that were more untimely and temporary. I would not say that this reduction was very significant, it will continue in the coming quarters. But it is true that management is making all efforts to reduce working capital.

Particularly we are working with accounts receivable leveraging, we have tried to obtain some financing from suppliers. Trying to control more [of] our inventory. So yes, there is a big concern regarding the release of working capital through effective management. We are in fact managing it actively. Some of the results can already be seen on the balance sheet for this quarter. But not everything you are seeing is the result of a, to give you an example, as we were not making the payment of the state of Pará TFRM. These amounts were being provisioned, so there is an increase, for example, of taxes to pay, which is a working capital account. So not everything you have seen in this quarter will be recurrent, since those taxes will be paid.

With respect to CapEx, our intention, as mentioned some times, is to keep CAPEX in line with cash flow. Rodolfo, you mentioned that there was an accelerating trend in the last quarter. But we will certainly have cash flow, the company's EBITDA shall be higher than CAPEX, keeping this profile, this trajectory of little leverage on the balance sheet. So I think we should expect, perhaps, a quarter with absolute value greater than in the third quarter. A more modest acceleration than in previous years.

With respect to 2013, as I was saying, we will provide details on Vale Day. We're still working on some final adjustments, but we expect 2013 CAPEX to be inferior to 2012 with the trend I mentioned. Without specifying a number, I'd say this is the trend. An increased pace in the fourth quarter of 2012, but a not very significant increase. And a 2013 lower than the 2012 accumulated figure.

Operator: Our next question is from Mr. Felipe Hirai from Bank of America.

Felipe Hirai: Hello, good morning, good afternoon to all. I have two questions. The first one refers to the iron ore price. Luciano, you mentioned this fall in the difference between the realization price and the platts price. I was wondering if you could explain in more details what contributed to this change of almost $8.50? And what can we expect in the future, in terms of realized price discounts? And my second question is regarding pellets projects. You shut down three pellet plants, but are still making investments in Tubarão, and continue making investments in Samarco. I was wondering if these investments may at some point also be reassessed Thank you.

Luciano Siani: Felipe, thank you for your question. I will ask our ferrous executive, José Carlos Martins, to answer it.

José Carlos Martins: Well, Felipe, regarding the issue of price. You have an effect, which is the freight effect. We had a better freight performance as our fleet grew with large ships coming into operation. We had a small reduction in freight. And then we also had a higher number of CIF sales. This allowed us to reduce the impact of freight, improve the FOB price. Because as IODEX, the market price is CIF, you have a lower freight, you have a better FOB price. The other factor is the factor related to VIU, at the beginning of the last months, we had a very strong pressure on the issue of silica. In relation to the market, there were many offers and then you have the demerits of silica. These demerits of silica have also decreased. So there is a combination of effects of the market per se, with a better performance from us.

Currently, almost 20% of our sales are in the spot market. And of course we are to the extent that we gain forces in this segment, we learn to work better. Luciano mentioned at the beginning of his presentation the issue of the extended company. We are postponing our sale timing. We realized that every time we try to sell ore in advance in the spot market, as we do it before our competitors who are closer, we end up getting a discount on top of an earlier attempted sale. Because buyers are not so sure. The guy buys today and by the time the ore gets there, he might have a different price situation than the one he purchased for. So we postponed a little bit the sales moment, and this helped a lot as far as pricing is concerned. There are several factors. Just to give you an idea, today, I find it important to mention, 20% of our sales are provided for in contracts. No, sorry, 20% of sales in the spot market, and 80% on contracts. The sales under contracts have a different distribution with respect to the pricing system. About 20% of contracted sales are under the old systematic, as to know a quarter with lag. We have approximately 35% of sales in the same quarter, as to know, in the current quarter. In monthly pricing, only we only 5% of sales. And nearly 40% of sales are on a daily pricing basis. If we add the 20% that are sold on the spot, and the remaining 20% that are sold under contracts, but priced daily. So this basket of contracts that we have, it ends by also leading to a difference in this pricing. As you are comparing with the average of the quarter, of IODEX, as you sell based on these different forms of pricing, you have an impact. And in this quarter, it was positive. This pricing basket ended up causing a positive impact on our prices. So, there are a lot of factors that I would say are market factors, exogenous factors dictated by the basket of products. And there's also the work of the commercial area, we better understand this market reality and try to sell at the best timing. But, in general, I would say that our price performance perspectives are better today than they were in the previous quarter.

Regarding pelletizing, we interrupted the pellet operation in the north, as well as two pelletizing operations in Tubarão. Basically, in terms of cost structure, these pellet plants that were shut down had a less favorable cost structure.

With respect to investments that have been made, which are in progress, they have already achieved an irreversible level. These are investments that will result in lower operating cost pellet plants. And we are constantly monitoring the market. If it is necessary, in the future, to make any additional adjustment in production, we will do it. And, of course, we will not choose to keep the pelletizing operations that have a better performance.

In the long run, our vision of pellets is a positive vision. We understand that, according to environmental and productivity aspects, of the blast furnace which, at this moment, is not very necessary, pellets are slightly more affected. Now, in the long run, the environmental issue and the issue of shale gas in the United States, we believe there will be a recovery of U.S. production in the future based on a direct reduction where pellets will be needed. So we have to adapt to conditions in force. Vale, as it has the option to sell the feed, we have to always be looking at the price relations, because the fact that I do not sell the pellet does not mean that I can sell the pellet feed, the basic raw material for pellet for a better price. When you compare the position of Vale in relation to other manufacturers of pellets in the market, they do not have that possibility. Basically they have to sell the pellet, we have the option to sell the feed. And that's what we're doing. Then the shutting down of pellet operations does not mean loss of volume, only a change in the product mix.

Operator: Our next question is from Mr. Renato Antunes from Brasil Plural.

Renato Antunes: Good morning everyone, thanks for the question. The first question is with respect to price. If you could only, in this whole explanation of José Carlos Martins, I just wanted to understand if there was some price carryover component from last quarter to this quarter that may have helped a little bit too? And also with respect to the spot price, you mentioned in the release the issue of destocking during September. If you are seeing some sign that we may restock towards the end of the year? That's the first question. And the second question is regarding the inspection fee in Minas Gerais and Pará; you mentioned that you reached a lower value in Pará and yesterday we saw that the Legislative Assembly of Minas has passed a bill allowing a discount of up 70% on the fee. I wanted to know from you, just to confirm, Vale, today, is not challenging and is adopting a more amicable posture, that is, to pay those fees, possibly at lower rates. And also I wanted to understand the $145 million that you earned today, if you could talk a bit more about the level of supervision fee that you provisioned? If it is $2.00 for both Minas and Pará, or if it was a little less, a little more than that? Thank you.

Luciano Siani: Thank you for your question. I will start with the inspection fee. I think it's important to have in mind that we currently are negotiating, quite friendly and comprehensively, with governments from both states, with a view to a comprehensive agreement involving all Vale's tax issues in these states. TRFM is only one component of these negotiations. We have things that are moving backwards, things that are moving forward, that is, it is a very broad relationship that has many facets, and we are addressing all of them. We want to find a solution working together with governments, a definitive solution to Vale's tax issues in those states. Obviously, these things take some time, they need to be, as you mentioned, the legislative assembly of Minas agreed to the possibility of payment in installments and reduction of TRFM in Minas Gerais. But there are also other components of such negotiations that will also take their due course, we hope that such determinations are approved. We can even, when we reach a broader agreement with governments, issue a special press release on the subject.

With respect to provisioning, if I understand the question. We provisioned according to what was being charged. So the provision was based on the amounts the states were planning to collect before those agreements. And, from now on, we will adjust to this new reality. It is important to note that there are other entities that may continue to challenge the TRFM. But, as regards to Vale, these negotiations are being conducted in a very broad scope with both state governments.

José Carlos Martins: Well, with respect to price, as I mentioned in the previous question of Felipe. Almost 20% of our sales that are based on the previous quarter are lagged one month. So this impact has been positive on the company's results, since the price began to fall. In the first quarter, this impact was positive, and it remains positive. When the price reverses the downward trend in relation to the average, and starts going up, this carry over will have a negative effect. But quarter specifically, this impact was around $1.20 under our charged price. It improved the charged price in $1.20. In the previous quarter, it was $0.60 so this impact is embedded.

Luciano Siani: So, in other words, José Carlos, in the narrowing of the price gap, is the difference between $1.20 and $1.60.

José Carlos Martins: Exactly! If you compare both quarters, this carry over has helped the price in the range of $0.60.

The great positive impact on price was the freight. The freight, it was almost a $2.00 gain in relation to the cost of freight that we had. Our freight basket last quarter, compared to the freight basket this quarter.

Well, in relation to restocking, I think all information is available. Ore inventories in Chinese ports are lower than before, as well as inventories at mills. In general, the market is working with lower inventories. Even the steel stock is greatly reduced. It is not yet possible to assess the inventory of steel products in the distribution chain, cars, buildings under construction, this whole thing. But, in general, what we're seeing in the stock of ore steel is positive in the sense that we have a possibility of system restocking.

And I think that price is the best indication of that. Price, for example, was of $120.50 today, a small increase in relation to yesterday, which was of $120.00. So the scenario is a scenario that I would say is not excellent, but it is positive. There are very positive signs of recovery of demand in China, which is where price is formed. Prices are defined in China.

But I insist that much of the decline we've had in recent months is much less due to demand, and more to supply. There was a substantial increase in the supply of ore to the Chinese market. And, of course, as prices are defined in that market, this has a reducing impact on prices. To the extent that this offer is now stabilizing at a higher level and there is a displacement of local producers of Chinese ore. The price trend is to evolve to a little higher level. It does not mean much, as, if prices continue to rise, local producers of China will return to the market. So you have a process of price regulation therein, a process of undershooting and overshooting, depending on the situation. Now we are in a process somewhat more positive about prices, but that does not allow great enthusiasm to the extent that there is a feeling towards pricing that is the cost of local producers in China. If price starts rising a lot, the trend of these local farmers is to return to the market. Now, there can be an exogenous factor which is the strongest growth in demand in China. Up until now this did not turn into steel production. The Chinese steel industry interrupted the operation of some blast furnaces in the last two or three months for maintenance, they are now resuming production, these blast furnaces, but this is still not a consolidated trend towards demand recovery. I think the most positive impact on prices, we will only feel if there is a stronger growth in steel production in China.

Operator: Our next question is from Mr. Leonardo Corrêa from Barclays.

Leonardo Corrêa: Good morning everyone, thank you. My first question, I actually have two questions for Martins, yet regarding the same topics. First point regarding the production of Chinese iron ore. A few days ago a major competitor of yours publicly said that there would be some indications of capacity reduction of around 100 million tons of iron ore adjusted. I wanted to hear a little from you, if you noticed similar numbers, if there is any number that you are using, or some interesting data point that you are seeing? Because the production data of crude iron ore in China probably is of very bad quality. Since this is a very important variable for pricing and to support the price of ore in the future. I wanted to have a little perhaps update about what's happening with the market of Chinese iron ore, the local producer? And Martins, do you think it is reasonable to expect a 2013 price scenario closer to $100.00 or to $130.00? If you could qualitatively indicate a price range in your opinion. That's the first question. Regarding the second question, sorry to come back to a topic that you somehow have already discussed in the last question. But if you could objectively state your initiatives to reduce the gap between realized price and reference price. Anyway, just so that we could try to understand a little better what we can expect ahead, if this gap between reference price and realized price may continue decreasing. Those are my two questions, thank you.

José Carlos Martins: Regarding your first question, you can easily calculate the displacement of local Chinese ore. If you take the pig iron production in China, which is a public number. You take 1.5 ton for each ton of ore, you get the amount of ore that was consumed. If you take out what they imported, which basically is a proxy of imported ore used in their structure, you have the local ore. So, following such rationale, in fact, the reduction of local ore sales is of that order, 100 million tons. We get this same number. Moreover, data from ore production, to date, indicates an increase in production. But ore production in China is not of final ore, it is basically run-of-mine. It is the crude ore before being processed. Concentrations of Chinese iron ore are falling dramatically. Not necessarily the production of run-of-mine production means equivalent ore production. Since levels are dropping, you end up having less ore.

We have also seen that local ore producers only sell if prices reach a level that is reasonable to them. So, I think there may be local ore storage within China. Because customers are not selling if prices are not within the range of $120.00, $125.00. Actually local ore was being sold, until some time ago, at a price above the imported ore, exactly because of that. So the question here is whether this situation will last, for me it is very much related to the price level. As the price level continues recovering, I believe that much of this Chinese ore will come to the market. So with that I am answering your other question, if I think the price will be above or below the current level. I believe it can have a great volatility in the period. But on average it should not be much different from the current level. If you look around, although ore price has reached $88.00 in the last two quarters, in the third quarter, the average price was in the range of $113.00. And, in this quarter, now, it is in the range of $115.00. In other words, in this quarter that started in September. So we'll have an adjustment mechanism, so the price really goes to a level higher than we are currently seeing, and we will rely on a stronger recovery of Chinese demand, of steel production in China. Up until now, there are signs of recovery, but it is not possible to say that this is a consolidated trend. I'd rather say that, next year, prices will be at the current level, with plenty of volatility in the quarters. We can see prices reaching, eventually, $140.00, $150.00, but we can see them going below $100.00. Because, as I mentioned, you have the destocking of imported ore, it is happening and the steel destocking is also happening. But it is very likely that we have a growth of local ore storage in Chinese mines.

With respect to the measures that we adopt in relation to pricing, we have seen a number of factors that have affected pricing. An important factor, as I mentioned, is the time to market, if I want to sell ore from Brazil, when it leaves the country, as it takes 45 days to get there, I have to offer a bigger discount on prices. I mean, not a discount, the market will offer less. That word “discount” is a word that we do not like to hear. In fact, we do not offer discounts, we sell at market prices. If the market pays more or less is a particular and specific situation. So, we noticed that when we try to sell ore, when it leaves our port, for example, FOB, the customer is willing to pay a lower price. Because it assumes the risk of that time. So we're looking to sell that ore later, closer to the moment our competitors do. Another thing we found is the size of the ships as well. Since in this market you have many customers who, due to cash and working capital problems, do not want to buy large quantities of ore. So, in order to optimize freight, you use large ships, but, on the other hand, at the time of sale, customer ends up offering less for a larger ship. So we have been trying to adjust all of this. The issue of ship size, lot size that is sold, and the issue of time to market. And there's also the quality issue, we have sought to improve the quality of the material we produce. We're managing a greater homogenization of our ore, and this also has an impact. When customer knows that the ore of a given system has greater variability of quality, it tries to reduce its price. So, it is a series of sets, of measures that are helping to improve the price. Now basically there is the market issue, we cannot ignore. In the past, iron units had a much higher value than they do today. If you look at the value of VIU, it fell much more than the ore value fell to 62%, the base ore. This demonstrates that when VIU falls, when the value of iron has a lower pricing, the influence of other contaminants acts otherwise. And this is a situation that, in the previous system we had, the price was set only in view of iron that did not appear. This is a market reality that we are also adapting to, and we are trying to work from a production standpoint to minimize its impact. So it's a series of measures that we have been applying every day that we have been learning and adjusting. But one thing I can assure you, the trend of our performance in this regard is to improve. Not only because of the mines performance, but also because of the market performance, the commercial performance.

Operator: Our next question is from Mr. Marcos Assumpção from Itaú BBA.

Marcos Assumpção: Hi, good morning everyone. First question, with relation to the project of Rio Colorado, if you can give us an update on the project, we saw that a significant amount was invested there in the third quarter. And how do you see this project? What risks do you still see there? How do you see this fertilizer market? And when will you be able to decide whether to actually go ahead with this project or not? And a second question regarding the cost-cutting initiative that you mentioned in the quarter. If you could give us more details on that, what are the key initiatives and eventually when may we begin to feel some of their results? Luciano said earlier, at the beginning of the call, that the portion of SG&A, we should already be seeing a slight decrease or stability in that account. But looking at other initiatives that you commented in a slightly more effective manner this quarter, what we can expect in the future in relation to cost reduction? Thank you.

Luciano Siani: Marcos, thank you. Firstly, in relation to the project of Rio Colorado, you will have a final assessment on Vale Day. We will hold meetings with our shareholders, internally, to reach a decision. We're trying to mitigate all aspects of the project, all risks, institutional and economic, that still exist. We are actively seeking partners for the project. And the combination of all factors, as to know, the feasibility or not of partnerships, plus the possibility or not to mitigate all risks involved in the project, is what will delineate the final decision. And that decision will be taken soon, over the months of October, November. And we will announce it, for sure, on Vale Day at the beginning of December.

With regard to cost savings, we have here, as I was talking about research and development, I mentioned one of the leverages, which is the reduction of mineral exploration, reduction of technological innovation initiatives that are not necessary at this time. I think that reducing the number of projects is an important leverage for reducing R&D, since the engineering development of these projects is classified as research and development and it has a significant impact. Since we already have lots of development projects, we do not need to move so quickly in the engineering of other growth options. With regard to SG&A, I mentioned the readjustment of the Company structure to the new reality. But most of the costs, we know, come from operating costs. And in this case we have some leverage. The first, which already mentioned, are the more structural cost reduction initiatives, in other words, we are reassessing of all our plants and units and individual assets, and challenging those which really do not have an adequate cost performance. In Canada, this has already resulted in the shutting down of two mines. Here in Brazil, we closed these older plants in Tubarão really because of a problem of cost performance. They are not as competitive as newer plants. We're also doing some revaluations in the area of phosphate. We have some older plants where perhaps there may be an optimization, you change the product being sold, or you take the production from one part and take it to another. The industrial flows are quite complex and often in the search for volume, growth, you do not stop to analyze the particularities of each case. What we are doing today is taking assets individually to assess their structural competitiveness. There is also another big change that should bear fruit perhaps within a medium to long term. We are reviewing our entire supply strategy internally. We found that Vale has not been sometimes competitive in hiring, mainly, services of lesser value. We always had an important intelligence of supply devoted to items of great value, big negotiations. But we're attacking in a decisive manner items of lesser value that are very fragmented, but that account for a very significant portion of our expenses. Currently approximately 50% of what Vale spends in its operations are items of small value which had not yet been given a specific approach. This is another initiative that is underway too.

And of course all operations on a daily basis, the managers of each of the units, have this very strong drive, this incentive to pursue cost reduction. We're always looking at what these optimizations are, where we perhaps have some gaps, inefficiencies in every detail. I can say that comprehensive programs to reduce costs at all levels of the Company are happening right now. But if I could highlight things of a more structural nature within operating costs, I would point out the revision of specific assets and the improvement of our profile of supplies for low-value purchases, but which, in the aggregate, are very expressive.

Operator: Our next question is from Mr. Humberto Meireles from Goldman Sachs.

Humberto Meireles: Good afternoon to all. My question is about the management of portfolios of assets in the sale of 600 million related to 10 vessels. How will this be reflected in your statement, looking forward?

Luciano Siani: What we all want is to take this capital base from assets. So there you have two situations from the accounting point of view that is imposed. If you simply imagine that I take the ship Valemax and sell it to a third party and lease it back for a period corresponding to the life of the asset, it is six of one and half a dozen of the other. That is, I get the value of the sale, but I state my long-term lease as if it were a debt. Because I believe that I'm just financing myself based on assets. This is not our goal that is why at the moment we cannot sell the ships Valemax. As they do not have a history in the market, there are no players willing to buy the assets and have them in hand and run lease risks. That is, if I sign a contract with a player who buys a ValeMax ship for 10 years, and this ship has a life of 30 years, it means that after the tenth year, the buyer would be in danger of leasing the ship again in the market. As the ship does not have a history of more widespread use, there is a counterpart in this transaction. So the only possible transaction with a Valemax ship would be to make a sale leaseback for a very long part of its lifetime, which would constitute a debt. And this is not our goal. However, the ships you saw we sell are like Boeings 737, they have great market acceptance and we can make the sale, make a lease for a term inferior to the life of the ship.

José Carlos Martins: And not necessarily of the same ships.

Luciano Siani: And not necessarily of the same ships, this is important. And therefore the residual risk is all with the ship-owner. In fact this is an effective sale of assets and a lease that is classified as operating lease.

So, on the balance, you'll have a really low asset, a cash input and you'll have an increase of expenses of production cost corresponding to the asset lease. Please note that when we operate the asset, we pay for the cost of operation. When you lease, you pay it too, you end up remunerating the capital invested in that ship.

Closing:

Operator: I would like to pass the floor to Mr. Luciano Pires, for his final comments.

Luciano Siani: Well, I hope you are somehow, we have been able to show, through punctual results, here and there, an already consistent trend towards what we have been planning, from the point of view of capital discipline and in terms of strategy. You have noticed that we have adopted a more conservative approach towards disclose, what is in progress, initiatives, we prefer to give the news when they come true, but I believe there already are many evidences and that Vale is determined to adapt in a very consistent manner to a new market scenario. To focus on the return to shareholder, at the expense of other goals and somehow balance this “trilemma” that has been imposed regarding the payment to shareholders, the continued investment program for the generation of long-term value and a prudent leverage. We want to be a strong company. We want to be a company that delivers short-term results to its shareholders. But a company that also has a portfolio, develops and creates value on the long run. This is the goal we are pursuing. And as I said, you can expect a flow of positive news, though we do not anticipate where, but we expect to be able to demonstrate that we are on the path we are promising.

Operator: The Vale conference call is over. Thank you very much for your participation. Have a good day. Thank you.