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VALE

1Q24 Preview: Not so bad, but not good enough

LatAm Metals & Mining

Main takeaways:

(i) S11D performing above expectations; **(ii)** Brucutu ramp-up loses production intensity for pellets, but sales remain strong; **(iii)** Surprising contractual premiums for pellets with a realized price of US$171.9/t (premium of ~US$34/t, +4.7% vs. Genial Est.); **(iv)** Sales gap in relation to nickel production; **(v)** Less relevant interruptions in copper production; **(vi)** Base metals still suffering from the nickel curve, with the realized price falling by -8.5% q/q (-1.3% vs. Genial Est.; -33.3% y/y); **(vii**) Revenue as the only major line expanding y/y. We project net revenue for 1Q24 of US$8.5bn Genial Est. (-34.8% q/q; +0.7% y/y); **(viii)** C1/t should reduce smoothly due to offsetting inverse effects. Our estimate indicates a C1/t (ex. purchase from third parties) of US$23.6/t (+5.1% q/q; -2.5% y/y); **(ix)** Freight costs should show a milder increase than spot, to US$19.5/t Genial Est. (+3.7% q/q; +9.2% y/y); **(x)** Proforma EBITDA projected at US$3.7bn Genial Est. (-43.5% q/q; -0.9% t/t), and an **Adjusted EBITDA** of US$3.3bn Genial Est. (-46.7% q/q; -9.4% **y/y), down high single digits y/y**; **(xi)** We estimate **net income to fall by -20% y/y**, due to **weaker pricing dynamics in fines** and an increase in the pace of provisions for the **Mariana (MG) accident**; **(xii)** We force pessimistic assumptions into the model, in order to attest to the attractiveness of the stock valuation, and yet the **FCF yield** rises to **13%** vs. 11.5%, based on the estimate made in January, due to the **high level of depreciation in shares' value**. Even with so many anchors hindering the stock's traction, we believe that **Vale trades below its fair value,** with a **4.1x EV/EBITDA 24E** (vs. 4.9x historical average). We continue with a **BUY rating** and a **12M Target Price of R$72.30** for **VALE3-B3** and **US$14.30** for **ADRs-NYSE**, indicating an **upside of +17.68%**.

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Company

VALE US Equity
Buy

Price: US$ 11.67 (17-Apr-2024)
Target Price 12M: US$ 14.30 (NYSE)

VALE3 BZ Equity
Target Price 12M: R$ 72.30 (B3)

Vale released its **1Q24 Production and Sales report yesterday** (April 4th) after the market closed. The **realized price for iron ore fines** was US$100.7/t (-14.9% q/q; -7.3% y/y), below the ~US$105/t of last Friday's Bloomberg Consensus and in line with our estimate of a **double-digit sequential downturn**. We anticipated that the consensus was, until last week, more bullish than it should have been with this particular variable. We commented on exactly this dynamic in our Operational Preview report, which is attached (Vale 1Q24: Operational Preview).

Table1. Mostly better figures than Est.

(Thousand Tonnes - kt)	Reported	Genial Est.	
Summary	**1Q24**	**1Q24E**	**% Diff.**
Iron Ore Production	70.837	67.477	**5,0%**
Iron Ore Fines Shipments	52.546	50.595	**3,9%**
Pellets Production	8.467	9.286	**-8,8%**
Pellets Shipments	9.225	9.193	**0,3%**

Source: Genial Investimentos, Vale

Table2. Reported vs. 4Q23 and 1Q23

Reported				
1Q24A	**4Q23A**	**% q/q**	**1Q23A**	**% y/y**
70.837	89.397	**-24,5%**	66.774	**6,1%**
52.546	77.885	**-35,0%**	45.861	**14,6%**
8.467	9.851	**-5,7%**	8.319	**1,8%**
9.225	10.285	**-10,6%**	8.133	**13,4%**

Source: Genial Investimentos, Vale

Genial Est. vs. consensus. It is important to note that **in the last 3 days**, some analysts have updated their estimates for the realized price of iron ore fines compared to their previous projections, and the consensus price for 1Q24 has dropped to ~US$98/t (vs. ~US$105/t previously), converging with Genial Est. However, these changes in estimates by other analysts happened shortly after our publication and in a **very short-time period**. If we look at it from this perspective, the **realized price of US$100.7/t** had an **upside of +2.8% vs. consensus and Genial Est**. We therefore believe that the drop observed in yesterday's trading session (-2.75% for the ADRs-NYSE and -1.20% for VALE3-B3) ended up being due to China's macro data on industrial production (which came in lower than expected), as well as the consensus downgrading estimates for the 1Q24 realized price.

Production and sales. As for **fine iron ore** production, Vale delivered 70.8Mt (-24.5% q/q; +6.1% y/y), **down double digits y/y**, but **up y/y**. Looking at sales, the figure reported was 52.5Mt (-35.0% q/q; +14.6% y/y), consolidating a slightly lower stocking dynamic than we predicted in our model.

The figures for the ferrous division came in with **production and sales in fines slightly above our expectations**, at +5% and +3.9% vs. Genial Est. respectively. Therefore, despite the sequential drop, we believe that the quarter showed a favorable composition of production, even considering the seasonality contrary to the operation, with Q1 marking the periods of highest rainfall. For **pellets**, production was lower than expected (-8.8% vs. Genial Est.), but shipments were perfectly in line (+0.3% vs. Genial Est.). The pellet price was a positive surprise (+4.7% vs. Genial Est.), marking US$172/t (+5.2% t/t; +5.8% y/y).

In the **base metals** division, the realized price for **nickel** came in line with the fall in the LME reference curve, making up a strong reduction of -8.5% q/q and -33.3% y/y, following the trend we expected. In the case of production, Vale exceeded our expectations (+6.6% vs. Genial Est.). For **copper**, production also exceeded expectations (+9.3% vs. Genial Est.). For both commodities, sales came in line.

Valuation and rating. The dynamics of the iron ore fines premium remain anemic. It turned negative in parts of 4Q23 and also in 1Q24. The premium stood at -US$1.6/t (vs. -US$1.3/t Genial Est.), with an even wider discount than we had estimated, and following the deteriorating trend compared to 4Q23 (-US$1.6/t vs. -US$1.1/t). Our expectation was that this situation, combined with the future price provisioning mechanism, would have a **strong negative impact on price realization**. As a result, Vale recorded a price realization in iron ore fines of US$101.7/t (+2.8% vs. Genial Est.), which represents a considerable drop of -14.9% q/q and -7.3% y/y, even though the 62% Fe iron ore curve averaged US$124/t during 1Q24, which would constitute just a mild retraction of -3.1% q/q.

The realized price was in fact slightly above our expectation, regardless of whether Vale earned a premium for quality with more discount. Our analysis suggests that the percentage of sales marked forward was most likely lower than the 24% we estimated, and we already had the assumption that Vale would try to work to lower this percentage, which in 4Q23 was 38%. This justifies the slight upward difference between our price estimate and what was realized. This percentage will only be disclosed in the **financial release**, on **April 24th**.

For more details on how the **forward provisioning mechanism** played a important role in price retraction, we suggest reading our Operational Preview report, which is attached (Vale 1Q24: Operational Preview). In the "Our Take" section, we have explained in detail how this mechanism works, why Vale uses it, and how the simple arithmetic of checking the average of the 62% Fe curve and applying the estimated quality premium on top can lead to a misleading conclusion, especially in quarters of high price volatility, as was the case here.

On the volume side, the level of stockpiles in fines was below what we projected, with shipments exceeding our estimates (+3.9% vs. Genial Est.), which is somewhat in line with the strong data from the Secretariat of Foreign Trade (SECEX), and with the possible upside that we commented on in our operational preview report on production. In other words, this means that production in 1Q24 demonstrates **Vale's good execution capacity** (+14.6% y/y), and that the guidance of 310-320Mt, which implies stabilization vs. 2023, may be underestimated. We are targeting **the middle of the guidance** (315Mt) in our model, and the **good news is that we can revise this figure upwards** over the coming months.

As for **pellets**, the performance was totally in line with the sales side, with production coming in slightly below our estimates. The excellent operational performance in 4Q23 ensured a very satisfactory level of shipments in 1Q24, given the **logistical delay** in the extraction of iron ore fines at the Brucutu mine (MG), which is being ramped up due to the commissioning of the Torto dam, which took place in 3Q23, until it arrives at the pelletizing plant at the Tubarão terminal (ES).

The **positive surprise in pellets came from the price side**, which marked a sequential evolution that we consider attractive (+5.2% t/t), unlike fines. The realized price was US$172/t (+4.7% vs. Genial Est.), doing an appropriate job of contract negotiations (which are less dependent on the situation in China), extracting a premium of US$34/t (+8.2% vs. Genial Est.), increasing the spread for the high grade iron ore price curve (65% Fe) to 24.2% (+9.6p.p q/q), a result above our expectations. We stress that our estimates already included a sequential upward movement in the premium, which became the first since 2Q23.

The effect we expect from these divergences vs. our previous estimate on revenue is an improvement to R$8.5bn Genial Est. (+5% vs. Old Est.), as the **higher realized price in pellets and higher volume of shipments in fines**, both vs. our previous estimates, **partially offset our pessimism about the realized price in fines**. We believe that the increase in the agglomerate's premium shows the **strength of Vale's strategy** to sell **blended and high silica** products, helping to offset the downward trend in the price of iron ore in the medium quality benchmark (62% Fe). In addition, a slightly higher volume of sales in fines (+3.9% vs. Genial Est.) could improve fixed cost dilution capacity and slightly lower our C1/t estimate.

Updating projections... As a result, our projection for adjusted EBITDA is now US$3.3bn Genial Est. (+8.6% vs. Old Est.), **up a high-single digit** on **our estimate** (equivalent to +US$270mn vs. Old Est.). Even so, **the quarter was still challenging**. This updated EBITDA projection still infers a drop of -34.7% q/q and -9.4% y/y.

Table3. New 1Q24 Est. vs. Old one

(US$ millions)	Genial Est.	Old Est.	
Income Statement	**1Q24E**	**1Q24E**	**% Diff.**
Net Revenue	8.512	8.108	**5,0%**
Adjusted EBITDA	3.355	3.088	**8,6%**
Net Income	1.618	1.396	**16,0%**

Source: Genial Investimentos

Table4. New 1Q24 Est. vs. 4Q23 and 1Q23

Genial Est.				
1Q24E	**4Q23A**	**% q/q**	**1Q23A**	**% y/y**
8.512	13.056	**-34,8%**	8.454	**0,7%**
3.355	6.290	**-46,7%**	3.703	**-9,4%**
1.618	2.480	**-34,7%**	2.040	**-20,7%**

Source: Genial Investimentos, Vale

Vale is discounted, and here's why:

We remind you once again that our financial modeling has become even more rigorous since our sector report published at the beginning of the month (Metals & Mining: Has China's economic model run out of steam?), which has reduced the 12M Target Price by -US$2.25 for ADRs-NYSE or -R$10.20 for VALE3-B3. The changes in assumptions led to a cut in the FCFF generation forecast to US$6.8bn (vs. US$7.2bn previously), now adjusted with the additional +US$270mn of EBITDA for 1Q24 vs. the old Est.

Still, interestingly, the **24E FCF yield improved**, now reaching **13%** vs. 11.5%, this time based on the estimate made in January. This improvement occurred as Vale's share price fell from ~R$60.00 vs. ~R$70.00 in the same period (Jan-Apr), or to ~US$11.70 in the NYSE ADRs vs. ~US$14.30, **suggesting a notable undervaluation of the company by the market**. Thus, despite the downward-biased adjustments in our model, **Vale still displays solid financial metrics**.

Currently, the company trades at **4.1x EV/EBITDA 24E** (vs. 4.9x historical average)**, which seems discounted** considering that **we are using purposely pessimistic assumptions** to deliberately force cash flow generation down. Despite the uncertainties linked to **(i)** China, **(ii)** the Mariana (MG) agreement and the railroads (EFVM and EFC), as well as **(iii)** government pressure amid attempts at political intervention in the company's management (suspension of the Onça Puma and Sossego licenses), we maintain our confidence in the operating performance. We continue to our **BUY rating**, with a **12M Target Price of R$72.30** for **VALE3-B3** or **US$14.50** for **ADRs-NYSE**, which represents an **upside of +17.68%**.

1Q24 Preview: In detail!

Now we'll go into more detail about what we think of the operating figures the company released yesterday, as well as what investors can expect from the **financial release** on **April 24th**.

S11D performing above expectations. As a result of the weaker seasonality typical of Q1, due to the torrential rains that come after warmer temperatures at this time of year, the company reported production volumes down by -24.5% q/q, at 70.8Mt (+5.0% vs. Genial Est.) but up by +6.1% y/y, due to the ramp-up of production. This year-on-year growth can be attributed especially to the performance of S11D, which delivered excellent production of 17.7Mt (+4.5% vs. Genial Est), up +8.5% y/y and exceeding our expectations.

We also saw a slight improvement at Itabira and a significant re-establishment at Vargem Grande (southeastern and southern system) on an annual basis, as well as the return of activity at the Ponta da Madeira Terminal (MA), which had been suspended during 1Q23 and is responsible for transporting i.o. from the northern system. This factor helped weaken the y/y base and make it easier to overcome in terms of shipments, which totaled 52.5Mt (+3.9% vs. Genial Est.), up +14.6% y/y, despite the sequential drop of -35% q/q, because of seasonality.

Table 5. Production Summary Vale (1Q24 vs. Genial Est.)

Vale Production Summary (Kt)	1Q24 Reported	1Q24E Genial Est.	% R/E
Iron Ore[1]	70.837	67.477	5,0%
Pellets	8.467	9.286	-8,8%
Nickel	39,5	37,0	6,6%
Copper	81,9	75,0	9,3%

Production Summary (Kt)	1Q24 Reported	4Q23 Reported	% q/q	1Q23 Reported	% y/y
Iron Ore[1]	70.837	89.397	-20,8%	66.774	6,1%
Pellets	8.467	9.851	-14,0%	8.319	1,8%
Nickel	40	45	-11,8%	41	-3,9%
Copper	82	99	-17,3%	67	22,2%

[1] Including third-party purchases, run-of-mine and feed of other pelletization plants.

Source: Genial Investimentos, Vale

Brucutu ramp-up loses intensity in pellet production, but sales remain strong. Following the ramp-up of the commissioning of the Torto dam in Brucutu (MG), we observed a marginal increase of +1.8% y/y, to reach 8.5Mt (-8.8% vs. Genial Est.), with a drop of -14.0% q/q in pellet production, measuring a production performance below our expectations. In terms of shipments, Vale reported an increase of +13.4% y/y, reaching 9.2Mt (+0.3% vs. Genial Est.), comprising a reduction of -10.3% q/q. We would point out that the sequential impact was not as intense as that seen in iron ore fines, just as we had anticipated in our operational preview report.

We believe that the company took advantage of the good volume of iron ore fines produced in the previous quarter, attesting to the logistical delay until the cargo arrived at the Tubarão Terminal (ES) and the subsequent pelletizing process. Therefore, according to our analysis, a representative part of the good sales performance in pellets observed in 1Q24 is actually correlated with the strong production of fines in 4Q23.

Pellet contract premiums are a positive surprise. The realized price for pellets was US$171.9/t (+4.7% vs. Genial Est.), up +5.8% y/y and +5.2% q/q, together with an implicit premium of ~US$34/t (+4.7% vs. Genial Est.). This figure was calculated using the weighted average premium of US$3.6/t reported by Vale, demonstrating that even though we were right about the sequential growth trend, we were faced with a positive surprise, since we had expected this same dynamic, but with less intensity. The reason for such a different performance of iron ore fines is related to the dispersion of pellet demand, which is more relevant in the USA, Europe, Japan and the United Arab Emirates. A more detailed explanation can be found in the Operational Preview report (link).

Table 6. Shipments Summary Vale (1Q24 vs. Genial Est.)

Vale Shipments Summary (Kt)	1Q24 Reported	1Q24E Genial Est.	%R/E
Iron ore fines	52.546	50.595	3,9%
Pellets	9.225	9.193	0,3%
ROM	2.056	1.665	23,5%
Nickel	33,1	33,3	-0,7%
Copper	76,8	73,5	4,5%

Shipments Summary (Kt)	1Q24 Reported	4Q23 Reported	% q/q	1Q23 Reported	% y/y
Iron ore fines	52.546	77.885	-32,5%	45.861	14,6%
Pellets	9.225	10.285	-10,3%	8.133	13,4%
ROM	2.056	2.158	-4,7%	1.665	23,5%
Nickel	33	48,0	-31,0%	40,1	-17,5%
Copper	77	98,0	-21,6%	62,7	22,5%

[1] Including third-party purchases

Source: Genial Investimentos, Vale

Widegap in nickel production vs. sales. The volume of nickel produced was slightly above our expectations, registering 40Mt (+6.6% vs. Genial Est.), showing a reduction of -11.8% q/q and -3.9% y/y. This drop was due to maintenance stoppages in the furnace at the Onça Puma (~9.5 weeks). We observed a gap to production, in line with our previous analysis. Two factors explain this difference: **(i)** the Onça Puma plant had zero nickel productivity, but the mine continued to extract and generate feed inventory as we had anticipated and **(ii)** Vale had already announced its maintenance stoppages for the current year and in 2Q24 there will be stoppages at some units in Canada, leading it to stockpile a fraction to fulfill contracts in the following period. As a result, the volume of shipments reported was 33.1Kt (-0.7% vs. Genial Est.), perfectly in line with our projection, marking a drop of -31% q/q and -17.5% y/y.

Less significant interruptions in copper production. In copper, interruptions related to maintenance or renovations were less relevant (<1 week) and there are no non-standard scheduled breaks. As a result, the vector in production was the opposite of that seen in nickel, growing +22.2% y/y to 81.9Kt (vs. 75Kt Genial Est.), despite the -17.3% q/q drop, which was due to the seasonal effect of the winter season on copper production from Thopmson in Canada.

In addition, there were no surprises in terms of sales volumes, with 76.8Kt shipped (+4.5% vs. Genial Est.), a fall of -21.6% q/q, and a rise of +22.5% y/y, mainly due to the ramp-up of Salobo 3, whose plant reached an average processing rate of 90%, and sales kept pace with production.

Base metals still suffering from the nickel price curve. Following the trend of the LME reference curve, and in line with our expectation, the realized price for nickel fell by -8.5% q/q to US$16,848/t (-1.3% vs. Genial Est.), a sharp decline of -33.3% y/y. Once again, the downside of oversupply seems to have been priced in and we therefore we expect the price to stabilize at this level throughout the year. Regarding copper, we saw slight progress in the realized price, rising smoothly by +1.1% q/q, despite the -18.8% y/y drop, to reach US$7,687/t (-3.4% vs. Genial Est). We expect an upside for copper as a result of the increase in demand and the pace of stockpiling in China.

Revenue as the only major line expanding y/y. Breaking down the top line, we are projecting revenues for iron ore fines at US$5.2b Genial Est. (-42.6% q/q; +6.2% y/y), with a sequential reduction due to seasonality and an increase on an annual basis due to the resumption of shipments through the Ponta da Madeira (MA) terminal. The same dynamic can be seen in pellets, which should record revenues of ~US$1.6bn Genial Est. (-5.6% q/q; +20% y/y). This time, the year-on-year growth is correlated with the ramp-up of the production of fines, especially in Brucutu (MG), and the subsequent logistic transfer to the pelletizing plant. Regarding base metals, we estimate revenues from nickel operations at US$901mn Genial Est. (-23.5% q/q; -40.3% y/y) and copper at US$590mn Genial Est. (-31% q/q; +12.7% y/y).

Looking at the consolidated dynamics, we project net revenue clocking in at 1Q24 of US$8.5bn Genial Est. (-34.8% q/q; +0.7% y/y). We see the pellet operation as a major positive highlight, which recorded a surprising premium and helped the company to achieve top line growth on a year-on-year basis.

Table 7. Net Revenue Vale (1Q24 Genial Est.)

(US$ millions)	1Q24E Genial Est.	4Q23 Reported	% q/q	1Q23 Reported	% y/y
Net Revenue	**8.512**	**13.056**	**-34,8%**	**8.454**	**0,7%**
Iron Ore Fines	5.291	9.214	-42,6%	4.982	6,2%
Pellets	1.586	1.681	-5,6%	1.322	20,0%
Nickel operations	901	1.177	-23,5%	1.509	-40,3%
Copper operations	590	855	-31,0%	524	12,7%
Others	144	180	-20,2%	117	22,8%

Source: Genial Investimentos, Vale

C1/t should reduce slightly due to compensatory effects. If we analyze the C1/t cost of the same period last year, we can see some effects that should be reversed this quarter, but in the end will probably create a net improvement effect of only slight intensity. In 1Q23, Vale had disclosed some one-off cost eventualities that included the anticipation of maintenance activities, since shipments were restricted due to the temporary flow interruption at the Ponta da Madeira Terminal (MA). We believe that this effect, which penalized the cost in 1Q23, should disappear in 1Q24. In addition to this factor, the volume of production and shipments growing y/y should help in the dilution, this time of fixed costs, creating a vector directing C1/t downwards. On the other hand, the exchange rate should play against it now. At the time, the BRL/USD exchange rate was ~R$5.20 and we saw an average of R$4.95 in 1Q24. As the company has contracts signed in BRL, a devaluation of the BRL/USD exchange rate will result in a lower capacity to dilute these costs due to the disparity in the strength of the two currencies. We therefore estimate a C1/t (ex. purchase from third parties) of US$23.6/t Genial Est. (+5.1% q/q; -2.5% y/y).

Freight costs should rise more slowly than spot. Freight is unstable due to the conflicts observed in the Middle East and has increased the spot price of SSY (Shark-Qingdao) by +US$7/t on an annual basis, reaching ~US$26/t (+2.0% q/q; +43% y/y). Of course, conflicts indirectly affect freight costs by making bunker (vessel fuel) more expensive, for example, but our intention is to show that the effect on Vale is less than you might think. This is because the company has less exposure to spot freight, adopting long-term contracts with shipowners, which follow price adjustment dynamics that are different from the volatility of the spot market. Our projection for freight costs is US$19.5/t Genial Est. (+3.7% q/q; +9.2% y/y).

Total nominal cost up slightly y/y, down y/y due to volume reduction. Our estimate suggests that the consolidated nominal cost will rise slightly by +0.3% y/y, with a reduction of -27.6% q/q driven by the seasonality of production and sales. We project a consolidated nominal COGS of US$4.9bn Genial Est. We highlight that, excluding seasonality in the sequential movement, we estimate an annual increase to mark a COGS of US$328mn in copper (+21.3% y/y), in line with the dynamics presented in the company's guidance.

EBITDA likely to shrink y/y. Although Vale has shown interesting production and sales figures, Proforma EBITDA should contract superficially on an annual basis, reaching US$3.7bn Genial Est. (-43.5% q/q; -0.9% y/y). This is mainly due to **(i)** the weakened price dynamics faced in the iron ore fines operation, which once again showed a negative premium (-US$1.6/t), **(ii)** the increase in total nominal costs (driven by a mechanical cost increase in copper operations, for example) and **(iii)** the increase in depreciation, due to the upsurge in the asset base y/y.

On the other hand, our projections prior to the release of the production and sales report were more pessimistic, and one of the main factors in dampening this sentiment was the good price performance achieved for pellets. As a result, our forecast for adjusted EBITDA is now US$3.3bn Genial Est. (+8.6% vs. Old Est.), equivalent to +US$270mn vs. Old Est. This projection corresponds to a reduction of -46.7% q/q and -9.4% y/y.

Table 8. EBITDA Vale (1Q24 Genial Est.)

(US$ millions)	1Q24E Genial Est.	4Q23 Reported	% q/q	1Q23 Reported	% y/y
Proforma EBITDA	**3.780**	**6.686**	**-43,5%**	**3.814**	**-0,9%**
Iron Ore Fines	2.668	5.467	-51,2%	3.320	-19,6%
Pellets	842	925	-8,9%	667	26,3%
Nickel operations	214	152	40,5%	353	-39,5%
Copper operations	239	375	-36,2%	220	8,8%
Others	(184)	(233)	-21,1%	(746)	-75,4%

Source: Genial Investimentos, Vale

We project net income down -20% y/y. After a shrinking EBITDA and a projected flat financial result y/y, we estimate net income clocking in at US$1.6bn (-34.7% q/q, -20.7% y/y). The larger drop gap in net income in relation to EBITDA is due to the increase in the rate of provisioning, which should be allocated to the non-controlling shareholders line, for Samarco, a JV that has Vale and BHP as equal partners (50% each) and which operated the Fundão dam that collapsed in 2015, in Mariana (MG). We project a US$270mn Genial Est. provision for 1Q24 related to this particular case and point out that in 1Q23 Vale did not pass through a significant amount in this line of the P&L, causing estimated net income to fall more strongly year-on-year.

Table 9. Income Statement Vale (1Q24 Genial Est.)

(US$ millions)	1Q24E Genial Est.	4Q23 Reported	% q/q	1Q23 Reported	% y/y
Net Revenue	**8.512**	**13.056**	**-34,8%**	**8.454**	**0,7%**
COGS	(4.964)	(6.855)	-27,6%	(4.949)	0,3%
Adjusted EBITDA	**3.355**	**6.290**	**-46,7%**	**3.703**	**-9,4%**
EBITDA Margin (%)	39,4%	48,2%	-8,77p.p	43,8%	-4,39p.p
Adjusted EBIT	**2.658**	**5.435**	**-51,1%**	**3.047**	**-12,8%**
EBIT Margin (%)	31,2%	41,6%	-10,41p.p	36,0%	-4,82p.p
D&A	(697)	(855)	-18,5%	(656)	6,3%
Financial Result	(530)	(874)	-39,4%	(530)	0,0%
Net Income	**1.618**	**2.480**	**-34,7%**	**2.040**	**-20,7%**
Net Margin (%)	19,0%	19,0%	0,02p.p	24,1%	-5,12p.p

Source: Genial Investimentos, Vale

Our Take on Vale

Vale reported **good production and sales figures**, showing an increase in the vast majority of its product mix. The big surprise was the realized price of pellets, while the big disappointment (within our expectations) came from the realized price of iron ore fines.

With major **uncertainties about the macroeconomic** environment that directly involves the company's pricing, i.e. China and the iron ore curve, we believe that still will be many doubts about the realized price of iron ore fines going forward. Everyone already knows that there is distrust of Chinese demand for iron ore, but to see Vale once again register a **negative premium**, this time of -US$1.6/t, **widening the discount**, poured cold water for investors.

Are the overhangs really getting in the way of the stock performing well? It's clear that these interferences are detrimental to the company, given that they not only affect investor confidence, but also now have a direct influence on the operation. Unfortunately, we recently witnessed the removal of the injunction holding up the licenses for operations at two mines, Onça Puma (with a focus on nickel) and Sossego (with a focus on copper), following a request for suspension by the Pará State Environmental Secretariat (SEMAS). Our understanding is that this is caused by pressure from the central government, which intends to use subterfuge to potentially pressure the board of directors to select a candidate to replace Mr. Bartolomeo as CEO from 2025. The state filed an appeal with the Court of Justice of the State of Pará (TJPA), in the second instance, canceling the effect of the injunction withdrawn in the first instance, and ceased the order to stop activity at both mines.

However, it's important to point out that we no longer believe that the overhangs are preventing the shares from being carried out to such an intense degree. For illustrative purposes, we can assign a weighting of ~90% to macro issues (China and iron ore prices) and ~10% to overhangs alone. In our sector report, we made several graphical comparisons of the fall in Vale's shares vs. the slowdown in the iron ore curve. And the values are very close.

This means that Vale does have an influence from overhangs, but the great pessimism in the stock seems to us to be more linked to questions about the uncertainty of China's economy and **investors' suspicions about a structural short in iron ore**, given that China's situation does not seem cyclical, but permanent, due to the oversupply of real estate and the decline in the population, inverting the age pyramid. In the short term, iron ore seems to be more linked to supply constraint dynamics, which can generate upside spikes, as we saw with the recovery of the v-shaped curve last year. However, this doesn't free the case from the question of where all the steel that will no longer be consumed in the real estate market will go? We comment more on this situation in our sector report, which is attached below (Metals & Mining: Has China's economic model run out of steam?).

Dividends affected. In our model, the **24E Dividend Yield** is now **~9% Genial Est**. (vs. 10.2% previously). This is due to the **tougher assumptions** we are using in our projections, such as the iron ore curve 62% Fe below consensus, the payment of complementary grants on the EFVM and EFC railroads, and the Mariana (MG) agreement. Both of these situations end up reducing the level of FCF, thus jeopardizing the payment of dividends, as we described further in the Operational Preview report. **For 1Q24**, we are projecting a payment of **~US$0.32/share** (or **~R$1.65/share** for VALE3-B3), which would suggest a **yield of 2.7%**.

Not so bad, but not good enough. We constructed the worst-case scenario we could imagine in order to testify the attractiveness of the shares valued at today's standards, even with so many anchors hindering its traction. The realized price of iron ore fines was indeed weak, but as some analysts quickly changed their values, lowering their estimates in the last 3 days on Bloomberg, the consensus value ended up being more depreciated than that reported by Vale. So, the price situation for 1Q24 isn't too bad, but it's also not good enough to guarantee a result with growth in EBITDA and net income either.

Still, the company is trading at **4.1x EV/EBITDA 24E** (vs. 4.9x historical average)**, which seems discounted** considering that **we are using purposely bearish assumptions** to deliberately force cash flow generation down. Despite the uncertainties linked to **(i)** China, **(ii)** the Mariana (MG) agreement and the railroads (EFVM and EFC), as well as **(iii)** government pressure amid attempts at political intervention in the company's management (suspension of the Onça Puma and Sossego licenses), we maintain our confidence in the operating performance. We continue with our **BUY rating**, with a **12M Target Price of R$72.30** for **VALE3-B3** or **US$14.50** for **ADRs-NYSE**, which represents an **upside of +17.68%**.

Appendix: Vale

Figure 1. Vale – Income Statement in US$ Millions (Genial Est. 2024-2029)

Income Statement	2024E	2025E	2026E	2027E	2028E	2029E
Net Revenue	**37.042**	**41.292**	**42.126**	**43.842**	**44.830**	**48.448**
(-) COGS	(23.944)	(26.237)	(26.383)	(27.586)	(29.085)	(31.495)
Gross Profit	**13.098**	**15.055**	**15.743**	**16.257**	**15.745**	**16.953**
(-) Expenses	(3.420)	(3.321)	(3.160)	(2.765)	(2.418)	(2.559)
Adjusted EBITDA	**12.824**	**15.437**	**16.030**	**17.078**	**17.049**	**18.243**
(-) D&A	(3.192)	(3.356)	(3.512)	(3.661)	(3.802)	(3.936)
EBIT	**9.633**	**12.081**	**12.518**	**13.417**	**13.247**	**14.307**
(+/-) Financial Result	(1.943)	(2.033)	(2.254)	(2.277)	(2.260)	(2.326)
(-) Taxes	(889)	(1.275)	(1.395)	(1.563)	(1.567)	(1.742)
Net income	**6.801**	**8.773**	**8.869**	**9.578**	**9.420**	**10.239**
Profitability						
Net margin (%)	18,36%	21,25%	21,05%	21,85%	21,01%	21,13%

Figure 2. Vale– Cash Flow in US$ Million (Genial Est. 2024-2029)

Cash Flow (FCFF)	2024E	2025E	2026E	2027E	2028E	2029E
Net Revenue	**37.042**	**41.292**	**42.126**	**43.842**	**44.830**	**48.448**
(-) COGS	(23.944)	(26.237)	(26.383)	(27.586)	(29.085)	(31.495)
Adjusted EBITDA	**12.824**	**15.437**	**16.030**	**17.078**	**17.049**	**18.243**
Adjusted EBIT	**9.633**	**12.081**	**12.518**	**13.417**	**13.247**	**14.307**
(-) Taxes	(889)	(1.275)	(1.395)	(1.563)	(1.567)	(1.742)
(+) D&A	3.192	3.356	3.512	3.661	3.802	3.936
(+/-) Brumadinho and Samarco	(1.988)	(1.446)	(1.204)	(915)	(875)	(733)
(+/-) Δ WK	3.404	831	140	(27)	(149)	(51)
(-) Capex	(6.500)	(6.500)	(6.500)	(6.500)	(6.500)	(6.500)
FCFF	**6.852**	**7.048**	**7.071**	**8.074**	**7.958**	**9.216**

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Neutral	Expected return between +10% and -10% relative to the Company's industry average	**41%**
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under Review	Under review	**5%**

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