

Alcoa Corporation

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Christopher LaFemina: Hi, everybody. Thank you for dialing in to this session. It's my pleasure today to host Bill Oplinger, who is the Executive Vice President and CFO of Alcoa. Obviously, lots going on at Alcoa. The format for this is going to be fireside chat. I think Bill is going to kick it off with just some comments about some recent news flow and about what's going on with Alcoa, and then we'll get into some of the more detailed questions I have.

But with that, Bill, I'm going to pass it off to you. And thanks a lot for taking the time today. We appreciate this, but happy to hear what you have say.

William Oplinger: Thanks, Chris. So yes, I'll just have some brief opening comments. If you don't know us, Alcoa, we originated in 2016. We were spun out of Alcoa, Inc. We have three lines of business. We have a bauxite business that's very large and low-cost, geographically dispersed. We've got a refining business that – it's also very large, also very low cost, some of the lowest cost refineries in the world. A smelting business. We've been working to reposition. It's a second quartile business on the cost curve. But in this type of a market environment, it's very profitable.

When I address the market environment, pretty strong dynamics in the market today. Some of the strongest supply/demand dynamics I've seen over the course of 20 years. Ten percent demand growth on a year-over-year basis, and we're starting to see both some near-term and longer-term supply side constraints. In the near-term, we've seen some issues in the refinery industry, and a couple of issues there have restricted supply. When we look at the longer-term, it's in the smelting side of the business. It's really around the fact that Chinese smelting industry has started to constrain supply, and we believe that the 45 million metric tonne capacity restraint that they have in place will remain in place and drive some better industry dynamics.

We then transition to Alcoa. Chris and I were just chatting before this call. Alcoa has made tremendous strides over the last five years. We've been very focused on fixing the balance sheet. Proportional net debt levels are within our target range now. We've done a lot of work around the pensions. Global pensions are greater than 90% funded. U.S. pension is approximately 100% funded. So the pension overhang that we had over the last few years is essentially completely handled at this point. And we have a [\$1] billion prefunding balance built up in our U.S. pension.

So we will not have to fund our U.S. pensions for a number of years. We finished the second quarter with \$2.1 billion of proportional net debt, so within our target range of 2 [billion] to 2 and a half [billion]. Getting many, many questions from investors about what's next around capital allocation. And so at this point, we have a pretty strong balance sheet. We would like to maintain that strong balance sheet through the cycle. The target net debt range, from time to time, we've been higher. I can foresee that we could potentially be lower than our target net debt range in this type of market environment.

That leaves three areas for capital allocation. Asset repositioning, which is one of the announcements that we made today, which I'll address next. We've made some good strides on asset repositioning over the last three or four years. We curtailed Intalco. We closed the Point Comfort facility. And today, we just announced the restart of the Alumar smelter down in Brazil, and I'll address that. The other areas for future capital allocation: shareholder returns and then growth. At this point, we don't have large shovel-ready growth projects.

We do have some smaller opportunities for growth. But at this point, we've talked to investors over the last year or two around some mid-sized growth projects in the refining business, but those are on hold at this point because they don't meet the return hurdles that we would be looking for.

If I transition to the news that we put out today, we announced that we're restarting the Alumar smelter. Our share of that smelter is 268,000 tonnes, and we're restarting it on our own. So not the entire smelter is being restarted. Just the Alcoa share. I want to reiterate the point that it is a low-cost smelter. When we curtailed it back in 2015, we curtailed it primarily for two reasons: high energy costs and a very weak U.S. dollar.

And since that time, we've been able to secure long-term power contracts that start in 2024. They're 100% sustainable renewable energy. And the power contract will position that plant to be very low cost in the future. Reason why it's low cost, it's co-located with the refinery that's there. We have a great workforce. It's good technology. We have some VAT tax benefits that we will be able to monetize. Those are VAT tax that have been on our balance sheet. We'll be able to use those VAT tax benefits going forward. That also adds to the benefit of restarting the smelter.

And then lastly, it will serve a short Brazilian market. The Brazilian market has become short and has to import metal units, and we will be able to serve largely those metal units in Brazil. So overall, a great – another great step forward on the repositioning of the portfolio. We've taken a curtailed asset that was costing us money on a monthly basis. We're going to invest \$75 million to restart it. We'll have it fully restarted by the end of next year, and it will be generating good EBITDA and have a very quick payback. So exciting news there.

Lastly, I'll touch on the third quarter. And we think the third quarter is going to be another record quarter for Alcoa. We had a record quarter in the second quarter. We think that the third quarter should be around \$100 million of EBITDA better than the second quarter. That includes the negative impact of an outage that we've had at the Alumar refinery, where we had to curtail capacity there due to the failure of the ship unloader. That's going to cost us \$25 [million] to \$30 million in the quarter, but that \$100 million better than I referenced already included the negativity from that reloader.

One other thing that's important, Chris, for investors to know about us is that we're fully exposed to alumina and aluminum prices. We don't forward hedge at this point. So unlike some of our competitors, we are completely exposed to what's going on in the market, which, today, is a very positive thing. And lastly, around the third quarter, the better earnings means that we'll pay more taxes. So we're upping our tax expense in the third quarter from \$100 million to \$125 million, which isn't necessarily a bad thing.

So if I summarize, very exciting times in the industry. Exciting times to be part of Alcoa. We think there's positive short and long-term market factors and the company's really positioned for success, and we've changed a lot over five years. We're positioned to do well in today's market environment but much better positioned for the cycle.

So at this point, Chris, I'll turn it back over to you.

Christopher LaFemina: Thanks for that, Bill. So you talked about the hard cap on Chinese smelting at 45 million tonnes. And obviously, that's a function of this focus on the environment, which is not just the focus in China, but it's a focus globally. And ESG, in general, obviously, in the world of the metals and mining has become a critical factor. So can you give us a little bit kind of color as to how – first of all, how you're positioned from an ESG perspective and how that might change over time in terms of using renewable energy, green premiums, et cetera? And with that, the aluminum industry is kind of front and center in the case of global decarbonization. So how does that fit for Alcoa?

William Oplinger: It's really interesting, Chris. The aluminum industry is not only front and center on the carbon side. I think our industry is front and center on many of the global ESG issues. If we start in bauxite mining, there's indigenous people's rights issues. We have an indigenous people rights policy. I think we've done this very, very well. We've engaged with our communities for a long period of time. And as you and I have discussed, even before ESG was popular, we were engaging with our communities 20 years ago.

If we then go to the refining part of the business, impoundments is a big issue after some of the problems that we've seen in some of the other companies around impoundments. We have been very focused on the impoundments over the last 20 years and feel good about our position there.

Carbon. We've got the broadest low-carbon portfolio of products out of any major supplier out there. We, on our smelting business, are one of the lowest carbon intensity producers of any of the major companies. In the refining business, because our refineries are largely gas fired, we are the lowest carbon producer from an intensity perspective out of any refining company out there. So we're well positioned on the carbon side.

And then if we go to the G part of ESG on governance, five years ago, we made a very decided view to make Alcoa Corp. have world-class governance. When we launched the company, we decided to have a declassified board. We split the Chairman and the CEO role. We had proxy access from the very start. So very – we're Delaware incorporated – so very, very strong governance. So interesting times, Chris, because I think some of the things that we have been doing are actually going to get recognized. If you then transition to – Okay. So Alcoa has been doing a lot of the right things. How do you actually provide a return for shareholders based on having done the right things?

I think there's probably four different ways that we can provide a return to shareholders. First, there is a developing green premium for our products. It's small. It's just starting. But over time, we think that green market for – the market for green aluminum and green alumina will get bigger and premiums will get larger. Second, carbon – having an implied carbon cost in the cost curve, and we're starting to see that in places like Europe. There's a Chinese emissions trading scheme, will drive a steepness of the cost curve. And given the fact that we're in the first or second quartile for all parts of our business, a steeper cost curve should mean that we generate better returns.

Third, over time, even though we don't have large growth projects today, I think positioning ourselves as an ESG leader will allow us to be invited into some of the best projects around the world. That's not happening today. We don't have large greenfield plans in the near-term. But over time, as this becomes more important, we – I think we'll be well positioned.

And then fourth, but not least, technology. We have the ELYSIS™ technology, along with Rio Tinto, no carbon smelting technology, inert anode. We've been working on it for a long period of time now. Coming up in 2024, we're projecting to have a commercial package in 2024. It's still an R&D project. But if that works, if it scales up, it will be an absolute game changer in our industry. And we and Rio will be the ones that have that technology. So those are the four ways that we monetize the value of ESG.

Christopher LaFemina: And in terms of – so you talked about the steepening of the aluminum cost curve. So just kind of to talk about the markets in general here. So is it a function of a steepening cost curve, which seems like it's highly likely to happen, but also a function of kind of renewed supply constraints. I mean getting – permitting to build these things is going to be much more difficult. If you think back the last 20 years, China basically built smelters quickly, right. There was no limitation to their ability to bring capacity online. But now that is a major limiting factor, which is around carbon emissions from smelters.

So is it possible that we're actually – if you look at the aluminum price versus the margin cost of production, the first point is that the marginal cost will rise. But the second point maybe that the price on average from the cycle is in a bigger premium to marginal cost and has been historically because it takes longer for the industry to respond with more supply when times are good. So do you think there's some validity around kind of the industry structure being very different and potential deficits lasting for longer and prices being far above cost curve for longer? We've seen that in other commodities but not really aluminum historically.

William Oplinger: Yes. So I do believe that both in the near-term and in the longer-term, market factors in our industry are driving substantial changes. I think we're at an inflection point in our industry. As I said earlier, the Chinese are – the Chinese industry is getting serious about reducing the growth in the industry and focusing on both the carbon emissions but also on the electricity usage. And as you know, China has launched this dual control mechanism for their provinces that looks at total electricity usage plus the intensity of the electricity per unit of GDP.

We think that's a favorable for the industry. And in the refining business, as we look forward, the growth in the refining business, as we see it over the next decade, is largely coal-based. And you have to look at that and say how much of those coal-based projects will get done over the next decade? And will there be an opportunity for really new technology that decarbonizes the refining business. So I think, Chris, that we're at an inflection point. Things are changing. Some of the market factors are really lining up for a stronger situation.

Christopher LaFemina: So how do we think about the kind of big picture in terms of Alcoa's overall position. Your balance sheet has gone from being an overhang to being a positive. Your portfolio has been cleaned up materially. You seem to be operating relatively well. You have some organic growth optionality, but it's not very capital intensive and it's kind of on the back burner for now. When you're potentially going to generate lots of cash flow, right?

So obviously, the – reinstating some sort of capital return program, it seems like a logical next step. But what do you do when you kind of have a potentially embarrassment of riches here where you're generating lots of cash flow and don't really have capital-intensive projects to deploy that cash. Is it about larger capital returns? Is it about looking for growth optionality elsewhere? Is it about – I mean, probably not going downstream – but in terms of kind of capital allocation is bigger picture for this period's high prices and strong cash generation for Alcoa.

William Oplinger:

Right. So we have a four-pronged capital allocation program, and it really starts with a couple of ideals. First, we make sure that we sustain the plants that we have. So we spend money on sustaining capital. Secondly, we will maintain a strong balance sheet. We have had a targeted net debt of 2 [billion] to 2 and a half [billion]. Like I said, we are at 2.1 [billion] in the second quarter. And we will most likely be below that in the third and the fourth quarter, given the strength of the cash generation that we're seeing under today under current market conditions.

After that, we look at the three areas of capital allocation, growth, repositioning the portfolio and shareholder returns. The repositioning of the portfolio, when we announced it two years ago, I think investors were thinking, "Oh, that's going to cost these guys \$1 billion to reposition the portfolio. They need to shut down all of these plants." We've executed now on about half of the smelting portfolio, and it's not cost us much at all. We curtailed the smelter in Intalco, but we repowered Portland, put Portland in a position to be successful for the next five years. And after that, be successful based on renewable energy potentially. We're announcing today the restart of Alumar.

So this massive amount of spend that I think investors were anticipating for the repositioning hasn't panned out yet, which leaves us with shareholder returns. We're going to be very thoughtful about shareholder returns. I get asked a lot of questions from investors around shareholder returns. We just hit our net debt target at the end of the second quarter. So there'll be more information forthcoming about capital returns, but we'll be very thoughtful.

Christopher LaFemina: Thank you for that. So it's – if you talk about the steepening of the cost curve, which is partially a function of carbon costs, right, which is probably the long-term story about aluminum was very leveraged to carbon. But there's also kind of maybe more cyclical inflationary pressures in manufacturing and in mining globally. And – because every industry seems to be feeling some cost pressures. And just wondering what you're seeing on the ground that your assets as cost inflation. And obviously, margins are expanding. These prices are very good. But is there cost inflation? And to the extent that there is cost inflation, is it mostly cyclical? Or are we seeing some cost inflation that might become more deeply embedded and you kind of have a higher fixed cost business going forward? Again, cost curve is steepening, so maybe your margins are

bigger anyway, but could some of this cost inflation likely to be more persistent?

William Oplinger: We're certainly not immune to some of the cost pressures that you're seeing around the globe. It starts with some of our raw material costs. We're seeing higher carbon costs, both in coke and pitch in the refining business, seeing some higher liquid caustic pricing. And so we believe those are typically – both of those are typically cyclical. They go up and down. Remember, we don't mind higher liquid caustic pricing because we're one of the lowest users of liquid caustic out of any refineries in the world. So higher liquid caustic pricing just steepens the alumina cost curve even more.

The energy environment is higher cost. You're seeing it in natural gas in Europe and seeing it in electricity prices in Europe also. One of the areas that we are exposed to higher energy prices is in Spain, where we've got electricity on a spot basis. And that's some of the highest priced electricity, if not, the highest priced electricity in the world for smelting. And so that's one of our areas of exposure. Other than that, we're starting to see some of the cost pressures that I think the other industries are seeing, but a lot of it is cyclical, Chris.

Christopher LaFemina: Right. And without getting too much into the kind of macro, what's your take on the potential impact to aluminum demand from Chinese property markets? I think Chinese properties, I don't know, 10% of the global demand or something. Are you seeing – first of all, are you seeing any evidence yet of weakening demand? It looks like physical markets are not really weakening at all, but is there some risk around demand, again, probably cyclical in the short term, but are you seeing any risk around that or any evidence of that materializing yet?

William Oplinger: It's way too early, Chris, to say how that plays out. And I think there's a lot smarter people than us that are thinking about how that situation plays out. We're not seeing any loss of demand currently, but that situation can evolve quickly.

Christopher LaFemina: Yes. I guess you focused on the factors that you can control, which is how you operate and how you manage your portfolio.

William Oplinger: Yes.

Christopher LaFemina: So I think you talked about – I've heard you talk in the past about value creating growth opportunities, right? So when you consider growth, you consider the – obviously, the return on that investment. How do you kind of judge or measure value creation from your growth? And then when you

think about that, are there potentially opportunities for you? Again, if we're considering an environment that could be a persistent environment of high cash flow, there's a lot of potential optionality you could explore. So is it possible as well that capital allocation for acquisitions via – either via assets or even companies is something that could emerge as being part of the Alcoa strategy? And so – and how do you think about that versus some of your organic growth, which is relatively small. But how do you kind of weigh that? And how do you assess it?

William Oplinger:

So we've been pretty clear over the last four or five years that we've been focused on organic growth opportunities. We don't spend a lot of money on growth currently, and that's really been a function of the fact that we've been really focused on paying down the balance sheet but more focused on the organic side, creeping our plants, potentially step outs in the refining business. We've invested some in our bauxite business, specifically in Brazil over the last few years. I would tell you, though, on an inorganic side, we look at everything that comes to market.

We'll look at any opportunity, run the numbers. If we're going to be focused on any type of inorganic growth, it will be focused on Tier 1 type assets that we can be certain that don't have legacy issues behind them. And at this point, that hasn't been the case. As far as the returns that we look for in our growth opportunities, we think our cost of capital is between 9% and 10%. We're looking for a hurdle rate that's above that. We have three mid-sized growth projects in the refining business. They're lower teens type returns using our long-term alumina prices. At this point, a lower teen's type of return doesn't excite us enough to execute upon it.

Now as we look forward, if we start to look forward into 2024 and 2025, if ELYSIS works, ELYSIS will be a game changer, and we will have to evaluate how we deploy ELYSIS and how much capital we spend on ELYSIS. But I really believe, that assuming that technology works, that will be something very welcomed by investors because it will give us a capital cost advantage, an operating cost advantage and a carbon advantage, which by mid part of the decade, could be really valuable.

Christopher LaFemina: And in terms of opportunities to create value organically, I mean another path that you guys have pursued has been more value-added products, higher price premiums, et cetera. Can you just talk about what we're doing in terms of positioning in the market to potentially improve your price realizations across the portfolio?

William Oplinger:

Yes. So if you go back to the height of the COVID pandemic, our value-add products business dropped probably from 55% of the portfolio down to 45% of the portfolio, and we were selling more commodity-grade aluminum. We're back to around 55% of our product being value-add. We're largely at capacity today. You can always creep capacity a little bit, but we're largely at capacity for our value-added products. We – some of

the smaller projects that we have worked on over the last few years, that we continue to work on, are investments in the cast houses to maximize value-add products.

Right now, the markets that we are in, Europe and North America, are very strong for slab products, for billet, really good demand and pricing premiums. And so we've looked at opportunities to incrementally grow our cast houses. These aren't huge amounts of capital. And so they're pretty easy decisions to make.

Christopher LaFemina: So on your existing portfolio, I think it's kind of normalized here operationally for Alcoa and then portfolio management is coming close to completion. You kind of have a very good asset base now. It seems to be operating well. How do we think about sustaining capital going forward? What's the right number annually on the existing portfolio? Is it 350 [million], 375 million per year? Or might that begin to creep higher as you pursue some of these kind of debottlenecking initiatives internally and more green initiatives, more value-add products, et cetera? How does sustaining CapEx progress?

William Oplinger: Yes. We'll typically provide some level of estimate of capital toward the end of this year, beginning of next year. What I would say, Chris, is that there will be some upward movement in our sustaining capital budgets. We are making the choice to invest in really invest in stability in some of our plants. And so that will be an upward creep. But we're not talking a huge magnitude, and we're working through those numbers today. But I think it's the right thing to do where we are in the market.

Christopher LaFemina: And in terms of where you think Alcoa still has the most work to do, where they might be the most upside, I mean, presumably, the low-hanging fruit has already been picked. But where do you see more upside organically in terms of what you can do operationally that might not – that we might not really fully appreciate yet?

William Oplinger: So there's still upside throughout the entire part of the company. We are actively focused on digitization work to try to digitize processes. We have a very active productivity program that is working to offset some of the raw material costs and energy cost increases. When I look at how we're positioned in the three parts of the value chain, really strong positioning in bauxite with mines in three parts of the world. And there's opportunities there to drive greater productivity and drive lower costs through smart initiatives, digitization and the mining piece.

In refining – as I look forward in refining, we're extremely well positioned in the refining part of this segment. We are first quartile. We've got two of the lowest cost plants in the world in Western Australia, continue to focus on how we incrementally creep those plants and really focus on the long

term that if we go toward a green environment, how we can further position those refineries to be lower carbon. There's opportunities that we announced. For instance, we're working on a project called mechanical vapor recompression that's being, in part, financed by the Australian government, which will decarbonize part of the refining business.

And then on the smelting side, we've repositioned the portfolio. We still have a little bit more to do there. We talked about 1.5 million metric tonnes. Today, with this announcement, we've executed on 750,000 tonnes. So more to come on the repositioning of the portfolio. We will be actively looking at some of the curtailed sites to see whether they should be permanently closed and other activities. So I think there's still tremendous upside. And clearly, in this market environment, the company is well positioned.

Christopher LaFemina: Right. So in the interest of time, maybe kind of to wrap things up, and maybe I'll summarize, and you can add to what I say here. So basically, you guys are in a position of strength financially now. You are on the verge of potentially reinstating potentially sizable capital returns, you are likely to benefit from green premiums, positioned well for a world of ESG, China supply constraints that are probably sustainable. There's – I mean I suppose that there are still a lot of investors who are not maybe fully aware of some of the progress that Alcoa has made and not really fully aware of the Alcoa investment case.

Maybe it's capital returns that kind of get people more involved. But what do you think the market might be missing? I mean based on your discussions with investors, what about Alcoa do people not really fully appreciate? Is it the – how material the changes have been? Because there's really been a significant transformation the last five or six years? Or is there something else in the business that you think people don't really fully appreciate yet?

William Oplinger: It's always hard to say what people don't appreciate about the company. What I think that people should consider is that the company is vastly different than it was five years ago. The balance sheet is largely fixed. I would say our balance sheet is strong. Could it get stronger? It could get a little bit stronger in today's market environment. The portfolio is repositioned. We're in a situation where all of the ESG work that we've done over the long term is now, I think, potentially – has the potential to be rewarded.

And as you look forward, we're uniquely positioned to be successful through the cycle at this point. We have really made an effort to try to cycle proof the company so that when times are good, we're generating a lot of cash. When times are difficult, like we saw in the pandemic last year, that we're positioned to succeed then. So overall, the company is really different than it used to be. And a lot of those legacy issues that we

had are largely solved at this point. And so if you haven't looked at Alcoa, you should take a look at us again.

Christopher LaFemina: And what is your biggest concern? Is it the macro risk that is the thing that could most go wrong? Or is there anything specifically related to Alcoa that keeps you up at night?

William Oplinger: I tend to focus on what we can control, Chris. And we're constantly – and I think you and I talked about this just a while ago. When we originated this company, we knew what we wanted to get done, and we have just consistently done it. We've consistently chipped away at many of the issues the company had. Now we're going to – we're looking at how do we reposition the company for this new market environment and what are the opportunities out there. So I think from my perspective, our company is really well positioned, and we will continue to execute on the things we can control. Made the big announcement today. So it's a quick payback project that results in a low-cost plant that will be successful over a couple of decades.

Christopher LaFemina: Great. Well, Bill, thank you very much, again, for taking the time today. I wish we had more time. There's lots to talk about, but we'll be keeping an eye on Alcoa. A lot of interesting things going on there, and a lot going on in the market. So good luck with it all, and thank you once again.

William Oplinger: Thanks, Chris. See you.

Christopher LaFemina: Cheers. Bye.