"Hindalco Industries Limited Q3 FY20 Earnings Conference Call"

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Moderator: Ladies and Gentlemen, good day, and welcome to the Hindalco Industries Limited Q3 FY '20 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Subir Sen from Investor Relations of Hindalco. Thank you, and over to you, sir.

Subir Sen: Thank you, and a very good evening or morning everyone. On behalf of Hindalco Industries Limited, I welcome you all to this earnings call for the third quarter of financial year '20. On this call, we will refer to the Q3 investor presentation available on the company's website. Some of the information on this call may be forward-looking in nature and is covered by the safe harbor language on Slide #2 of the investor presentation.

In this deck, we have presented the consolidated quarterly financials, included all segments of India business and our overseas subsidiary, Novelis to give you a comprehensive view of all our businesses. For this purpose, standard principles of consolidation have been applied as per the Ind-AS. For comparison purposes, all the prior period consolidated financial numbers are presented in a similar manner.

On today's call, we have with us from Hindalco, Mr. Satish Pai - Managing Director; Mr. Praveen Maheshwari - Chief Financial Officer and CEO, Copper Business. From Novelis, we are joined by Mr. Steven Fisher - President and CEO.

I will now hand over the call to Mr. Pai for his opening remarks. Thank you, and over to you, sir.

Satish Pai: Thank you, Subir. Greetings to everyone and thanks for joining this earnings conference call for third quarter of FY20 of Hindalco today.

Let me start with a quick review of our quarter 3 results. Praveen will then present the operational and financial performances of all our businesses in detail later on.

Coming to Slide 5, Hindalco delivered yet another steady quarterly results driven by strong operational and financial performance by Novelis, supported by a resilient show by the Indian aluminum business and partially offset by the copper business performance which was impacted by lower realization and volumes.

Novelis reported its best ever Q3 EBITDA of 343 million, up 7% year-on-year and an adjusted EBITDA per tonne of $430, up 7% year-on-year. Net income without exceptional items was at

$132 million, up 31% year-on-year. Overall, shipments were flat year-on-year at 797 Kt in Q3 with can sheet and automotive body sheet shipments higher by 4% and 3% respectively over the previous years.

In January, Novelis also successfully issued $1.6 billion bonds at 4.75% due in 2030. These replace one of our existing US $1.15 billion bond at 6.25% due in 2024. This offering extends the debt maturity profile of Novelis, at an attractive rate with the net interest savings of around $17 million per annum.

On the Aleris acquisition, we have received the antitrust approval from China. The European Commission is currently evaluating the suitability of the proposed buyer of Aleris' automotive plant in Duffel in Belgium. The US arbitration proceedings are in progress. I had indicated by Novelis earlier, this transaction could take some more time to close, but we remain committed to close this transaction at the earliest.

Moving onto Hindalco's aluminum business. The domestic markets for aluminum contracted by 14% year-on-year and 5% on a year-to-date basis. Global aluminum prices in the quarter have declined significantly by around 11% year-on-year to an average of $1,754 per tonne. Hindalco's operations remained stable with alumina and aluminum metal production at 662 Kt and 330 Kt respectively. Metal sales were up 2% year-on-year at 328 Kt in Q3. Sales of aluminum value-added products excluding the wire rod sales were flat year-on-year at 75 Kt compared to the same quarter last year.

The aluminum business including Utkal reported an EBITDA of Rs. 1,036 crores versus Rs. 1,252 crores in the prior period. This drop in EBITDA was mainly on account of lower realizations. This was partially offset by lower input costs and the reduction in renewable power obligation. This EBITDA margin was at the healthy 19% despite volatile and challenging market conditions.

Turning to the copper business on Slide 6. The domestic copper market growth moderated to 2% year-on-year in Q3. Value-added CC rod sales grew 3% year-on-year at 58 Kt with the share of VAP to total sales at 69% in the third quarter of FY20. Copper EBITDA stood at Rs. 256 crores in Q3 versus Rs. 490 crores in the quarter 3 of the previous year. This was comparatively lower year-on-year due to lower volumes and realizations in this quarter. The benchmark Tc/Rc for calendar year 20 settled at 15.9 cents per pound, which is 23% lower than last year.

Now let us take a look at the consolidated performance of the quarter. Hindalco reported its consolidated EBITDA of Rs. 3,676 crores for the third quarter of FY20 compared to Rs. 4,080 a year ago. Consolidated PBT before exceptional item was Rs. 1,487 crores as compared to Rs.

1,931 crores in Q3 FY '19. Consolidated Profit after tax for the third quarter was Rs. 1,062 crores compared to Rs. 1,394 crores year-on-year, down 24%.

Finance cost in Q3 FY20 was Rs. 889 crores, lower by 4% on account of reduction in interest rates during the quarter. The consolidated Net debt to EBITDA stands at 2.65 times at the end of December 2019 as against 2.48 times at the end of March 19.

I would like to share that one of our recent recognitions in the field of finance. Hindalco was awarded the Silver Shield for Excellence in Financial Reporting for FY 2018-19 given by the Institute of Chartered Accountants of India.

Turning to the broader economic environment on Slide 8. The US economy grew by 2.3% in 2019 versus 2.9% in 2018, propelled by public spending and government expenditure. Economic activity in the Euro area remains subdued. The Chinese economy slowed down to a 29-year low of 6.1% in 2019 mainly due to subdued demand and the US-China trade war. According to the IMF, the estimated global growth is expected to moderate to 2.9% in 2019 versus 3.6% in 2018 reflecting the weaker than expected growth in the emerging markets. Global growth is expected to rise from 2.9% in 2019 to 3.3% in 2020. The coronavirus outbreak presents a threat to economic recovery, though the full impact is not yet clear.

Moving to the Indian economy. In FY20, the economic growth moderated over a number of factors; subdued consumption, slowdown in investments, and geopolitical issues such as trade tensions. However, the latest manufacturing PMI shows a positive outlook. It rose to 55.3 points in January from 52.7 points in December. Some of the measures announced in the recent Union Budget for the rural economy, infrastructure as well as rationalization of personal income tax augur well for the economy. According to the first advanced estimates of the government of India, the economy is likely to grow by 5% in FY20.

Let me take you through the aluminum industry overview on Slide 9. The Global consumption growth in 2019 declined by 1%, the lowest since the global financial crisis. The prolonged US-China trade war, uncertainties around Brexit and sluggish industrial activity across the region dampened consumption growth during the year. In 2019, demand in the world excluding China contracted by 3% versus a growth of 2% in 2018 due to subdued demand in regions notably the US, Latin America, France, Italy, Japan and South Korea. Chinese demand moderated to a marginal growth level of 0.5% in 2019 as compared to 4% the previous year. Across regions, slow growth in end user industry such as automotive, construction, electric and power, machinery and equipment were the major reasons for the drop in demand.

On the supply side, the global production declined by 300 Kt to around 64 million tonnes in 2019. This was mainly due to Chinese production declining by 2% due to a disruption at 2 major smelters whereas in the rest of the world, production grew by 1%. The overall market deficit in 2019 was around 840 Kt versus 1.2 million tonnes in 2018.

Global demand in 2020 is projected to rise by 2% with the easing off trade tensions between the US and China and the likely Brexit deal. We expect manufacturing activities to revive in 2020.

Moving to the domestic aluminum segment. Domestic demand registered consecutive decline in Q3 FY20 by 14% to 863 Kt. The continued slowdown in user industry such as automotive, building and construction and electric sectors were the primary reasons for the sluggish growth in consumption during the quarter. Year-to-date FY20, domestic demand declined by 5% to 2.8 million tonnes. Imports including scrap also recorded a degrowth of around 17% in Q3. Year-to-date, imports including scrap degrew by 7%. Despite this degrowth, imports maintained a market share of around 60% in FY20. The factors that will drive demand in FY21, are withdrawal from the RCEP trade deal, revisiting some of the other trade deals, focusing on country of origin, the thrust of the government on infrastructure, housing and electrical sector especially renewables.

Moving to Slide 10. The global FRP demand continued to grow at a steady pace of around 3% in CY20. Global demand for beverage can stock is growing strongly on account of a continued shift in the packaging material to aluminum and products like new energy drinks, sparkling water and crafted beer resulting in a growth in a range of 3 to 4% in the beverage can sheet market. Strong and steady demand for automotive body sheets in the transportation segment like trucks, electric and premium vehicles due to global adoption of strong light-weight formable aluminum in vehicle parts and structures. This market is expected to grow at a CAGR of 10% between CY20 to 25.

Domestic FRP demand declined by 4% year-on-year in Q3 FY '20 with subdued demand in the construction and transportation sector. Year-to-date, the Indian market on FRP is contracted by 1% year-on-year. The domestic FRP market is expected to grow next year at about 6%.

Turning to the copper industry on Slide 11. Global consumption for refined copper contracted by 0.3% in 2019 versus a growth of 3% in the previous year. In China, consumption growth moderated to 1% in 2019 versus 5% in 2018, where consumption in the rest of the world contracted by 1.7% in 2019 versus a growth of 1.3% in 2018.

On the supply side, mine disruptions in 2019 were high, notably in Peru, Chile and Africa. Copper concentrate consumption grew negligibly by 1% to 16.7 million tonnes in 2019. And the concentrate market recorded a deficit of 142 Kt in 2019 versus a surplus of 95 Kt in the previous year.

Going forward, agreement on Phase 1 deals should encourage the consumer confidence. In addition, new semis capacities across several regions will support strong consumption in 2020. However, the full impact of the Coronavirus outbreak on copper demand is not yet clear. We expect the market next year to grow in the range of 1% to 1.5% from a decline of 0.3% in 2019. On the supply side, the benchmark TC/RCs dropped by 23% in 2020 due to an increase in demand and the lower productivity of mines.

The concentrate market is expected to be in a deficit of 200 Kt in CY20. In the domestic market, consumption recorded a marginal growth of 2% in the third quarter to 193 Kt as consumption from strips and transformers, winding wires and railway was sluggish. During the same period, imports touched 99 Kt, taking a market share of imports to 51% from 40% in Q3 FY '19. We expect demand to remain flat in Q4 FY '20.

In FY '21, recovery in demand from sectors like auto, railways and transformers will increase copper consumption. Imports from ASEAN and other FTA countries continue to put pressure on domestic pricing. On the positive side, on the 8th of January, the Government of India imposed CVD, or countervailing duties, on the imports of wires from Malaysia, Indonesia, Thailand and Vietnam to support the domestic producers.

Praveen will now take you through the business performance highlights of each of the business segments in quarter three.

Praveen Maheshwari: Thanks, Satish. Let's review our operational performance on Slide 14. Novelis delivered yet another steady quarterly performance with its best-ever Q3 adjusted EBITDA, adjusted EBITDA per tonne and a very strong net income in Q3 of FY '20 year-on-year. This performance was on the back of strong operating and financial performance, supported by favorable market conditions.

Global demand for aluminum FRP remained steady, with overall shipments of Novelis at 797 Kt in Q3 FY '20. Beverage can sheets and automotive body sheets also grew in this quarter Year on Year driven by growing consumer preference for sustainable packaging and automotive light-weighting globally.

Progress on all 3 major strategic capacity expansion projects is quite satisfactory. These projects, as you know, are in the U.S., China and Brazil. Out of this, the 200 Kt greenfield automotive finishing plant in Guthrie, Kentucky, has begun commissioning and will be ready in the coming months. Satish has already explained to you in the previous slides about the position of Aleris acquisition and the fact that Novelis successfully issued $1.6 billion bonds, and we'll explain more at the time of Q&A.

Moving to Slide 15. Novelis achieved an adjusted EBITDA of $343 million and EBITDA per tonne of $ 430, both up 7% Y-o-Y in Q3 FY '20. This growth was on account of increase in share of can and auto sheets and operating cost efficiencies, partially offset by less favorable recycling benefits due to lower aluminum prices.

Slide 17 shows the details of the performance of Indian aluminum business, including Utkal. Alumina production in Q3 FY '20 was 662 Kt. Aluminum metal production was 330 Kt in Q3 FY '20, reflecting stable operations during the quarter. Value-added products, excluding wire rods, recorded a production of 80,000 tonnes in Q3 FY '20 versus 82 Kt in Q3 FY '19.

Coming to Slide 18. Aluminum metal sales volumes grew 2% at 328 Kt in Q3 versus 323 Kt in the previous year. The VAP sales, excluding wire rods were flat year-on-year at 75 Kt, but grew 5% in 9 months year-on-year basis. Share of VAP in total sales was about 24% in this quarter.

Moving on to the financial performance of the aluminum business, including Utkal, on Slide 19. This segment recorded a revenue of Rs. 5,467 crores in Q3 FY '20 versus Rs. 6,019 crores a year ago on account of lower LME in Q3 FY '20. EBITDA, including reversal of provision of regulatory changes related to RPO in Q3 FY '20 stood at Rs. 1,036 crores versus Rs. 1,252 crores in Q3 FY '19, which is down 17% Y-o-Y. The EBITDA margin was at a healthy 19% of revenue in this quarter despite the current challenging macroeconomic business environment.

Moving to Slide 21. The overall copper metal production was lower by 18% at 86 Kt in this quarter compared to 105 Kt in the previous year. Quarterly production of CC rods was lower by 8% at 60 Kt in Q3 FY '20, driven by market conditions. DAP production was higher by 6% at 80Kt versus 76 Kt last year on account of stable operations in this part.

Coming to Slide 22 on sales volume of copper and its VAP. Copper metal sales were lower by 14% year-on-year at 84Kt due to lower production. Copper value-added products which is CC rod sales in Q3 FY '20 were higher by 3% Y-o-Y at 58 Kt, which was in line with the current market growth.

The financial performance of copper segment is on Slide 23. Revenue stood at Rs. 4,774 crores versus Rs. 5,943 crores a year ago, down 20%, mainly due to lower LME and volumes. EBITDA stood at Rs. 256 crores in Q3 FY '20 versus Rs. 490 crores last year as a result of lower volumes and realization.

Let me now hand over the call back to Satish to give you a brief on our consolidated results and an update on our key focus areas.

Satish Pai: So, on Slide 24, Hindalco reported a consolidated revenue of Rs. 29,197 crores, an EBITDA of Rs. 3,676 crores, a PBT before exceptional items of Rs. 1,487 crores and a PAT of Rs. 1,062 crores in Q3 FY '20. The detailed quarterly comparative financial numbers are attached as an annexure to this presentation on Slide 28.

The Hindalco India business reported a revenue of Rs. 10,254 crores, an EBITDA of Rs. 1,388 crores and a PAT of Rs. 262 crores in Q3 FY '20. These details are also provided as an annexure to this presentation on Slide 29.

Let me now end by giving you an update on Hindalco's key focus areas on Slide 25.

There are 3 crucial broad focus areas for Hindalco. First, the company's continued focus on cost efficiency through integration and resource security.The ongoing Utkal Alumina expansion of 500 Kt is 70% completed, and the expected commissioning is in December of this year. This expansion will help in the cost reduction by getting the best and most economical alumina to strengthen the existing resource security further. Dumri captive coal mine coming up in the next financial year will add up to the company's overall coal security apart from its current coal linkages with Coal India.

Second, Hindalco's focus on a sustainable business model with a downstream strategy of product expansion in India, where it will increase its flat rolled product capacity by 2 times and extrusions by 3 times in the next 5 to 6 years. And this will enhance the share of value-added products to insulate the consolidated Hindalco EBITDA from LME volatility further. Hindalco has already made certain investments towards enhancing capacities in the extrusion breadths and capabilities in products such as circles and hard alloys with investments in a new scrap furnace in Hindalco's Hirakud facility. Novalis' use of recycled content has reached around 62% in Q3 FY '20, driving its sustainability journey. Hindalco also launched India's first all-aluminum freight trailer towards its sight for aluminization in India.

Coming to ESG initiatives. Novelis has achieved the ASI certification for its Ohle plant in Germany in terms of responsible production sourcing and stewardship of aluminum. Hindalco has also made investments in the fuel gas desulfurization for control of SOx and NOx in its sustainability initiatives.

Third, Hindalco's focus on organic and inorganic growth initiatives. Organic growth initiatives in India include a US$ 1.2 billion aluminum downstream expansion and a US$ 200 million Utkal expansion project, which are progressing well as per the company's strategy. Novelis' strategic expansion in U.S., Brazil and China of US$ 700 million will come online in the next 2 years. In addition to these organic plans, Novelis' acquisition of Aleris will provide strength to its existing product mix further, diversifying its product portfolio and will also provide integration and synergistic benefits. The intent is that these 3 focus areas will support Hindalco in following a sustainable path to become resilient, reliable and responsible metals major.

Thank you very much for your attention, and we'll now open up the forum for questions.

Moderator: Thank you very much sir. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Pinakin Parekh from JPMorgan. Please go ahead.

Pinakin Parekh: Yes. Sir, my first question is on the Copper segment. For the last 3, 4 quarters, we are running at some 90,000 tonnes in terms of production. When can we go back to 100,000 tonnes of production, which was there in F '18?

Praveen Maheshwari: Yes. You're right. In the last 2, 3 quarters, we have seen those problems. Quarter 2, particularly, we had the issue of floods in Gujarat. Those were unprecedented floods, which created havoc in that area. Quarter 3 also, we saw some of the impact of similar issues. Basically, one fundamental difference between aluminum and copper business is that unlike aluminum, where if there's a problem with a pot, you can take it out and repair it. In case of copper, it is one full smelter. It's a very large smelter and many parts are there. If anything goes wrong anywhere, the whole line stops, and then it has an impact on the production. Also, the production gets impacted in the quarters where we have a planned shutdown as well because then the whole plant is kind of stopped. So, in Q3 as well, we had a couple of such issues, which were unplanned shutdowns. And gradually, we are expecting that these issues will go away. Q4, so far, is running all right. Some of the impact of Q3 will come in Q4 as well. But post the repairs, the plants are running well at the moment. We have scheduled shutdowns also in quarter 1 and quarter 3 of next fiscal . And we'll update you on those activities as we go along.

Pinakin Parekh: Sure, sir. Just containing with the copper business, while the company mentioned that CY '20 TC/RCs have been set lower, given what is happening in China and news flow about smelters, custom smelters not picking up copper concentrates, that ideally would have led to spot TC/RCs moving sharply higher. Now in terms of the company's exposure, does it have any exposure to the spot market? Or everything is locked in to the annual contracts?

Praveen Maheshwari: Typically, we have about 85% of our requirements locked in with long-term contracts. It works both ways. Today, you're seeing spot TC/RCs, you may see an opportunity. But it has also helped us when cases like even last year and before that as well, where spot TC/RCs were very low, and therefore, it actually helped us sustain our profitability as well. So we may have some small pockets of opportunities there, but it's not big in terms of a portion of our requirement.

Pinakin Parekh: Sure, sir. And sir, just last question on the Duffel plant, now what we know is that it's a $50 million EBITDA, but we don't know as to what value has the plant been sold to the new buyer.

Now Aleris was acquired at a transaction multiple of roughly 7x the EV/EBITDA, now would the Duffel plant divestment be at a higher multiple than that because it's in the auto business and auto is seen as something which is structurally more positive?

Satish Pai: I'll let Steve answer that. But Pinakin, I think, at this stage, we will not be able to give you any guidance on that till we get approval from the European Union on the acceptance of the buyer. But Steve, do you want to add anything more?

Steven Fisher: No, Satish, I think that's appropriate at this point in time. I have to leave it there.

Moderator: Thank you. The next question is from the line of Sumangal Nevatia from Kotak Securities. Please go ahead.

Sumangal Nevatia: First question is with respect to our Utkal expansion. I mean, is our strategy completely to replace existing high-cost production? Or we'll be selling in the market as well? And if we are just replacing, what sort of cost benefits one should expect?

Satish Pai: So look, I think it will be fair to say that it will be a mixture of both because though we have restarted Muri, and Renukoot is a very old refinery, we would take that, the first part will be to replace some of the alumina of Renukoot with Utkal Alumina. And I think currently, the market price, which we are transferring at is around 280 to 300. And both Renukoot and Muri refinery cost of production is actually in this range whereas Utkal is half of that. So, any replacement will mean nearly $150/ton of alumina cost benefit.

Sumangal Nevatia: Understood. Alright. Secondly, with respect to the Copper business, now the TC/RCs we read is settled at around 20%-25% lower. So, in our overall profitability, say EBITDA of around 1,100 - 1,200 crores, how much is linked to TC/RC and what portion of this is with respect to byproduct credits, DAP, etc.?

Praveen Maheshwari: Broadly, if I divide this into 3 parts, TC/RC is roughly 50% of our contribution; 25% is towards the value-added products and markups etc. in the domestic market; and balance 25% is towards the byproducts, we have sulphuric acid and DAP.

Sumangal Nevatia: Okay. So, it will be fair to estimate that the 50% will be down 20%, 25%, and the remaining 50% should continue at the existing run rate and whatever is the market changes?

Praveen Maheshwari: That is by and large true, but there are many other factors which go into it. So, there are input prices, which also, for example, in case of the by-products, input prices have been lower; coal and LNG have been lower. So, it is difficult to just straight away put it. But broadly, I can say, you're right.

Sumangal Nevatia: Understand. Okay. And with respect to our CC rod, the rampup appears to be quite slow. So, is there a demand issue or some teething troubles with the plant?

Praveen Maheshwari: No. So, there are no teething troubles or any kind of troubles with the plant. In fact, the rod production has been running very smoothly. It has also been improving its quality now. So, it's a very good and stable operation. It is unlike the smelter operation, where I just mentioned that it's one large plant, and CC rod is more like a downstream operation. If there are problems, you can always correct it. We are planning to use some digital analytics as well as we go along. But so far, it has run very well. Q3, you saw the numbers are little low because of the market conditions. The market in Q3 was very depressed. And as we mentioned, the imports have been coming into India. The CVD has come only from January 2020. So hopefully, going forward, you'll see a better utilization of CC rod capacity.

Sumangal Nevatia: Okay. Just one more question, if I can squeeze in. With respect to our long-term plan of $1.2 billion spend towards the downstream aluminum, what sort of ROCs one can expect here? And I mean, it's a 5-6-year investment. So I mean, how will it be spread in the next 5 to 6 years? Because, I mean, I think, we've been aiming this and talking about since last 2 years, but I believe the progress on this has been quite slow.

Satish Pai: So as we said, let me first tell you that this year's Rs. 2,000 crores CAPEX, about 800 was the sustaining CAPEX; Rs. 500 - 600 crores was Utkal; and we put in the downstream about 300 crores this year. So, if you remember in my closing comments, I talked about the scrap furnace came up in Hirakud, extra circle line, tension leveler, an extrusion press in Renukoot, all these are now coming on stream by the middle of this year. So, what we will do, and frankly, as I said, I want to remain within our cash flows as well. So, we are going to maintain around a Rs. 2,000 crore CAPEX, Rs. 800 being sustainance Capex. So, since the Utkal is coming to an end, next year, I'll be able to put instead of Rs. 300 crore, maybe about Rs. 600 crore into the downstream. So, this is the way we'll do it. And the IRR, we are getting out of these projects are around 13% to 15%, is the way we target these projects.

Moderator: Thank you. The next question is from the line of Amit Dixit from Edelweiss. Please go ahead.

Amit Dixit: Sir, I have 2 questions. The first one is on domestic demand dip in Q3, which is like quite, I would say, acute at 14%, I'm talking about aluminum here, whereas our VAP sales actually remained flat. So, what all segments do you see the maximum pain? And how do you see it going forward in FY '21?

Satish Pai: Yes. So, the maximum pain for us, you see the largest aluminum consuming sector in India is the electric sector, which is conductor and cables. And that is where we saw quite a lot of market pressure. So, this was where quite a lot, though I have to say, in December, the orders did start to pick up. Now the sectors like packaging and pharma, we saw very strong orders. So, you're right, Q3 was probably the slowest quarter we have seen in a long time. Though end of sort of December, middle and January, the electrical sector orders have started to pick up. So, we are expecting that Q4 will be a good quarter. I mean, it's also the final quarter. So, government budgets and all tend to get spent, and Q4 normally is our best quarter. So, seeing the results of January, I can say that the electrical sector demand is starting to pick up.

Amit Dixit: Okay. The second question is on Dumri coal block. So once your captive mines start, what kind of savings per GCV we can expect?

Satish Pai: So, look, honestly, the captive mines are not really a cost saving. They are actually providing us the coal during the times when Coal India production gets very tight. The cheapest coal in the Hindalco is linkage coal. And normally, we run at about 60% to 70% is linkage coal. In fact, Q3, our aluminum business performed very well, if you notice the EBITDA as well as the percentage. It's because the linkage coal percentage went up and our cost of production fell by 5% Q3 to Q2. So what Dumri will do is it will bring in just like the Gare-Palma coal during the next monsoon period etc. We will have a backup when Coal India supplies starts to get tight and when they start prioritize the power sector. So, we normally use our own mines as a swing producer. The cheapest coal in the system is still the linkage coal from Coal India.

Moderator: Thank you. The next question is from the line of Ashish Kejriwal from IDFC Securities. Please go ahead.

Ashish Kejriwal: Sir, as you mentioned in the last comment that cost of production of aluminum was down 5% quarter-on-quarter. So, is this because of just higher linkage? If it is, is it possible to share the linkage share in this quarter versus last quarter? And what is the current cost of production?

Satish Pai: Yes. We don't give out the cost of production, but the cost of production was down 5%. So first, you have to realize that, as usual, our efficiencies and operations are running smooth. Now the cost of production was down because linkage coal went from 60% in Q2 to 69% in Q3. And linkage coal, as I told you, was our cheapest. Besides that, the other input costs have also sharply come down. So the carbon, normally, CP coke, pitch, even caustic, all these prices have come down QoQ. So as a combination, our cost of production, if you remember, I was guiding to flat to 1% or 2% down. Actually, it went down by 5% in Q3. And anticipating your next question, in Q4, I expect it to be down by another 2%.

Ashish Kejriwal: And this another 2% is, again, on account of linkage coal? Or...

Satish Pai: And other input costs as well.

Ashish Kejriwal: Okay. So sir, is it possible to share power cost per GCV for this quarter?

Satish Pai: No. We don't give out that. Because our power cost is a combination of a number of CPPs. So, we don't give that out.

Ashish Kejriwal: No issues, sir. And in terms of copper profitability, because now, we have changed our last quarter numbers as a means...

Satish Pai: That is cost allocation.

Ashish Kejriwal: Yes. So, if I'm looking at, is this the new normal for Copper business, excluding the lower TC/RC, which we are going to recognize from fourth quarter?

Praveen Maheshwari: Yes. So, I would generally say that next year is going to be a difficult year for Copper business, and TC/RC surely has a big impact. We are also anticipating a longer kind of shutdown for DAP part of DAP production because of one particular inspection, which is due at the moment for ammonia tank. So copper, next year, is a little difficult one. But this is probably the bottom as we see. The hints we get from the miners and the bodies etc. is that this 15.9 cents is probably the bottom in the current cycle. And we should see some comeback in the next year, that is, calendar '21 in terms of the TC/RC.

Ashish Kejriwal: Sir, assuming if it remains like this for the entire year and we come back with our production numbers of roughly around 400 Kt, then will it be making sense to make around 1,000 crore EBITDA also?

Praveen Maheshwari: So, I cannot give you any guidance on EBITDA numbers at the moment. I can only tell you that the TC/RC is low, which is a fact. But we will try to make up, by higher production, operational efficiencies etc. And we will try to counter this as much as possible.

Ashish Kejriwal: Sure. And, sir, lastly, on this $1.2 billion CAPEX plan for the next 6 years, the first 2 years, okay, it will be somewhat on a lower end. But when we are seeing it as a peak CAPEX as well as when we start getting some benefit out of it?

Satish Pai: So look, the downstream is modular. There will not be a big sharp spike in CAPEX spending because there are multiple projects that we keep doing over a period of time. So, the rate at which we'll do the projects, which I tried to explain earlier, will depend on the cash flow generated in India. And with the current LME, I can afford to put about Rs. 2,000 crores of CAPEX. If the LME goes up, we can accelerate a few more projects.

Moderator: Thank you. The next question is from the line of Abhijit Mitra from ICICI Securities. Please go ahead.

Abhijit Mitra: I have 3 questions. Firstly, on the coal consumption for the quarter, if you can give up a breakdown of the tonnage between e-auctions, linkage and captive, that would be great. Secondly, just to understand the 2% cost savings that you are highlighting for the next quarter, it does not factor in any benefit despite the start of Muri because it's almost at the same price at what the market price is? Thirdly, 2 quick questions on Novelis.

Satish Pai: So coal mix, linkage was 69%, e-auction was 15%, and between own mines and imported was the remaining. So Q3 was largely linkage and e-auction coal. Dumri does not start till April 1, after which we'll start to remove the overburden. So, production will really start in the subsequent months. And I repeat, again, Dumri will not bring my overall coal costs down. But during the monsoons, when I get tight on coal, it will help me.

Abhijit Mitra: Yes. The one more question on the restart of Muri. I mean, it's not going to change the cost structure much at this market price of alumina. Was the understanding, right?

Satish Pai: Muri's impact in Q3 was 77 crores. So if you remember, in Q2, it was another 80 odd crores. So that expense will not be there in Q4. So it will not help me save money on the alumina, but the cost impact of the fixed cost, the mines, which all we had to take, some of the repair costs that we had to do, all that effect will not be there in Q4.

Abhijit Mitra: Great. And 2 quick questions on Novelis. First, with the restart of the auto finishing plant in Kentucky, there will be a further shift of specialty portfolio towards autos, right? So that can again surprise the street on the margins. Is the understanding, right?

Steven Fisher: Yes. So, as we talked about yesterday, the auto finishing line coming up in Guthrie, Kentucky, of 200 Kt will be fed from our Logan Kentucky facility, which will have a mix shift away from specialties , and some can sheet towards auto over the next couple of years. And obviously, EBITDA margins on auto business are higher in the U.S. than the other businesses.

Abhijit Mitra: Right. And lastly, regarding the selection of the buying or sort of interested party for Duffel, it looks a bit odd given the sort of news flow that we keep on reading about Liberty Group. Will that come as an impedance for getting the approval of the EC? Or is it is something that you've already factored in and you are okay with possible outcomes?

Steven Fisher: So, the European Commission in January 2020 has already stated that there are no competition concerns with the Gupta Family Group or Liberty House. We've done our diligence associated with Liberty House and believe that they are very much a suitable buyer for Duffel that will provide long-term strategic investment in the downstream auto business that comes out of that plant. And so, we're confident that, ultimately, we will get the European Commission's approval of the Gupta Family Group.

Moderator: Thank you. The next question is from the line of Pallav Agarwal from Antique Stock. Please go ahead.

Pallav Agarwal: So, my question is again on the Copper business. So what kind of recoveries are we seeing in copper at our smelter? Because the LME prices are down, so is the lower free copper revenue also impacting our profitability over there?

Praveen Maheshwari: But that impact is not much actually because that's a very small part of the overall profitability. Theoretically, yes, there is some free copper which comes. But LME movement because of that, the impact is not so much. And recovery, yes, recovery is important. That's one of the driving factors. So, whether it is uptime of the plant, whether it is a feed rate, whether it is process loss or recovery, as you call it, all these factors do play into the profitability.

Pallav Agarwal: Okay. So even the duty differential on finished copper would not be very material for the profitability, then, I guess?

Pallav Agarwal: The differential between finished copper and the import duty on concentrates?

Praveen Maheshwari: No. So, it's a little complex question and answer for this because some countries have duty-free under free trade agreement, where you can import concentrate duty-free. Similarly, if you are exporting, then you can obviously get it against license. And on the finished product, there is a 5% duty, but again, you have imports coming in at zero duty from countries which have an FTA with us. So, there is no direct answer to this question.

Satish Pai: But what we are trying to do is to get the government to make the concentrates coming into India duty-free. Today, 60% of our concentrate is zero duty because it comes from Chile. We are trying to get the remaining also to be made zero. That's one of our key demands we have with the government.

Pallav Agarwal: Right, sir. First, the standalone, gross and net debt figures including Utkal, probably?

Satish Pai: Yes. So net debt on the Hindalco India is Rs. 15,683 crores. Novelis in rupee terms is Rs. 24,305 crores, which gives you a consolidated net debt of Rs. 39,881 crores at a net debt-to-EBITDA of 2.65 times.

Moderator: Thank you. The next question is from the line of Vikash Singh from Phillip Capital. Please go ahead.

Vikash Singh: Sir, I just need a clarification. In your notes to accounts, you have written that RPO last half year, right, that's 60 crores. While in your presentation, it's 72 crores. So which one is the correct figure?

Satish Pai: That's because it's a standalone versus with the Utkal. So it's 72 crores, including Utkal.

Praveen Maheshwari: You should not look at standalone numbers now. You should look at what we present in our presentation because standalone is more by statutory requirement. So, it doesn't have the full picture including Utkal. And what we give in our presentation is the full picture of the business segment.

Vikash Singh: Yes. So remaining 43 crores of this quarter, this should be recurring in nature, right?

Satish Pai: That's correct. Just be clear that this is just Odisha. We are expecting in Q4 that Madhya Pradesh RPO benefit might also come in.

Vikash Singh: If that comes, then what kind of savings we are expecting there?

Satish Pai: We are expecting to write back about 50 crores in Q4 in caseMadhya Pradesh RPO thing comes in.

Vikash Singh: Understood, sir. And sir, my second question with regards to our captive coal mines, don't we have the obligation to produce at least the 80%?

Satish Pai: No, because these were Schedule 1 mines. So, we have that obligation only for the first year of production. After that, we can produce to our win. It's the newer mines that are being auctioned now that the government has put that requirement.

Vikash Singh: Okay. So in our older mines, there are no such requirements, so that can be kind of a flexible production that we can...

Praveen Maheshwari: Absolutely.

Moderator: Thank you. The next question is from the line of Rajesh Lachhani from HSBC. Please go ahead.

Rajesh Lachhani: Sir, my question is on the Copper business. So, you spoke about some shutdowns in Copper business next year, and there is going to be a long shutdown. So, what can be the impact on the production due to those shutdowns and also on the cost, if you can just throw some light on that?

Praveen Maheshwari: So, these are regular planned shutdowns. So, the smelters have to go through some of the yearly shutdowns, which are shorter in duration. So, in quarter 1, we have planned a 20-day shutdown for smelter-1. And the longer one is for smelter-3 between December and January wherein it's going to be close for about 1.5 months. So, in terms of production loss, it's directly based on the production per day, but the impact is after the shutdown, because you end up with a lot of improvements in all parameters, including process recovery, including the feed rate, uptime etc. So, it is more than made up by the improvement in efficiencies afterwards.

Rajesh Lachhani: Sir, so just to get this correctly, are we expecting our next year production to be lower than what we have done in FY '20? And would the cost be slightly higher than FY '20?

Praveen Maheshwari: No. That is not true because FY '20, we suffered some unplanned shutdowns. And this is actually in terms of number of days of operations, it will not be less next year compared to FY '20.

Moderator: Thank you. The next question is from the line of Vishal Chandak from Emkay Global. Please go ahead.

Vishal Chandak: Sir, my question was with respect to coronavirus in China and what is the kind of impact that you are seeing in the upstream business, especially for the aluminum in terms of smelting capabilities getting shut or impacted because of this entire thing?

Satish Pai: Look, I don't think that there has been any upstream aluminum smelting capacity shutdown because of the coronavirus. We have not heard of any smelter in China shutting down pots because of the coronavirus.

Vishal Chandak: So in that case, would it be a fair point to assume that the demand probably would be coming off unless and until there is a stimulus being offered in China, but at the same time, the production continues?

Satish Pai: So look, the reduction in LME had picked up in January to over 1,800. And with the start of the coronavirus, the LME corrected down because of that fear of Chinese demand impact. So, we'll have to wait and see till the full effect is known because anyway, it was during the Chinese New Year, which is a slow period, and one more additional week has been lost, and then people are going back to work. So, we'll have to watch and see. So, people are expecting the Chinese GDP to be impacted by some 0.3% to 0.5% in the calendar year quarter 1. So, the fuller impact on the Chinese demand, we'll need to see because people and the government are expected to pump in a lot of money into the economy to get the demand going. So how much the Chinese demand for aluminum will be impacted will be known probably in a little bit awhile after this whole thing calms down a bit. Too early to quantify anything right now.

Vishal Chandak: Understood, sir. Secondly, sir, my question was on the downstream product CAPEX that you mentioned in India. When can we see the production lines coming up gradually? As you mentioned, it's a modular CAPEX and depending upon the cash flows you will do. But for the cash flows that have already been spent so far, what kind of production run rate we can expect over the next 2 to 3 years' timeframe?

Satish Pai: So look, I think, next year itself, we will start to call out a little bit the downstream EBITDA, and you will start to see next year some of the positive impacts of that downstream investments will start to show.

Vishal Chandak: Okay. And sir, lastly, on this downstream CAPEX alone, if you could quantify the total CAPEX and the spend so far?

Satish Pai: So, as I told you, I think, this year, we have spent about 300 - 400 crores in downstream CAPEX.

Vishal Chandak: The cumulative CAPEX, sir, till date?

Satish Pai: Because this year was the first, I started talking about it, as you said, 2 years ago. The main CAPEX spend has been, I think we did about 100 - 150 crores in, what is it, '18/'19, then '19/'20 is current year, which is about 300 crores. So, we have spent about 300 - 400 crores so far.

Moderator: Thank you. The next question is from the line of Sumangal Nevatia from Kotak Securities. Please go ahead.

Sumangal Nevatia: So just wanted the hedge book position which we give regularly?

Satish Pai: Q4 FY '20, 39% of the aluminum is hedged at US$ 1,964 a tonne. So, 11% is rupee LME at Rs. 1,54,700 a tonne and 28% is commodity only at US $1,892 a tonne. And the currency is 38% hedged at 75.32.

Sumangal Nevatia: Okay. And what about '21?

Satish Pai: Yes. '21, we have 20% of the total commodity hedged at $1,864 a tonne. 1% is rupee LME at Rs. 1,70,640, and 19% is commodity only at US$ 1,836 a tonne. Currency is 28% hedged at Rs. 76.42.

Sumangal Nevatia: Okay. Sir, if you have the number, I mean, if you can simplify this, what sort of hedging benefits would we incur in the full year this year? And a large part of that will discontinue next year? So, do you have the number with you?

Satish Pai: So, this year, I think, the hedging benefit so far has been around Rs.1,000 crores.

Sumangal Nevatia: And is it fair to assume that large part of that will not continue next year?

Satish Pai: Well, it depends on your LME projection because we are 20% hedged on the commodity side at US$ 1,864, and we are 28% currency hedged at 76.42. And of course, we'll try to get the hedging levels. As you know, our strategy is about 25% to 30%. But we wait for the spikes to catch it.

Praveen Maheshwari: To answer your question a little differently. If the LME, let's say, goes up, let us assume it goes to $2,000, you will see some hedging losses in that case. But on 80% of the remaining open position, we are going to gain hugely. So I don't think you should really look at hedging loss or gain separately and make an assessment based on that.

Satish Pai: It's an insurance policy for us, we don't try to do it for speculative money making.

Sumangal Nevatia: Yes. And in between, sir, you said that Muri expense during 3Q was Rs. 77 crores. So where is this recorded, is it a P&L?

Satish Pai: Yes. The Rs. 11 crores is in the exceptional item and Rs. 66 crores in the aluminum EBITDA.

Sumangal Nevatia: So I mean, we have to add 66 crores, it's an expense, okay, I understand.

Moderator: Thank you. The next question is from the line of Kamlesh Jain from Prabhudas Lilladher. Please go ahead.

Kamlesh Jain: Yes. Sir, just one question on the Novelis part. So, if we see Q3 EBITDA margins per tonne basis, like say, historically, we have seen $50 to $60 reduction quarter-on-quarter. But in this quarter, we had seen roughly around double of that, like $125 reduction quarter-on-quarter. So, I do accept that there is seasonal element in that and destocking issues have been there. But are we going to see the improvement, like say, historically, which we have seen from Q3 to Q4? Like say, last year Q4, we had done $530-odd. So, are we confident enough to reach that particular level again in this quarter? Or there would be some weakness on those margin levels?

Steven Fisher: Yes. I have Devinder Ahuja, the CFO, is here with me too, and I think, he can address this question.

Devinder Ahuja: Alright. So let me first start by just pegging you to what you should be generally expecting. And as we have been saying very consistently that, broadly, you should be pegging around $420 to $430 per tonne. There are quarterly fluctuations. And what happened in this quarter, which led to a little bit of a lower EBITDA per tonne, was some destocking that happened in the specialty segment. So really, the specialty supply situation in the U.S. has actually gone through a bit of an oversupply case. And as a result of that, the buyers felt comfortable in keeping less inventories. There is enough availability. So, we saw some destocking impact on the specialies side. So really, there were some lower volumes. The other thing that you have to keep in mind is that with dropping premiums, particularly Midwest, and lower LME prices, the spread did normalize a bit or went down a bit. So, these are 2 factors which impacted us in this quarter. Again, coming to the point, quarter 4 should normalize a bit more. And in general, you should be expecting around $430 per tonne EBITDA. That is the guidance to keep in mind. So, this quarter had a couple of special items. And we are also comparing against difficult comps. Your question is sequential, but if you really think about what happened historically last year, we had the opposite. There was heavy buying because of all the trade war situation. As a result of that, we got a bump. So, we are just tiding over some market rebalancing situations.

Moderator: Thank you. We take the next question from the line of Rajesh Lachhani from HSBC. Please go ahead.

Rajesh Lachhani: Sir, so this is the question to Steve. So earlier, we were expecting the Novelis EBITDA per tonne to be higher than $400 per tonne. But since we have recorded $430 and this is the EBITDA per tonne now you're expecting, so have we reached a higher sustainable EBITDA per tonne at Novelis? And also, since we'll be also seeing some product mix improvement from next year, can this EBITDA per tonne also go up higher than $430?

Devinder Ahuja: Yes. So, let me try to answer this. So, we were reaching EBITDA levels in the last 2 quarters, quarter 1 and quarter 2 of the fiscal at levels of $448/ton, as you would recall. And we kept coming back to the point that we should be expecting more around like a 430 level. There could be quarters which are below. There could be quarters which could be slightly above. So broadly, like quarterly fluctuations taken into account, $420 to $440 are levels that we should be generally expecting. Now when you ask about sustainability from an operating perspective, this is a sustainable level. We are running at high-capacity utilization. We have been getting the benefit of mix change of higher volumes. And so that is all reflected. Therefore, the answer is that the earlier guidance of above $400 to now a range of around 420 to 440, basically, sort of addresses the point about improving utilization levels, improving mix and all of that. The things that we are not able to, obviously, predict is what happens on metal prices because then that impacts the scrap spreads, and that will be unknown, that one has to keep in mind. So all in all, this is a kind of direction that I can provide to you. So subject to metals, this is the level at which we should be sustaining ourselves.

Rajesh Lachhani: Understood. Sir, but just if the spreads remain where they are currently, if the product mix is improving in FY '21 because of the output from the Kentucky plant, shouldn't that further improve the sustainable EBITDA per tonne?

Devinder Ahuja: Well, yes, I would say, it should. But then I would not speculate too much on giving you a forward guidance, as things happen, as we see the capacity utilization because it's not like right in the first year, we will be working at high-capacity utilization. The ramp-up takes a bit of time. And in the beginning, because of lower-capacity utilization, the EBITDA per tonne will not so quickly ramp up. I mean, if we are starting a 200 Kt plant in Kentucky or a 100 Kt plant in China, the ramp-up will take, like, at least about 1.5 years. And as it reaches those ramp-up levels, the answer to your question would be, yes, it should go in the positive direction. But as the ramp-up phase happens, the costs are there in the beginning. But the capacity utilization levels take time and therefore, we will have to go through a period of a bit of a muted EBITDA per tonne. I hope you understand what I'm trying to explain.

Moderator: Ladies and gentlemen, that was the last question. I now hand the conference over to the management for closing comments.

Satish Pai: Thanks, everyone, for being on the call. And I think, as we said, we are going through, I think, for Novelis a good period, and hope we can close Aleris soon. And I think on the India side, we are hoping that post the coronavirus, the LME will stabilize as it had started to do at the beginning of January. And we will just continue to focus on keeping our operations and costs under control. So, thank you very much for everyone participating on the call.

Moderator: Thank you very much, sir. Ladies and gentlemen, on behalf of Hindalco Industries Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.