"Hindalco Industries Ltd Q1 FY19 Results Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Hindalco Industries Limited Q1 FY '19 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 '*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Subir Sen. Thank you and over to you, sir.

Subir Sen: Thank you, and good evening and a very good day everyone. On behalf of Hindalco Industries Limited, I welcome you all for this Earnings Call for the first quarter FY'19.

On this call, we will be referring to the 'Investor Presentation', which is already uploaded in our Company's website. Some of the information on the call may be forward-looking in nature and will be covered by the safe harbor language on Slide #2 of the presentation.

As you know the financials includes relevant numbers of Hindalco's 100% subsidiary, Utkal Alumina International Ltd., that is Utkal, to present the comprehensive view of the business. For this purpose, standard principles of consolidation have been applied, for the elimination of intercompany transactions, unrealized profits in the inventory. For comparison, previous year's numbers have also been presented in a similar manner.

On today's call, we have with us Mr. Satish Pai Managing Director along with Mr. Praveen Maheshwari – Chief Financial Officer and Mr. J. C. Laddha – Head of Copper Business.

Now, let me hand over this call to Mr. Pai for his opening remarks. Thank you and over to you, sir.

Satish Pai: Thank you, Subir. Good Evening or Morning, everyone. Welcome to our earnings call for the first quarter FY'19 of Hindalco Industries Limited.

Let us move on to Slide #3. I will start by giving you the Key Highlights of the Company's performance in Q1 FY'19. This will be followed by an update on macroeconomic and industrial environment. Later on, I will be covering operating performance of all our business segments in more detail and Praveen will elaborate on the financial performance in this quarter.

Let me start with Key Highlights, starting with slide #5: It was a record-breaking quarterly performance for Hindalco. Our Indian businesses have achieved the highest quarterly EBITDA of Rs.1,951 crores versus Rs.1,661 crores in the corresponding quarter, up by 17% on account of supporting macros, higher by-products realizations in the copper business. This was partially offset by increase in input cost mainly in coal and furnace oil. Profit before tax was up 68% at Rs.1,007 crores on account of lower interest outgo and higher EBITDA. Profit after tax this quarter doubled to Rs.734 crores, up by 102% compared to the corresponding quarter last year.

The net debt-to-EBITDA continues to be below 3 at 2.57 times as on 30th June 2018 versus 2.67 times at the end of March 2018. This shows our continued focus towards maintaining a strong balance sheet. In Q1 FY'19, our Aluminium business EBITDA was Rs. 1,531 crores, up 35% versus the corresponding quarter with an EBITDA margin of 27%, this is the highest in the last 28-quarters. This is despite the fact that the business face headwinds on account of oversupplied domestic market due to high imports and high input cost mainly coal and furnace oil.

With respect to production, the company achieved consistent Aluminium production of 323 KT versus 321 KT in Q1 last year. Alumina production was at 695 KT, marginally lower compared to corresponding quarter last year due to a planned maintenance shutdown in one of the refineries.

Moving on to Slide #6, the copper business also reported a good set of numbers despite lower volumes on account of a planned maintenance shutdown of around 23-days in Q1 and there was some additional days in July 2018. The plant is now fully operational. The copper business did an EBITDA of Rs. 335 crores in Q1 FY'19, higher by 4% compared to the corresponding quarter, mainly due to supporting macros and improved realization of by-products like DAP and sulphuric acid. As I mentioned, because of the shutdown of one of our smelters, cathode production was lower at 81 KT versus 109 KT in Q1 FY'18. Our CC Rod production was higher at 61 KT due to the benefits coming from the commissioning of the new CCR#3 rod mill which is ramping up well and that has added 24 KT in Q1 FY'19. The DAP production is getting back to normal this quarter and 70 KT in Q1 versus 67 KT in the corresponding quarter.

Coming to Novelis performance for the quarter, I hope you must have gone through the full financial results that was declared on 7th of August. I will just share with you some key highlights of its performance. Novelis reported yet another strong performance this quarter as well. Overall shipments have gone up by 2% YoY and the automotive shipments were also up 3% in Q1 versus the corresponding quarter. It has achieved the highest ever quarterly adjusted EBITDA of US $ 332 million with the highest ever quarterly EBITDA per ton crossing US $ 400 and reaching US $417 in Q1 FY19. This shows consistent growth in operational performance of Novelis. The net income was US $ 137 million in Q1 versus US $ 101 million in Q1 FY'18, up 36% YoY. As you must be aware, Novelis has signed a definitive agreement in July 2018 to acquire Aleris Corp. of US for an EV of US$ 2.58 billion and this deal is expected to close in the next 9to15 months. This is in line with our next phase of Aluminium value-added products growth strategy.

Let us now look at the broader economic environment in Slide #8. Global GDP continues to expand though amid divergent growth trajectories of major economies. The US economy performed strongly in Q2 CY'18 on the back of strong consumer and business spending as well as surge in exports. In Q2 CY'18, GDP grew by 4.1%, the fastest pace since Q3 FY14 at 4.9%. In the Euro Area, economic growth though moderated due to subdued consumer demand and political uncertainties. In China, GDP growth witnessed marginal moderation in Q2 CY'18. Post the eruption of trade war with the US the Chinese government, is providing key policy support to boost domestic economy. Among other emerging markets, growth in the ASEAN region is expected to stabilize due to robust domestic demand. The IMF has maintained its global economic forecast at 3.9% for CY'18. The occurrence of trade war between major economies and geopolitical issues are posing risk to global economic growth.

On the domestic front, economic growth continues to accelerate in the current financial year. The index of industrial production strengthened in April, May 2018 to 4% YoY as against 3% YoY in the corresponding period last year, on back of strong production in capital goods, infrastructure and construction and consumer durables. The PMI manufacturing index is also indicating growth in the economy as the index value remains in expansionary phase at 52.1 in April to July of '18 as against 50.7 in the same period last year. RBI has maintained the growth forecast at 7.4% for FY'19.

Now, I move on to the Aluminium industry overview in the next slide. Global consumption in CY'18 is expected to grow in the range of 4-5% on account of robust demand outside china. Consumption in China grew by 5% in the first half of CY'18 as compared to a growth of around 10% in the corresponding period last year. However, the recent policy stimulus and thrust on infrastructure by the Chinese government is likely to support demand in H2 of CY'18. Global production though, is likely to grow marginally by 1-2% in CY'18 as against the growth of 7.5% in CY'17, thereby creating a deficit in the global market including in China.

In order to improve air quality, China has announced a repeat of winter cuts in CY'18 also. According to Chinese government, mandated cuts would be implemented differently in CY'18 as compared to CY'17. In CY'17, production cuts were implemented across –the-board whereas in CY'18 the producers who had implemented cleaner production standards and have applied production cuts would face lesser mandated cuts or no cuts. In another reform, China is clamping down on illegal and outdated coal-based power plants. This move is in line with further tightening of emission norms.

The US has implemented 10% import duty on Aluminium products for countries which were exempt earlier like Canada, Mexico. The US government also imposed an anti-dumping duty of 167% on downstream products from China in order to protect their own domestic downstream industry.

The next slide talks about domestic industry outlook on Aluminium. Demand in the domestic market continues to accelerate due to robust demand from user industries. In Q1 FY'19, demand witnessed growth of 10% YoY to 924 KT as against 839 KT in the corresponding period last year. However, increase in low cost import of fake semis and wire rods from China and ASEAN countries, coupled with the surge in scrap imports impacted domestic demand for the primary metal. Cost of smelting in India is rising due to increase in coal price and constrained availability. Further due to elevated oil prices, furnace oil and other carbon related input costs are also rising.

Due to sanctions on UC Rusal, LME price of Aluminium touched 7-years high in mid-April '18 and the gap between the LME and China SHFE metal price also widened further to around $650 a ton. The sanctions on Rusal also impacted the global supply chain. As a result, regional premiums moved up in Q2 CY'18; however, with the extension of the wind down period, LME prices of Aluminium and regional premium witnessed moderation. But with the recent actions of the US government yesterday, again uncertainty has been created.

I now move on to Slide #11 on the copper industry overview. CY'18 started with the supply side concern due to labor negotiations. There were more than 40 mines that is around 7.3 mt, 35% of total mine production, which was supposed to undergo labor negotiations in Chile and Peru. Till now, all the negotiations have happened smoothly with some of them materializing ahead of schedule. Negotiations are underway at Escondida which is the world's largest copper mine.

Global demand conditions are broadly supportive especially after the stimulus announced by the Chinese government. We are expecting global demand for the refined copper to grow 3% to 23.6 million tons in CY'18. On the domestic front, the demand for copper recorded a robust growth of 12% YoY to 178 KT in Q1 FY'19. We are expecting demand for refined copper to continue the growth momentum in the remaining quarters of FY'19. Due to production disruption in the domestic markets, the share of imports touched 40% in Q1 FY'19 from 28% in the previous quarter. LME prices of copper were volatile during Q1 FY'19 due to trade tensions between the two largest economies of the world; however, LME price of copper witnessed the growth of 21.4% YoY in Q1 CY'19.

Now, let me come to the operating performance of our businesses on Slide #14: The Indian Aluminium units operated close to design capacities. Alumina production was marginally lower at 695 KT due to maintenance shutdown in one of the refineries. . Utkal continues to perform as the most economical alumina producer globally and continues to deliver excellent performance.

Aluminum metal production was consistent at 323 KT in Q1 FY'19, that was in line with the corresponding quarter as well as the previous quarter. On the value-added side, the production was maintained in Q1 FY'19 despite challenges with respect to continuous increase in the flow of imports.

Moving on to the operating performance of our copper business in Slide #16. As discussed earlier, production of cathodes were marginally lower on account of planned maintenance shutdown of around 23-days in Q1 FY19. The new copper plant CCR-3 commissioned in Q4 of FY'18 is ramping up well as per schedule. The overall CCR production in Q1 FY'19 was 61 KT which was up 56% compared to the corresponding quarter. The DAP plant is now operational and has achieved production of 70 KT in Q1 compared to 67 KT in Q1 FY'18 and 30 KT in Q4 FY'18.

I will now cover the operational performance of Novelis in Q1 briefly and then we will move on to the financial performance of all businesses. Coming to Slide #18, Novelis with its excellent operational performance increased asset efficiency combined with favorable market conditions has again come up with a strong quarter. Going shipments in automotive, product portfolio diversification and optimization of costs have helped Novelis to maintain its leadership position in the growing Aluminium flat rolled products market. Total FRP shipments in Q1 was 797 KT, up 2% with its increase in automotive shipments by 3% compared to the corresponding quarter. Automotive shipments of around 20 KT were impacted in Q1 FY'19 due to one-time events like the national truckers strike in Brazil and an unplanned downtime of North American auto customer. If this would not have been there, we would have achieved even better growth in automotive segment in Q1FY19. This is expected to be fully compensated by higher shipments in the coming quarters. Novelis has entered a new phase of growth with its announcement two weeks ago, to acquire Aleris Corp. Novelis also announced its plans to add 300 KT of new automotive ship finishing capacity with investments in the US and China. These projects are already underway, the sites are being prepared and we anticipate having both facilities to be online in calendar year 20 or 'FY21.

The Beverage Can market continues to remain strong in near and long-term as Aluminium remains a packaging material of choice for many beverage brands and demand continues to benefit from growth in emerging economies.

With that, I would now like to hand over the call over to Praveen for a more detail review of our financial performance.

Praveen Maheshwari: Thank you, Satish. Coming to Slide #20, this slide gives a brief snapshot, the key numbers for our financial performance during Q1 FY'19 and its corresponding quarters for Hindalco standalone plus Utkal. As we mentioned earlier, this presentation has been modified to include the financials of Utkal. Revenue in Q1 FY'19 stands at Rs.10,670 crores versus Rs.,10,414 crores in Q1 FY'18. It attained the highest ever quarterly EBITDA at Rs.1951 crores in Q1 FY'19 and was up by 17% on account of supporting macros, operating excellence and higher by-products realization in the copper business.

Profit before tax and before exceptional items in Q1 FY'19 jumped to Rs.1,007 crores in Q1 FY'19, showing a significant increase of 68% compared to Q1 FY'18 due to strong overall business performance and savings in interest outgo. As compared to the previous year, interest expense was lower by 23% due to prepayment and repricing of long-term loans in India. Profit after tax doubled at Rs.734 crores in Q1 FY'19 and was up by 102% versus Q1 FY'18.

Now, I will move on to segment wise performance: On Slide #21, we have given the performance of our Indian Aluminium business which includes the financials of Utkal as well. Revenue for Aluminium segment for Q1 FY19 was Rs.5,667 crores versus Rs.5,014 crores in Q1 FY18. EBITDA was up 35% at Rs.1531 crores compared to Q1 FY'18 on account of better macros and stable operations despite pressure on raw material cost. EBITDA margins were at 27% which is the highest in the last 28-quarters. If you wish to know the separate Hindalco standalone performance, they are available in the appendix to this presentation.

Coming to the financial performance of Copper business on Slide #22: Copper revenues in Q1 FY'19 were at Rs.5,006 crores versus Rs.5,403 crores. They were lower due to lower volumes on account of planned maintenance shutdown in Q1 FY'19 in one of the smelters. Despite this, EBITDA was higher by 4% versus Q1 FY'18 due to supporting macros and higher by-products realizations.

I will now take you through the financial highlights of Novelis on Slide #23: Novelis revenues were up by 16% to $ 3.1 billion in Q1 FY'19 versus $ 2.7 billion in Q1 FY'18. This was driven by higher average Aluminium prices, higher shipments and more favorable product mix. Novelis has achieved highest ever adjusted EBITDA of $ 332 million in Q1 FY'19 from $ 289 million in Q1 FY'18. This was mainly on account of increasing operating efficiencies, better metal spreads and effective cost management. Novelis has also reported highest ever quarterly adjusted EBITDA per ton at $417 in Q1 FY'19 versus $368 in Q1 FY'18 on account of favorable product mix, better utilization and recycling benefits.

With this, let me hand over back to Satish for his comments on the overall business performances and key takeaways.

Satish Pai: Let me now summarize on this slide our overall sustainable business performance and some key risks. During Q1 FY'19, we achieved the highest ever quarterly EBITDA on the back of our excellent operating performance across all our India businesses in Aluminium and copper despite increase in input cost, mainly coal and furnace oil and high imports. Profit this quarter doubled to Rs.734 crores compared to the corresponding quarter last year. We continue to strengthen our balance sheet as Hindalco standalone plus Utkal Net Debt-to-EBITDA has improved to 2.57 times at the end of June '18 as compared to 2.67 times at the end of March '18.

The Standard & Poor's have recently upgraded Novelis rating from B+ to BB- and its senior unsecured notes rating from B to B+.

On the growth opportunities, our CCR-3 is ramping up well after commissioning in Q4 last year and has produced around 24 KT in Q1 of this year. Our Utkal alumina expansion is on schedule and is expected to commission by FY'21 to take our alumina capacity to 2 million tonnes.

Novelis to acquire Aleris Corp. which will further solidify its position as the World's #1 aluminum value-added player. This transaction is expected to close in the next 9 to 15 months. You must have also seen Aleris' remarkable performance last quarter.

Demand for aluminum flat rolled products remains high for Novelis in automotive and also in beverage can segments. With its focus on product diversification and increasing the automotive share, it will continue to perform better. It has achieved in this quarter the highest ever quarterly adjusted EBITDA per ton of $417 in Q1.

Our key risk is majorly, the rising input cost, mainly the coal price and furnace oil prices. Also, increasing imports in both aluminum and copper to India will continue to remain a challenge.

Thank you very much for your attention. We will now open up for questions.

Moderator: Thank you very much. We will now begin the question-and-answer session. We will take the first question from the line of Sumangal Nevatia from Macquarie. Please go ahead.

Sumangal Nevatia: First, could you just comment on the coal cost, what is the inflation and how do you see it in the coming quarters, and also on caustic and carbon cost?

Satish Pai: Our integrated metal cost in Q1 of this year was flattish with the cost in Q4. Now, it was flat even though coal prices went up a little bit, furnace oil prices went up because fixed cost in the Q1 tend to be a bit lower. So, our fixed cost in Q1 was a bit low. So, the integrated cost in the metal Q4 to Q1 was flat. Now, more important, let us look at Q2. So, I expect the integrated cost of the metal to be about 3-4% higher in Q2 versus Q1 and majority of that will probably come from coal and furnace oil.

Moderator: Thank you. We will take the next question from the line of Pinakin Parekh from JP Morgan. Please go ahead.

Pinakin Parekh: Sir, my first question is regarding alumina. Now obviously alumina pricing is very-very strong. Just wanted to understand sir, within our older refineries either in Renukoot or other refineries, do we have a scope to increase production from them, I assume it would be higher cost because those are not fully captive bauxite based, but do we have the ability to extract more alumina in this current environment?

Satish Pai: Yes, good question, Pinakin. I think that our Muri facility certainly has a bit of capacity and we are going to try to do that, in fact, Muri sells excess hydrate into the domestic market already. Utkal also we will be trying. The only thing is this second quarter is a tough one because it is a monsoon quarter and it is raining very heavily in Odisha. So, we expect that we probably will only come into the third-party market in Q3, I doubt in Q2 we will be able to sell anything.

Pinakin Parekh: Sir, my second question is on copper. Given that this quarter was impacted by production, but it looks like the strong by-products credit environment has helped the segment. Now, from here volume should come back but sir how is the by-products environment holding out – is it as strong as it was in Q1, has it improved further, just trying to get a sense of the copper segment profitability?

J.C. Laddha: In Q2 also, the by-products realizations are almost the same as in Q1, slightly better and the result is basically because international prices of DAP is going up.

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

Rajesh Lachani: Sir, my question is with regards to aluminum. So, you had production of close to 323 KT but the sales were lower at 300 KT. So, basically can we expect good amount of sales more than production in 2Q? Secondly, you have also announced $1 billion of CAPEX for the next five years in the aluminum downstream. So, just wanted to get more clarity on what are your plans and what is the execution going currently?

Satish Pai: The first part of your question is we produce 323 KT and we sold 300 KT. So, two things are there in that delta of 23 KT. We had about 5 KT that was stuck in the ports that did not make it. But I think more important, we had about 8 KT that we have now adopted the new revenue recognition standard as per Ind-AS. So, in aluminum this year, the last few days of sales, we actually did not take it. So, it is a one-time impact that you will see in Q1. But from next quarter onwards, you would not. So, to answer your second question, I am expecting sales in Q2 to be north of 320 KT at this stage. But the 320-323 delta we were planning to sell roughly 313-314, about 8 KT we did not take for revenue recognition to bring it in line with IndAS. So, it is a one-time impact. Your next question on the downstream. On the downstream side, as I said, it is over the next five years. So, we have a series of projects ongoing and this year we have given the CAPEX guidance of I think about Rs.1,500 crores. So, the projects on the downstream are included in that Rs.1,500 crores. Normally, our sort of maintenance CAPEX tends to be around Rs.800-900 crores, so the extra Rs.600 crores you are seeing, some part of it is the Utkal expansion and some part of it is in the downstream projects.

Rajesh Lachani: Sir, I just wanted to understand what are the projects that we are planning and what could be the additional margins that we can see from these projects, so some clarity on these projects?

Satish Pai: On the projects, as I said, we are doing two things: One, we are upgrading our portfolio, so we sell about 300 KT of downstream, so the first part is to get technology quality to upgrade it and then we will take that 300 KT to 600 KT with an expansion form. What we are expecting to see is that we are doing roughly $40, 50 per ton of EBITDA, we want to take it to $150 per ton of EBITDA. So, that is the end result we expect to see in another three to four years.

Moderator: Thank you. We will take the next question from the line of Sanjay Jain from Motilal Oswal. Please go ahead.

Sanjay Jain: Could you help us understand this improvement in the EBITDA sequentially in aluminum segment by about 300-odd crores, what will you attribute this to – is it purely LME or reducing cost of production was flattish sequentially, so how have the hedge played in this revenue?

Satish Pai: First, largely the aluminum EBITDA improvement is from the fact that the average LME was $2,259 compared to $2,159 in Q4. The cost of production was flat. So, it is coming from the macros. On the hedge, it is not much. Q1 notional hedge loss was lower. If you remember, when you guys had asked me in Q4, I had given you our hedging position. In Q4, the hedging loss was about Rs.198 crores whereas this quarter it came down to Rs.180 crores. So, it is not because much about the hedging loss, it is mostly because of the macros.

Sanjay Jain: Did you see higher product premium here?

Satish Pai: Yes, actually we did see. The premium if you look at MJP in Q1 was $129 Vs about $10, $15 less in Q4. So, roughly, we have seen an improvement of about $15 in the realized premium in Q4 to Q1 in India and not to forget the Rupee in Q4 was 64.3 and in Q1 was 67.

Sanjay Jain: So, when you said cost of production was flat, was it in dollar term or rupee term?

Satish Pai: Rupee term. Dollar term, it actually improved because I am now dividing by 67.

Sanjay Jain: Second question is, is the hedge position same or like would you like to update us on the hedge position?

Satish Pai: I will give you the remaining nine months position. I think last quarter I gave you the full year position. So, for the remaining nine months, we have 27% hedged at rupee LME at Rs. 1,40,000, so this is without the premium, it is just LME and rupee and 11% which is commodity only at $.2,274. So, that is our remaining hedge position for the next nine months.

Sanjay Jain: What was Utkal alumina production, I just want to understand the margins there? Is there any change in pricing policy there when you account Utkal?

Satish Pai: That is a good point. The first their production in Q1 FY'19 was 374 KT, so Q4 was 360 KT, the previous year was 380 KT, so roughly flattish, they are at their 1.5 million tons run rate. The transfer price in Q1 FY'19, we now changed from taking the Q-minus to the M-minus, that is the change we have made. So, the transfer price for Utkal in Q1 FY'19 was $527 versus in Q4 FY18 the transfer price was $445.

Sanjay Jain: But this should not affect profitability because …?

Satish Pai: No, it does not, that is why we give it as Hindalco plus Utkal, so it is all in the aluminum EBITDA now, there is no third-party sales, so it does not make a difference.

Moderator: Thank you. We will take the next question from the line of Abhishek Poddar from Kotak Securities. Please go ahead.

Abhishek Poddar: Sir, regarding the copper smelting, we know that the large copper smelter in India is not operating now. So, is it possible for us to increase the production from 400 to maybe your capacity of probably 500 KT?

Satish Pai: The way we answer that question is no, at this point we cannot increase our current smelting capacity, depending on heat rates you can get 5 or 10 KT more, but you cannot substantially improve. But the change that we are making which is very important is that before our copper rod and India is largely a copper rod market, not a cathode market, we used to sell roughly 150 KT of copper rod. With the coming of the new CCR-3, this year we plan to sell about 250-270 of copper rod. So, the domestic sale percentage will go up because we will be selling more copper rod. When you sell copper rod domestically more versus exporting cathode you should make at least $200 per ton EBITDA more.

Abhishek Poddar: What was the consolidated net debt number for this quarter and standalone as well?

Praveen Maheshwari: Consolidated including Novelis gross debt is Rs.54,000 crores, treasury is about Rs.12,000 crores, so net debt is about Rs.42,000 crores at the end of June '18.

Abhishek Poddar: This has increased mainly because of the working capital?

Praveen Maheshwari: Yes, it goes up and down in the working capital because So at, Novelis also because of the LME going up, working capital was higher and in copper business as well you have as the LME goes up your working capital will go up.

Abhishek Poddar: Could you also please give the net debt numbers for India including Utkal?

Praveen Maheshwari: Including Utkal, Hindalco had 23,300 crores of gross debt, 6,000 crores of treasury, so about 17,300 crores of net debt.

Moderator: Thank you. We will take the next question from the line of Hardik Shah from Max Life Insurance. Please go ahead.

Hardik Shah: One quick clarification with the debt. So, post the acquisition of Aleris and also the proposed CAPEX, what would be the peak debt that we see?

Satish Pai: When we did the road show, we said that Novelis net debt to EBITDA would be below 4 times and the consolidated net debt to EBITDA would be 3.3 times On closing, within two years, Novelis get down to 3 and Hindalco consolidated would be less than 3 times.

Hardik Shah: This 3.3, does it include the standalone CAPEX as well?

Satish Pai: It includes, yes, all the CAPEX as well as the organic expansion that we declared in Novelis and Hindalco India.

Hardik Shah: The rating agencies, have they given any indication for this 3.3 whether they are comfortable at further existing rating?

Satish Pai: That is why my comments I put out the Standard & Poor's have actually upgraded and you can imagine that the upgrading was done I think a couple of weeks before we announced, they were fully aware of the acquisition plans that we had and we had shared with them our balance sheet plans and our Net Debt-to-EBITDA going forward plans.

Moderator: Thank you. We will take the next question from the line of Ashish Jain from Morgan Stanley. Please go ahead.

Ashish Jain: My first question is on your downstream expansion that you are seeing, if I take the EBITDA, you indicated $150 on volume of let us say 0.6 mt, getting an incremental EBITDA of roughly $90-odd million and for that we are doing CAPEX of a billion dollars, is it like 19% ROCE kind of a project we are looking at?

Satish Pai: Actually, the ROCE that we are targeting is probably in the range of 11-12%. But the other important part you also need to take into account is that the Indian market on the primary side is already oversupplied and my competition is only in primary. So, the other delta you have to take into ROCE is that instead of exporting primary, I will be selling value-added in India. The same logic I just gave for the copper rod in my previous comment. So, by adding value-added portfolio, it allows you to sell domestically more and then the combined ROCE is pretty good.

Ashish Jain: Sir, your differential EBITDA between domestic and exports is only to the extent of the import duty on aluminum or it is much more than that?

Satish Pai: It is about Rs. 6,000 to 7,000.

Ashish Jain: Secondly, on copper, in response to a previous question, you said that we cannot ramp up copper smelting to 500 KT. Is this more like a technical reason?

Satish Pai: No, the smelter has got the certain capacity. You can get a better throughput by getting some better concentrate, but generally you cannot do a step change, if you have to do copper smelter expansion, we are evaluating it but that will take time. Our smelting capacity can be anywhere between 400-500 KT, depending on the concentrate mix that we get as well.

Moderator: Thank you. We will take the next question from the line of Ashish Kejriwal from IDFC Securities. Please go ahead.

Ashish Kejriwal: Sir, in one of the previous questions you mentioned that cost of production was flat QoQ, but coal and furnace oil prices went up. So, what is the change in the coal of furnace oil prices? Secondly, despite the fact that in second quarter our volume will be higher than what we sold in the first quarter, we are saying that 3-4% QoQ increase in cost?

Satish Pai: Regardless of the volume I am selling because I am producing consistently, so I am giving my cost on a consistent basis. Q1 cost as I said the coal cost had not gone up that much, I am seeing the cost has gone up in June which is why I am taking that run rate for Q2. This normally happens in the monsoon quarters, because as you can imagine the coal availability gets tight, rigs get adjusted, so the spot auction prices go up a little bit, linkage realization percentage comes down. So, I am giving you a sort of conservative estimate going forward that I see a combined 3-4% increase on a per ton basis. But let me repeat, on an EBITDA basis, Q2 will be more because I am going to be selling more volumes.

Ashish Kejriwal: Sir, why your fixed cost was low in first quarter?

Satish Pai: What happens is when you do a fixed cost, basically SG&A, Q4 tends to be the highest, Q1 tends to be the lowest, because we get allocations and all coming in from the corporate levels as well. So, that normally Q1 is our lowest quarter, Q4 is our highest quarter.

Ashish Kejriwal: Sir, secondly, we are going to ramp up our value-added production. But when we are seeing that for example this quarter also we sold less than what we sold last year because of maybe increasing imports. So, firstly, how is the domestic market you are seeing, and do you think that when we are going to ramp up production we will be able to sell more in the domestic market?

Satish Pai: It is our whole game in Hindalco, that is why I used to get to a higher caliber of downstream products in terms of quality. In Q1 what happened is wire rod imports went up. Wire rod is not a very high value-added and a lot of it came from Malaysia. So, wire rod is what we could call primary value add, with one step above ingots, then billets and wire rod. The way we have to differentiate our services versus competition is to go up the value chain which is what we are planning to do. That is #1. And #2. Imports has surged 20% QoQ and that is largely because of ASEAN - FTA and Chinese imports coming in which is in some ways impacted by the tariff war that is going on. We are working very hard and expecting the government to put some sort of quantitative restrictions or anti-dumping duties to make sure that this market distortion does not happen.

Ashish Kejriwal: Sir, what is the market size of this value-added products in India?

Satish Pai: It is roughly 40% of the 3.3 million.

Ashish Kejriwal: Out of this 1.2, 1.3 mt, we are providing 300,000 tons…?

Satish Pai: 300 to 350 KT counting the lower end as well. We are about 30% of the total India market right now.

Ashish Kejriwal: Secondly, in our P&L, we are seeing cash flow hedge which was other comprehensive income. Last quarter it was Rs.1,084 crores positive and this quarter it is Rs.633 crores negative. So, is it possible to explain what is it?

Praveen Maheshwari: This quarter has been driven more by the currency change. If you notice the rupee, dollar exchange rate has moved significantly between end of March and end of June 2018. So, that creates a notional depletion in the benefit that we already have in the results. So, that explains the movement in the hedging reserves.

Ashish Kejriwal: Is it because of that fact only our other income was low or is there anything else, other income down from 205 crores to 105 crores?

Praveen Maheshwari: No, that is very different. So, OCI is different, that is what I explained just now to you. Other income actually the previous quarter had some one-timer. There are two, three reasons, that is one. Second is as we repay some of the loans, the treasury is coming down significantly. So, once you have lower treasury, the treasury income is lower. Third, there was a sharp movement in the bond yields. So, that impacted the treasury income as well. So, this quarter we did not have any other extra income coming from anywhere else, it is purely a treasury income at a lower surplus and lower yield. None of the cash flow hedges are impacting the other income.

Ashish Kejriwal: Can we expect similar kind of other income going forward?

Praveen Maheshwari: Typically, we maintain about 4,000-5,000 crores of treasury and the normal yield that should be expected is about 7% per year. So, that is the normal that should be there but once in a while you can have yields going up and down and that may impact the treasury income plus you may see some one-timers coming in which can also inflate or deflate the treasury income.

Moderator: Thank you. We will take the next question from the line of Vikash Singh from B&K Securities. Please go ahead.

Vikash Singh: I just want to understand what was the differential in pricing from Utkal in terms of transfer from last quarter versus this quarter?

Satish Pai: It went from $445 in Q4 to $527 in this quarter.

Vikash Singh: Just looking at your realization, which is roughly $110 higher, while 50% or little higher is coming at $82 higher, so is the fixed cost impact was so much so that our entire EBITDA per ton for aluminum has improved so much?

Satish Pai: No, the EBITDA for aluminum has improved because of the macros. The LME went up from $2159 in Q4 to $ 2259 in Q1. The premiums realized were also up by $15 and the Rupee Dollar went up from 64 to 67. These were the major reasons, why the aluminum EBITDA went up. The overall cost per ton was flattish in Q1.

Vikash Singh: Sir, is it possible to give the increase in power cost per ton basis in absolute terms, the cost increase in coal and all that for Q4 versus Q1, you said that coal and furnace cost have increased, so in terms of absolute value, is it possible to give?

Satish Pai: No, I will give you in percentage terms, coal cost was up about 2%compared to Q4 and I think furnace oil was also in the similar order.

Moderator: Thank you. We will take the next question from the line of Bhaskar Basu from Jefferies. Please go ahead.

Bhaskar Basu: On the coal sourcing, what is the current mix and if I remember the Krishnashila linkage was due to expire in July or June, what is the status there?

Satish Pai: Yes, the Krishnashila- will be re-put for auction, somewhere in September of 2018 as per our expectations. The coal mix stays more or less as it was before; we got about 60% or so from our linkages, about 15% from our captive mines and about 20% from the e-auctions in Q1 .

Bhaskar Basu: In the interim, you would continue to get coal from Krishnashila is it till the auction is done?

Satish Pai: Yes.

Bhaskar Basu: Just in terms of your outlook for an increasing cost in the coming quarters, the 3-4%, it is largely driven by coal or the other carbon related components?

Satish Pai: Furnace oil has also got some part of it. I think more than half of it is coal. Because furnace oil by the way we use it in alumina calcining. So, that is why it has a smaller impact.

Moderator: Thank you. We will take the next question from the line of Kamlesh Jain from Prabhudas Lilladher. Please go ahead.

Kamlesh Jain: Sir, if I see the standalone P&L, if I just do the cost, divide by the aluminum sales volume, so aluminum cost per ton seems has gone by roughly around 7-8% QoQ? So, I believe there would be an element of alumina. So, when you say that there would be 3-4 increase, so is it only on the basis of like say not including the alumina transfer price or it is only on the basis of your excluding alumina cost increase?

Satish Pai: It is excluding alumina cost. When I talk about cost of production, I take integrated cost. Alumina cost increase would be much higher because alumina prices have gone up a lot.

Kamlesh Jain: In the case of copper, next quarter, could we see around a lakh ton of sales volume?

Satish Pai: This quarter we produced about 80 KT and next quarter is also going to be probably similar because the shutdown took up some part of July18 and then the ramp up will take some time. I think you will see the volumes of copper in Q2 to be flattish but then Q3, Q4 should go above 1 lakh.

Kamlesh Jain: The margins would be much higher because of value-added products and then DAP higher realizations?

Satish Pai: That is correct, copper performance in Q2 will be better than Q1.

Moderator: Thank you. We will take the next question from the line of Ashish Jain from Morgan Stanley. Please go ahead.

Ashish Jain: Sir, earlier in the call you indicated that on account of hedging, there was a loss of around roughly Rs.180 crores in booking. So, how is that number moving from here on – should we see that number going down based upon the current aluminum prices and all?

Satish Pai: That is why I give you the rupee LME because then it just depends on the LME, you can make the calculation yourself. So, we are at Rupee LME hedge at Rs 1,40,000 for 27%, and only commodity hedge at $ 2,274 for 11% for the remaining nine months of this financial year So, it really depends on how the LME rupee moves. At current levels, the notional loss in Q2 will be lower because Q1 LME was $2,259, as when the US sanctions on Rusal came in, it spiked higher.

Moderator: Thank you. We will take the next question from the line of Dhaval Joshi from Haitong Securities. Please go ahead.

Dhaval Joshi: Sir, just a question on the copper business. What portion of the profitability would we have been benefited because of the switch which you mentioned from exporting cathode to selling domestic wire rod, as in was it a substantial portion during the quarter, we could see that moving materially in Q2?

Satish Pai: Copper rod-3 has just produced 24 KT in Q1 and we also had the shutdown. So, really we have not seen any benefit of that yet. That will probably come in Q3, Q4 when we start producing cathodes at the rate of 100 KT a quarter, then more of that will be sold domestically as rod rather than exported as cathode. So, that increase in my opinion you will start to see from Q3, Q4. Q1 was really good because of by-products realization and that continues, it will be slightly higher in Q2 as well.

Moderator: Thank you. We will take the next question from the line of Abhisar Jain from Centrum Broking. Please go ahead.

Abhisar Jain: Sir, first question is on the copper business. I think if I recollect correctly, at the end of last quarter call, you had mentioned that the copper division is looking to do 400 plus KT volumes in FY'19. So, are we remaining on track for that considering both first, two quarters are around 80 KT?

Satish Pai: Yes, because we have taken the shutdown in our planning. Have to admit the shutdown to come out a week more because of the rains but we are committing to that because post the shutdown the feed rates go up. So, we will be 400+ Kt.

Abhisar Jain: Close to 250+ out of that in terms of copper rods?

Satish Pai: Absolutely, that I am hoping we can beat a little bit because the copper rod-3 is ramping up well, so we should be able to probably to do better than that.

Abhisar Jain: Another question is on your view on LME pricing and the current aluminum prices. So, given the fact that alumina continues to remain strong on several disruptions in the alumina supply chain and also the coal cost remain on the higher side, is not the global cost curve gone up in the last six to nine months if you can give some comments on that? And then what is the outlook for the LME given that today it is lower than $2100 after all the volatility that we have seen?

Satish Pai: First part of your question, that is the global cost curve has gone up is absolutely correct. There are two things that are driving the LME. On one side is the fundamentals and other side is I would call market feelings because of trade war and its potential impact. So, let me take the part that we can logically assess which is the fundamentals. Fundamentals are that demand is very strong, Chinese production is quite restrained, China has already said that winter cuts will be repeated. So, if anything there should be a bias towards the higher LME in H2 versus H1. So, that is what the supply/demand and fundamentals tell you. Now, what is playing a little bit of motion here is the trade war and its impact. So, will that be good for the economy or not? This is what causing sudden upsides and downsides, copper prices also came down a bit because people were worried about the economy. That is little bit difficult for me to give you a view, but if I go by fundamentals of supply/demand and input cost, my feeling is that the LME has a bias towards the upper side in H2 versus H1 of this calendar year.

Abhisar Jain: Sir, if at all, with the data that might be with you, could you have any indication towards how much the cost curve would have moved in say last six to nine months for the global aluminum industry?

Satish Pai: This is a difficult part, because alumina prices have gone up by like 40%. So, it really depends as a producer whether you are backward integrated or not. If you are not backward integrated, your cost has gone up by some huge margin. So, it is very difficult to give you an average year. It really depends whether are you backward integrated or not. So, you take someone like us. Our cost curve remained flat and in dollar terms actually went down because the rupee depreciated. So, we look on the cost curve now, we are like at the complete extreme left end of the first quartile.

Moderator: Thank you very much. We will take that as a last question. I would now like to hand the conference back to the management for closing comments.

Satish Pai: Thank you very much. I think we had a great quarter and we think that with the increased sales and our operational efficiency, Q2 should also be more or less in line with Q1 and Q2, is normally our most difficult quarter in the monsoon, after that, Q3 and Q4, I expect to see us going back on the growth trajectory. With that, I thank you for your attention and would like to see you again in the next quarter.

Moderator: Sure, thank you very much. On behalf of Hindalco Industries Limited, that concludes this conference. Thank you for joining us, ladies and gentlemen, you may now disconnect your lines.