CENTURY ALUMINUM COMPANY: 4th Quarter 2023 Earnings Call

February 21, 2024/4:00 p.m. CDT

SPEAKERS

Jesse Gary, President, Chief Executive Officer & Director
Gerald Bialek, Executive Vice President and Chief Financial Officer
Ryan Crawford, Investor Relations & Financial Planning and Analysis Manager

ANALYSTS

John Tumazos, Analyst
Lucas Pipes, Analyst

PRESENTATION

Operator

Good afternoon. Thank you for attending the Century Aluminum Company Fourth Quarter 2023 Earnings Conference Call. My name is Matt, and I'll be your moderator for today's call. All lines will be muted during the presentation portion of the call. (Operator Instructions)

I'd now like to pass the conference over to our host, Ryan Crawford with Century Aluminum. Ryan, please go ahead.

Ryan Crawford

Thank you, operator. Good afternoon, everyone, and welcome to the conference call. I'm joined here today by Jesse Gary, Century's President and Chief Executive Officer; Jerry Bialek, Executive Vice President and Chief Financial Officer; and Peter Trpkovski, Senior Vice President of Finance and Treasurer.

After our prepared comments, we will take your questions. As a reminder, today's presentation is available on our website at www.centuryaluminum.com. We use our website as a means of disclosing material information about the company and for complying with Regulation FD.

Turning to Slide 1, please take a moment to review the cautionary statements shown here with respect to forward-looking statements and non-GAAP financial measures contained in today's discussion.

And with that, I'll hand the call to Jesse.

Jesse Gary

Thanks Ryan and thanks to everyone for joining. I'll start today by quickly reviewing our 2023 performance, before turning to the current macro environment and some dynamic operating conditions we are working through in Q1. Jerry will then take you through the details of the

fourth quarter results and Q1 outlook and then I'll finish with an update on the Inflation Reduction Act and potential further potential benefits that we expect to receive.

Turning to slide 3, market conditions remained volatile last year, reflecting a seemingly "new normal" we have experienced post-COVID where a broadly balanced global supply and demand picture for aluminum is paired with historically low levels of inventories. Tight global inventories along with rising and dynamic geopolitical tensions has created a market where small changes in market conditions are driving outsized effects on aluminum prices.

Despite this continued volatility, Century produced Adjusted EBITDA of $120MM in 2023, including $57MM of adjusted EBITDA in Q4, reflecting the impact of our 2023 Inflation Reduction Act Advanced Manufacturing Credit. Jerry will give you the full details here in a bit.

Our team completed several strategic projects last year, including the acquisition of our 55% share in Jamalco, completing our long-held ambitions to secure a captive supply of high-quality alumina and bauxite for our smelters to create a more balanced, consistent and robust operational footprint and better position us to deliver strong performance through commodity cycles. Returning this asset to its full potential will continue to be one of our main priorities in 2024.

Finally, we continue to focus on our most important priority, to return our employees home safely at the end of each and every day. While we will never be satisfied until we achieve zero workplace injuries, our team should be proud to have reduced injuries by 20% over 2022 levels. We hope to significantly improve on this trend in the coming year.

Market conditions for Century's businesses continue to reflect uncertain macroeconomic conditions in much of the world. As you can see on slide 4, global supply and demand remain roughly balanced and global inventories remain near all-time lows. The driving forces behind these balanced markets, however, are much more dynamic than years past and reflect the complexity of the current market.

Supply was largely constrained over the past year. In China, growth was limited by their 45MM tonne capacity cap and continued curtailments in Yunnan and surrounding provinces. Western supply also remained challenged over the past year by a difficult demand picture that ultimately led to the curtailment of two more western smelters in Neuss, Germany and New Madrid, Missouri. A bit further east, Russian metal continues to be disfavored in Western markets, where Russian metal today constitutes 90% of all LME inventories. There have been increasing calls for Russian aluminum sanctions in the EU and US, following the initial implementation of a 200% tariff on Russian products into the US and an EU ban on certain downstream Russian aluminum products into the EU.

On the demand side, Western world demand appears to have reached a low in Q3, driven by continued destocking across downstream users and challenging EU industrial growth. The market saw increased demand in Q4 and we now expect an improved and growing Western demand equation in 2024. Overall, we expect that western demand will return to its long-term growth rates as falling interest rates and improved GDP growth returns to the US and EU markets and the Inflation Reduction Act and similar spending programs in the EU and elsewhere continue to drive increased aluminum demand in automotive and renewable energy

applications.

The largest demand side story in 2023, however, was the strength of the Chinese market, where we saw Chinese demand growth of 5% in 2023 and expect to see similarly high growth rates this year. We estimate that the Chinese market imported about 1.3MM tonnes of non-Chinese production last year and we expect that to expand further this year. Chinese demand growth has been driven by the broad macro trends we have long expected, namely in aluminum-intensive electric vehicles and renewable energy applications. We expect demand growth in these areas to continue to accelerate this year, both in China and the West.

As we have discussed over the course of the past year, billet demand in the US and Europe has been a relative weak point in the market as post-pandemic destocking continued and increased imports of extrusions into both markets decreased domestic billet demand. Due to the annual contract structure for billets in the US, we were somewhat insulated from this downturn in 2023 by higher annual contract prices set in late-2022. Unfortunately, demand conditions for billets in both the US and Europe remained weak in Q4 and into Q1 of this year, which created a headwind in our 2024 billet contract negotiations and led to lower pricing that we expect will impact our Q1 results by around $10MM from Q4 levels.

Despite these near-term headwinds, we continue to anticipate very constructive long-term billet demand trends in both the US and Europe, as automotive lightweighting and renewable energy applications drive increasing aluminum consumption. We expect this trend to support significant long-term demand expansion for primary aluminum billet and slab in the EU and US.

In addition, as you can see on Slide 7, we expect that the pending US Anti-Dumping/Countervailing Duty trade case against extrusion imports from 14 countries will have a significantly positive impact on domestic US billet demand beginning in the second half of 2024. In August, the US aluminum extrusion industry filed suit alleging dumping and illegal subsidies by countries constituting over 68% of extrusion imports and over 27% of total US extrusion demand.

The US International Trade Commission has already determined there is indication of material injury to the US industry and in March and May of this year, the US Department of Commerce is expected to rule on the preliminary implementation of Antidumping and Countervailing duties against the subject imports. If implemented, the duties would immediately go into effect and are expected to have a material impact on the US extrusion and billet markets.

Just as an example, when antidumping duties were first placed on aluminum extrusions from China in 2011, imports of subject extrusions from China immediately dropped to almost zero due to the significant relief provided by the antidumping and countervailing duties and the domestic industry accordingly took back significant market share. We would expect a similar impact from this case if duties are leveled in March and May, meaning that the 27% of domestic extrusion demand currently met by the subject imports would have to be served by increased US extrusion production and a corresponding increase in US billet demand.

While we are not direct participants in the case, we have reviewed the case in detail and believe it is strong on the merits. If successful, the AD/CVD duties would benefit spot billet premiums in the second half of 2024, and we have accordingly left more of our second half billet volumes

open to potentially benefit from the higher pricing environment. The AD/CVD duties would remain in place for at least 5 years driving increased US billet demand across the period and beyond.

Turning to operations, we saw strong and stable performance across our smelters in Q4, while the Jamalco refinery continued to recover from the energy-related disruptions suffered in late September. We now expect that some of the production and cost efficiencies that we expected at Jamalco in Q1 will instead begin in Q2.

In Iceland, a relatively dry and cold winter has led to water levels in the nations hydro scheme falling below normal levels and the energy companies have accordingly issued partial curtailment orders across their industrial customers, including our Grundartangi smelter. These curtailments first began in early December and are expected to reduce Grundartangi's energy consumption by approximately 20MW, about 3% of our total load. We expect that the curtailment will finish by the end of April, but this remains subject to weather patterns and reservoir levels in Iceland. Based on the scheduled curtailment end date, we expect that the curtailments will reduce Grundartangi's 2024 production by approximately 3,500MT. This impact is included in our Q1 and full year volume guidance. It also impacted our Q4 production levels, and you can see the impact in the volume column on our bridge on Page 9.

Finishing out the energy picture, energy prices in the US have generally been constructive, driven by a mostly moderate winter and natural gas prices near $2. A nationwide mid-January cold snap did drive about a week of very high US power prices which we expect to have a negative impact of about $5MM in Q1. Other than this week of very cold weather, power prices have been very constructive and power price forwards have fallen significantly since the cold snap, reflecting the low natural gas price.

On the raw material side, we have begun to see many of our raw material imports begin to return towards historical, pre pandemic price levels, with coke, pitch and caustic soda prices moving most significantly downward over the past couple of months. Due to our contractual and physical inventory lags, the benefits of these price decreases will take some time to roll through our results, which Jerry will give you a bit more detail on. We do expect coke prices especially to continue to moderate further over the course of this year.

Finally, in light of the currently suppressed demand environment, we have implemented a new cost-control program designed to lower our spending while aluminum prices remain depressed. We of course have executed similar programs in the past and we are confident that we will be able to reduce costs and also our cash spending during this period. Jerry is leading this initiative for us and will provide you with the details. In light of the current environment and long-supply chains, we continue to work on our Mt. Holly restart plans, but do not expect that we will have any significant capital or cash requirements for the restart over the course of 2024.

Jerry will now walk you through the quarter and our Q1 outlook.

Gerald "Jerry" Bialek

Thank you, Jesse. Let's turn to slide 8 to review 4th quarter results. On a consolidated basis, fourth quarter global shipments were nearly 174 thousand tonnes, up 1 percent sequentially. Realized prices, however, decreased substantially versus prior quarter,

due primarily to significantly lower lagged LME prices and delivery premiums, resulting in net sales of $512 million, a 6 percent decrease sequentially.

Looking at Q4 operating results, adjusted EBITDA attributable to Century was $57 million, an improvement of $48 million compared with the third quarter. During the period, we recorded a full year benefit of $59 million related to the Inflation Reduction Act Advanced Manufacturing Credit Section 45X. Adjusted net income was $40 million or $0.39 per share. The major adjusting items were add-backs of $7 million in costs related to the Jamalco equipment failure, $3 million for the unrealized impacts of forward contracts, and $1 million for share-based compensation. We had strong liquidity of $312 million at the end of the quarter, consisting of $89 million in cash and $223 million available on our credit facilities.

Turning to slide 9 to explain the $48 million fourth quarter sequential improvement in adjusted EBITDA. In total, adjusted EBITDA for the fourth quarter was $57 million. Realized lagged LME prices and delivery premiums were significantly lower in the quarter. Realized LME of $2,182 per tonne was down $55 versus prior quarter, while realized US Midwest Premium of $425 per tonne was down $68 and European Delivery Premium of $280 per tonne was down $44. Together these factors amounted to a $19 million headwind in the quarter. Power costs increased by $1 million. Realized alumina cost was $382 per tonne, $13 lower on a sequential basis. Realized coke prices decreased 9 percent and realized pitch prices decreased 5 percent. Remember there is a 3–4-month lag for alumina, coke and pitch costs to work through our income statement. Together, alumina and other raw material costs resulted in a $14 million improvement in EBITDA.

Volume/Opex and premiums/mix were headwinds of $2 million, and $3 million respectively. And as I said earlier, during the period, we recorded a full year benefit of $59 million related to the IRA Advanced Manufacturing Credit.

For additional clarity, the IRA credit was calculated as 10 percent of production cost incurred, excluding direct and indirect material costs. Note the Department of Treasury is still considering including direct and indirect material as eligible costs. Jesse will elaborate further in his closing remarks.

With that, let’s turn to slide 10 for a look at cash flow. We began the quarter with $93 million in cash and ended December with $89 million. Capital expenditures totaled $30 million, $22 million of which relates to the Grundartangi Casthouse project. Semi-annual interest payments were $13 million and net debt repayments were $30 million. Working capital and other items contributed $68 million. We continue to maintain our focus on optimizing working capital, but as I mentioned last quarter, some of these savings are related to the timing of material flows which may reverse in subsequent quarters.

Let’s turn to slide 11 and I’ll give you some insight into our expectations for the first quarter of 2024. For Q1, the lagged LME of $2,190 per tonne is expected to be up about $8 versus Q4 realized prices. The Q1 lagged US Midwest Premium is forecast to be $416 per tonne, down $9. The European delivery premium is expected at $222 per tonne, or down about $58 per tonne versus the fourth quarter, but we have seen

improvement in EDPP in recent weeks with pricing earlier this week at nearly $250 per tonne. Taken together, the LME, and delivery premium changes are expected to decrease Q1 EBITDA by approximately $2 million versus Q4 levels. We expect power prices to be flat quarter over quarter, despite a $5 million negative impact from the January cold snap.

Looking at our key raw materials, lagged realized Alumina cost is expected to be about flat. We expect a favorable impact from lower coke and pitch prices. Caustic soda prices are trending down, as I'd like to remind you that it takes 5-6 months for caustic spot prices to flow through our P&L. All in, we expect lower raw material costs to contribute $5 to $10 million to EBITDA. The weak billet demand has driven Value-Added Premiums down. We therefore expect about a $10 million VAP impact to EBITDA in Q1. We expect volume to be a slight headwind, given the power curtailment imposed on our Grundartangi facility.

Finally, we expect OpEx to contribute $5 million to EBITDA in Q1. As Jesse highlighted in his opening comments, we have developed a robust playbook aimed at navigating the current demand landscape by effectively managing costs and preserving cash flow. We actively identify areas for efficiency enhancement, exercise prudence in discretionary expenditures, and diligently pursue cost reduction initiatives, all in pursuit of establishing a sustainable and financially sound operational framework.

All factors considered, our outlook for Q1 adjusted EBITDA is expected to be in a range of between $5 to $15 million. From a hedge impact standpoint, we expect no impact in the first quarter as we have very limited hedges in place. We expect tax expense of approximately $0-5 million. As a reminder, both of these items fall below EBITDA and impact Adjusted Net Income.

Now referring to slide 17 for full year 2024 financial assumptions. We expect shipments to be flat compared to 2023. In line with our objective to conserve cash, we are managing spending very deliberately. We do expect to invest approximately $10 to $15 million in sustaining CapEx and about 10 to $15 million in Jamalco. In addition, investment of approximately $15 to 20 million remains on our Iceland casthouse project, which will be funded in Q1 from our dedicated Grundartangi casthouse credit facility. The impact of the hedge book will vary with market conditions throughout the year, but to assist with anticipating these impacts on a go-forward basis, we have updated our previously reviewed Financial Hedge Landscape which can be found on page 19 in the appendix. Note, we have no remaining Nord Pool exposure in 2024.

And now, I'll turn the call back over to Jesse.

Jesse Gary

Thanks, Jerry. If you turn to page 12, I'd like to finish with some additional discussion regarding Section 45X and our expected benefits thereunder. As we discussed in December, the proposed regulations clarified many aspects of the law but Treasury asked for comments on several others while specifically highlighting the important "role that critical minerals like aluminum play in the renewable energy and energy storage industry."

First and foremost, the proposed regulations confirmed the application of Section 45X to substantially all of Century's primary aluminum production in the United States. The proposed regulations also clarified that eligible costs that qualify for the 10% credit are to be construed broadly to include all costs incurred by the producer in the production of the critical minerals, other than certain direct and indirect materials costs.

Importantly, the Treasury Department also specifically notes that it is still considering adding direct and indirect material costs as eligible costs under Section 45X and requested comments regarding how such costs should be treated for purposes of the critical minerals tax credit.

We are discussing with Treasury the essential nature of these materials and the significant associated costs, as indeed, it would not be possible to produce US aluminum without materials like alumina and carbon anodes. Our position is in line with a broad set of industry participants, ranging from critical mineral producers to our downstream customers, including automotive companies seeking to ensure stable domestic supply chains. Overall, there seems to be broad consensus amongst industry and consumers that such costs should be eligible for the tax credit and we are very hopeful that they will ultimately be included as eligible costs.

Importantly, Senator Manchin, along with several of his colleagues, recently submitted comments to Treasury noting that their intent as drafters was for the direct and indirect material costs to be eligible and they called on Treasury to expeditiously revise the regulations accordingly.

If direct and indirect material costs are ultimately added as eligible costs under 45X, we would expect to recognize an additional annual benefit of $50-$55MM for 2023 and similar annual amounts for 2024 and going forward. Any potential increases in future production would also be eligible for the production tax credit and would be expected to increase our annual benefit on a roughly pro rata basis to the amount of increased production. We will continue to update you as we receive more guidance from the Treasury Department.

We look forward to your questions today and will turn the call over now to the operator.

Questions and Answers

Operator

We will now begin the Q&A session. (Operator Instructions) The first question is from the line of Lucas Pipes with B. Riley. You line is now open.

Lucas Pipes

Thank you very much, operator. Good afternoon, everyone. My first question is following up on the 45X commentary. And specifically, I understand there's a process for the review of the direct and indirect costs and including that in the benefit. But I wondered if you could maybe elaborate on kind of what the process looks like from here? What's the potential timeline? What is the IRS looking for to make a determination on those? Thank you very much.

Jesse Gary

Hi, Lucas. First of all, I'd just like to say we're very thankful for the program, and the proposed regulations clearly have a material benefit for Century and also for US aluminum production. To your point on process, we are working with Treasury on the proposed regulations, which, as I mentioned in my comments, included several questions for industry and other participants about which costs should be included as eligible. There's obviously been a lot of support coming in from industry and also from some of the drafters of the bill, which is obviously important to the ultimate intent of the law. So, we do think there's good potential for more benefit to come, but it will obviously depend on the process.

So these regulations, as we call them, are proposed regulations, and the process will be -- there's a comment period, which a number of comments have already been submitted. And there also will be a hearing. And then after that, Treasury and the IRS will take that feedback back. And we'll ultimately issue either another set of proposed regulations or set of final regulations. There's no prescribed timeline there. So, we'll just have to wait and see when we see the next set of proposed or final regulations.

Lucas Pipes

Thank you. And do I remember it right that some of the hearings are tomorrow? And, do you have a view on or do you know when the comment period might close? Thank you.

Jesse Gary

Yes. The mutual comment period is already closed, Lucas, and the hearing is in fact tomorrow.

Lucas Pipes

Very helpful. Thank you. And then I wanted to ask about Hawesville. I'm curious, kind of, if you could share your views on where that asset could sit on the US cost curve with lower energy prices more broadly with the 45X credit. There was a recent announcement about a curtailment of a smelter in the Midwest. So kind of curious what might be similar or different in Hawesville compared to that asset that's idled, or maybe, again, more broadly on the cost curve? Thank

you. Thank you very much.

Jesse Gary

Sure, Lucas, a good question. Yeah, so we were very sad to see the announcement that the New Madrid smelter in New Madrid, Missouri closed earlier this year. But, obviously, each and every smelter in the US has its own mix of costs and circumstances, and it's difficult to really make broad generalizations or comparisons across them.

With respect to Hawesville, specifically, we have obviously seen power prices in the Midwest return towards attractive levels, mainly driven by the low price of natural gas, but also as additional renewable energy is built in the grid, and it's actually quite rewarding to see just how green the overall Midwest power environment has become.

So, with respect to Hawesville, specifically, I think, as we said before, it'll be a holistic decision based on many factors. Obviously, the power price situation is helpful and when we have final guidance on the IRA credits, that will also be very helpful towards making that decision. But we'll evaluate all factors at the time, including, you know, our corporate allocation of capital, power supply, LME outlook, and restart costs. Of course, our first priority as we said before, will be restarting at Mt. Holly. And as I mentioned, we continue to work on that and make some progress.

Lucas Pipes

Thank you very much for that. I'll try to squeeze one quick one in on Jamalco. First, could you provide some color as to the contributions of Jamalco to Q1 EBITDA on an attributable basis? And then the $10 million to $15 million CapEx for 2024, is that kind of a good steady-state number for your interest in the asset? Thank you.

Jesse Gary

Yeah. So, obviously, as we continue to work on Jamalco and bringing it back to its full potential, which, as I've said before, we're quite confident over time. We will return the asset to producing in the second quartile of the global cost curve. But we did have a few headwinds in Q4 and into Q1 when there were some delays in the restoration of some of its high-efficiency boilers. And we continue to have a little instability coming out of the energy-related disruptions we had towards the end of Q3.

So we now expect some of those production and cost efficiencies that we had previously talked about to be achieved in Q2 rather than in Q1. But we do expect Jamalco to be roughly breakeven on an EBITDA basis in Q1. Obviously, there's some of the quarter to go still. And then as we see the production and efficiency improvements take hold, we think that EBITDA generation will improve in Q2 and beyond.

Sorry. And then to your CapEx -- to your CapEx questions, Lucas, $10 million to $15 million reflects some of those restoration projects that we have in place in the powerhouse that we've talked about before. So there's a little bit of mix of investment and sustaining CapEx in there, Lucas. So we'll just have to watch that, and we'll continue to guide you as we go forward on that CapEx breakdown in future periods.

Lucas Pipes

I really appreciate all the color. I'll turn it over. Best of luck. Thank you.

Jesse Gary

Thanks, Lucas.

Operator

Thank you for your question. The next question is from the line of John Tumazos with Very Independent Research. Your line is now open.

John Tumazos

Thank you. With spot natural gas well under $2 and the Henry Hub recent $2.50, how are long-term electricity prices behaving? Have long-term prices fallen? Is this an opportune time to contract wind or solar renewable energy from Mt. Holly or Sebree? And if there ever was a time to think about Hawesville, I would think it's when natural gas is almost free.

Jesse Gary

Thanks, John. It's a good question. Unfortunately, natural gas isn't quite free yet, though I agree that would be a good environment. There's a few things going on in your question. So on Midwest and US power prices generally putting aside the cold snap we had in January, they have been very constructive in the back half of last year and now certainly in the first quarter of this year, putting aside that brief week of very cold weather. So you've got the range right. You know, you've seen them trading with low gas prices in the high 20s and low 30s over the balance of 2024. And you have seen the near part of the curve come in and reduce back towards sort of pre-pandemic levels in the Midwest.

On the renewable side, however, you continued to see renewable supply chains be very stretched, and renewable prices remain well above pre-pandemic pricing levels for renewables. So it's pretty dynamic out there. There's a lot of things going on. It's kind of hard to make broad generalizations of the overall energy environment, and, but, certainly, it is a bit more constructive for Sebree as we continue to operate there.

John Tumazos

If I can ask another, with your 5% demand growth estimate for last year from China, does that mean Chinese exports fell last year?

Jesse Gary

Yeah. When you look at -- and you can sort of take a broader look and look at imports level, we saw about 1.3 million tonnes of aluminum going into China. The window was certainly open for most of the year, and largely that was based on very strong demand for EVs and

renewable energy applications within China.

So then your corresponding question on exports is a bit more complex because you did see a lot of that demand go into not semis exports, which are easier to track, but more complete downstream demand applications. And it's a bit harder to say exactly, but what we can see is that the drivers are those long-term demand drivers for aluminum we've long talked about, which is increasing aluminum intensity in electric vehicles and increasing aluminum intensity in renewable energy and renewable energy transmission applications.

John Tumazos

Thank you.

Jesse Gary

Thanks, John.

Operator

Thank you for your question. (Operator instructions) There are no additional questions waiting at this time. So I'll pass the call back to the management team for any closing remarks.

Jesse Gary

Okay. Thanks, everyone, for joining. And we look forward to talking to you after Q1. Thanks a lot.

Operator

That concludes the conference call. Thank you for your participation, you may now disconnect your lines.