Transcript

CENTURY ALUMINUM COMPANY: First Quarter 2008 Earnings

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SPEAKERS

Shelly Lair, Vice President and Treasurer
Logan Kruger, President, Chief Executive Officer, and Director
Wayne Hale, Executive Vice President and Chief Operating Officer
Michael Bless, Executive Vice President and Chief Financial Officer

PRESENTATION

Moderator: Ladies and gentlemen, thank you for standing by. Welcome to the First quarter 2008 Earnings conference call. At this time, all participants are in a listen-only mode. Later, we will conduct a question and answer session. Instructions will be given at that time. As a reminder, this conference is being recorded. I would now like to turn the conference over to our host, Shelly Lair. Please go ahead.

S. Lair: Thank you, Roxanne. Good afternoon, everyone, and welcome to the conference call. For those of you joining us by telephone, this presentation is being Web cast on the Century Aluminum Web site www.centuryaluminum.com. Please note that Web site participants have the ability to advance their own slides.

The following presentation, accompanying press release, and comments include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements relate to future events and expectations, and involve known and unknown risks and uncertainties. Century's actual results or actions may differ materially from those projected in these forward-looking statements. These forward-looking statements are based on our current expectations, and we assume no obligation to update these statements.

Investors are cautioned not to place undo reliance on these forward-looking statements. For risks related to these forward looking statements, please review Annex A and our periodic SEC filings, including the risk factors and managements' discussion and analysis sections of our latest annual reports and quarterly reports.

In addition, throughout this conference call, we will use non-GAAP financial measures. Please refer to the appendix, which contains the reconciliation's to most directly comparable GAAP measures. This presentation, including the appendix, is available on our Web site.

I'd now like to introduce Logan Kruger, Century's President and Chief Executive Officer.

L. Kruger

Thank you, Shelly. Welcome to the first quarter conference call, everyone. Participants joining me today are Mike Bless and Wayne Hale, and also, in Monterey, are Bob Nielson and Steve Schneider.

Let's move on to slide four, just to give you a bit of an overview of what's happened in the quarter. We believe we have had a good start to the year in our first quarter. The robust aluminum markets continue. The LME average somewhere around $2,729 per tonne in the first quarter. As you all know, this is an increase from $2,447 in Q4 of '07. Price support from a weak U.S. dollar, ongoing rising costs, and the continued ongoing demand in China is part of the support of this price. We do note that there are a number of supply side risks, as has been evidenced by some of the winter storm events in China.

The U.S. aluminum plants are operating well, and our production levels are at capacity or above at all facilities. Grundartangi in Iceland, the expansion is complete, and you'll note that our production at an annual rate run rate 268,000 tonnes in Q1. We've initiated site preparation at Helguvik, our new greenfield project, and we'll commence construction efforts in the second quarter of this year.

Additionally, we've acquired a 40% stake in the newly constructed carbon anode facility located in south China. This is part of our strategy to insure that we have access to materials important to our plants in Iceland. The Jamaica refinery project is moving into a full feasibility study with our partner, China Minmetals. We continue to pursue further growth opportunities. Overall, we've had a good start to the year and a good first quarter.

If we move on to slide five, there's more about the Helguvik greenfield project in Iceland. Material contracts, permits, and the project team are in place. The groundbreaking schedule for May, and the initial preparation of the site has already commenced. We continue to anticipate first metal in the fourth quarter of 2010. We are likely to be at the high end of the projection range for our Phase I. If you remember, we indicated a range of 150,000 to 180,000 tonnes of capacity per year for Phase I.

The project capital expected for the total full pipeline of 360,000 tonnes is in the order of $5,100 to $5,300 per annual tonne of capacity. You will have noted from previous discussions we've had with you that this project is front-end loaded on capital expenditure in Phase I. These include rectifiers and services, as we've discussed before. We're putting those in place, and they will be used to their full capacity, as we initiate the Phase II and Phase III.

If we look at the capital cost for Phase I, it's somewhere around $1.2 billion, and that's for the full 180,000 tonne capacity. This gives you an order of measure around $6,600 to $6,700 per annual tonne of capacity. 2008 spending on this project is in the order of about $200 million. At full production, operating efficiencies for this project are expected to exceed our world-class facility at Grundartangi. We have adopted and are using the most modern technology available, the Alcan Pechiney 36+ technology.

We move on to slide six, just a few comments about the market and the market fundamentals. As you will note from the slide, the forward curve has undergone significant flattening and an upward shift in the forward curve itself. Forward pricing indicative of strong markets over the longer-term. For example, 2013, the price looks at about $3,000 per tonne. Capital and operating costs are up globally. Energy, carbon, freight, just to name a few. China's high cost structure is continuing to add new production capacity in the fourth quarter. Greenfield and brownfield expansion projects costs are increasing and the length of time required to complete these new projects is ever increasing. And there continues to be developing supply side constraints around power.

YTD global consumption is about 6% over 2007. Particularly in China, 15% demand growth, China year-on-year. China's GDP for the first quarter is about 10.4% or 10.6%. Industrial production, which we track for demand growth, in China is 16.4%. This is despite the New Year in China, as well as the weather impacts. YTD, global production is about 8.7% over 2007. 13.5% supply growth has happened in China year-on-year.

Can we move on to slide seven? Just taking up a bit on the cost structure of China, this is just a composition of the fourth quarter out of the cost curve. China is a significant and growing percentage of the fourth quarter of smelter cost curve, and I think most of the production introduced in China goes into this quartile. Expensive power contributes to the high cost position. The Chinese government continues in its efforts to discourage the investment in power intensive industries like aluminum and steel. They have increased taxes. They have removed preferential power prices, and are ever increasing their regulations in a stricter fashion. It's expected that China will become a net importer of aluminum in 2009 or sooner.

Can we move on to slide eight? If we look at the aluminum inventory versus price, we anticipate the global market will be balanced or have a modest surplus in 2008. You'll have noted at the beginning of the year a lot of commentators were expecting a major surplus. This is moderated somewhat, as you know, of the production setbacks, both in South Africa and China, just to name a few. The days inventory remains low, less than 30 days, approximately 29 days of global demand.

A few comments on markets in the U.S.: the markets in the U.S. are subdued. The markets are soft and this is with the exception of the aerospace, which remains very strong. Midwest premiums strengthened to $0.045 per pound recently, and this is in the range of the historical averages.

Note on pricing on alumina, spot alumina prices are around about $428 per tonne. Cost pressures and supply side disruptions are ever supportive of this price structure as well. Overall, the aluminum market fundamentals remain strong, as indicated by current prices and the forward screen. And for discussion on the operations, I'll now hand over to Wayne.

W. Hale

Thanks very much, Logan. Let's turn to slide nine. Smelters continue to operate well during the quarter. In the environmental health and safety areas, the plant leadership's consistent execution of programs drove year-on-year improvement in safety, health, and environment. In particular, Grudartangi has seen a 40% reduction in their loss time injuries, as compared to year-end 2007.

Operations at the domestic smelters were in control and solid during the quarter. Reliability Excellence, one of the key strategic initiatives to improve the operations and reduce operating costs, was initiated during the quarter. Reliability Excellence is a marriage between operations and maintenance where they work together as a team to reduce breakdown, improve reliability, and reduce costs.

Jim Chapman joined the Century Aluminum team as VP of Operations at West Virginia. A former native of Ravenswood, Jim brings extensive operations and leadership experience to the plant. We're pleased to have Jim on the team.

In February, we were notified by Appalachian Power that they had filed with the West Virginia Public Service Commission for a 17% rate increase. We're working with the Public Service Commission staff and the consumer advocate to mitigate these increases and its impact on the Ravenswood plant.

Progress continues with the Big Rivers unwind to secure long-term cost based power for the Hawesville plant until 2023. Public hearings via the Kentucky Public Service Commission have commenced. We expected the unwind to be completed in the first half. However, this is a complicated process involving many people and constituencies, and now the unwind may not be completed until the second half of the year. As a result, in light of this potential delay, we're speaking with EON and other providers to explore options to cover the unpriced portion of our power contract for the second half of the year.

At Grundartangi, the operations continue to move from strength to strength. The operations are stable, purity has improved, and the control to costs are lower than they were in 2007.

If we move on to slide ten, I'll say a few words about our refining, mining, and metals sales and marketing. In so far as St. Ann Bauxite, they have shown a year-on-year improvement in safety. In operations, mine and rail tonnes were impacted by rain delays and truck availability. Ship production was reduced by ship availability as well. Despite these challenges, in-plant requisite inventory was maintained and there was no impact to our customers.

Recently there has been news of a work slowdown at St. Ann's to highlight the union's leadership concern about the lack of contract negotiations progress. Though there has been minimal impact to the operations, we are in discussions with government officials and union leadership to bring resolution to some of the more foundational issues. This is not unusual in Jamaica to have protracted labor negotiations, and we are working through the issues to achieve a satisfactory result for all stakeholders.

Gramercy Alumina Refinery met all production and cost metrics for the quarter. The plant is operating well with few problems.

Turning to sales and marketing, despite a year-on-year reduction of 2% in U.S. metal demand, we continue to see a strong demand for our premium products. Billet, in our segmented market, is extremely tight, as secondary producers are being impacted by tight scrap and higher natural gas costs.

The Midwest Premium, as indicated by Logan, has increased due to tight scrap market and higher fuel costs that have driven up the import costs.

Our finished goods inventories at all our facilities remain low to take advantage of the markets.

Now I'll turn it over to Mike, who will discuss the financials.

M. Bless

Thanks very much, Wayne. If we could turn to slide 11, as usual, in addition to referencing the slides, I will make reference to the financial information that's appended to the earnings release itself, as well as the reconciliation slides in the back of the slide deck. And so if you could have those in front of you, it'll make my comments easier to follow along with.

First, on the market, before we dive into the numbers, Logan made reference obviously to the fact that sequentially now Q4 to Q1, the market was up to the cash price, as he said, was up 12%. With a one-month lag, the cash price was up about 4%.

Turning to our realized prices, when you look at our average realized price worldwide, that's the average of our direct sales and our total sales in Iceland. On an as reported basis, our sales were up about 8%. Adjusting for the impact of the cash flow hedges, and I'll get to this in a moment, our sales sequentially, direct and total average realized price, were up about 4%, so right in line with the marketplace.

And now before I go on, so that I can set the context for the comments that I'll make, if we can just turn to slide 12 for a moment. We'll turn back to 11 in just a second, but 12, I think, is important, as we talk about the data this quarter and going forward.

This is the forward fixed price forward sales situation. This is a continuation of some of the information we obviously have been providing for a couple years now, but that we started providing last quarter. This looks at nine quarter's worth historically, ending with the one that just ended, of hedge actual settlements. The tonnes settled on the left and the actual dollars that we've paid out on the right.

And just to orient you, going back to the left, as you'll remember, what we said is that in 2008 versus 2007, the actual tonnes settled would be about the same. As you see, Q1 over Q4 was a little bit more, 59,000 versus 52,000 tonnes. Yet, the accounting composition of those settlements would change. That, after this quarter, that 9,000 tonnes of cash flow hedges are the end of our cash flow hedges, and that all the rest of the volumes going forward would be derivatives. And so, you see that major difference carried over to the right.

I just want to orient you. When you look at the dollar value of the cash flow hedges settled Q4 versus Q1 over at the extreme right-hand portion of the right-hand chart, $23 million last quarter or two quarters ago, now I should say, $7 million in the quarter just ended. That $16 million delta there is the difference between the cash flow hedges, and that’s the anomaly or the difference that I’ll reference here in some of the data that I give you. We’re going to come back to this chart later to talk about the cash, but if we could now flip back to 11, we’ll talk about the income statement and some of the rest of it.

Before we get to the income statement data, you maybe had a chance to see the operations data in the back of the financial information. From a tonnes basis, our domestic volumes were flat quarter-to-quarter, as we expected. We shipped in the quarter at an average rate of 533,000 annual tonnes, nicely above our rated capacity. As Wayne said, the plants are running extremely well.

In Iceland, as you've had a chance to see, and as Logan referenced, our volumes were up 2.4% sequentially, shipping at a 268,000 tonne annual rate, at the high end of our expectations, and we're quite pleased with that.

Turning to the income statement data itself, revenue, as you can see here, up on a reported basis, sequentially 9% or $39 million. If you adjust for that difference in cash flow hedges, that $16 million that we just looked at on slide 12, the revenue was up 5% or about $23 million. Deconstructing that $23 million, about 85% of it was due to the price and 15% was due to the incremental volume at Grundartangi.

Continuing down the income statement data, if you're looking at the data on the bottom of the earnings release, gross profit increased $36 million, as reported, $20 million excluding again the cash flow hedge delta.

Let me give you a couple major items that impacted cost of sales during the quarter, the first of which were our LME based costs. Those, as you know, are the costs of our alumina in the U.S., at Mt. Holly and Ravenswood where we purchase on an LME based contract basis, and our electric power in Iceland, which of course is indexed to the LME. Those two items in total were up, i.e. unfavorable about $6 million Q1 over Q4, about 50/50: $3 million alumina, $3 million Iceland power.

Raw materials, continuing a theme that we have seen, and obviously the industry is struggling with, Logan referenced our investment in the carbon plant in China. Raw materials were up, unfavorable again, $5 million quarter-to-quarter. Most of that is carbon, some fluoride and other materials as well. U.S. power costs up about $2 million, none of that is electric power. Our electric power costs at the three smelters were actually flat quarter-to-quarter. That entire $2 million is natural gas, about half of that at the refinery, our 50% share obviously of Gramercy, and the rest due to the modest amounts of natural gas we use at the smelting facilities.

Lastly, Wayne referenced how pleased we are with the operations at Nordural Grundartangi, and the operating costs there quarter-to-quarter, obviously exclusive of electric power, were favorable by $4 million, so we're very pleased.

Continuing down the income statement, let me make a couple comments about SG&A. First, to set the context, the Helguvik development costs are no longer being expensed on the income statement, consistent with GAAP, as we've been expecting. Those costs are now being capitalized in addition to the actual capital costs themselves, and we'll get to that when I make a couple comments about the cash flow statement in a moment.

You see on the face of the income statement $18.9 million in SG&A, and let me make a comment about that. About $6.5 million of that number is due to long-term compensation costs in excess of what we normally book, and I'll get to that in a moment. And so if you exclude that amount, the residual or about $12 million is in line with our expectations.

Now that $6 million, where did it derive from? About 60% of it, just under $4 million, is the accounting for the plan period that just ended. Our long-term compensation plans are in three-year increments, so this is the '05 to '07 plan that just ended and paid out a couple months ago. And, as you may know, our long-term incentive plans are totally based on common stock, and obviously the accounting for them depends upon the stock price at the time the grant is made. So the same number of shares, higher stock price translates into a higher charge than we had been accrued for. In addition, due to the company's financial performance and operating performance during the plan period, a higher payout was made as well. And so those two items conspired to push long-term compensation expense up about $4 million versus our norm.

In addition, the design of the long-term plans, going forward, has changed modestly. The target amount hasn't changed at all, but just the design of the plans has changed just a little bit. And due to that, the proper accounting for those plans has changed in that more of the expense needs to be recognized under GAAP, under FAS 123R, sooner than it did before, so we have a one-time, about $2.5 million recognition of that. And then we go back to the prior amount. So about $6.5 million of long-term comp expense in excess of what we would normally have.

Continuing down the income statement data, loss on forward contracts, as you can see, $448 million during the quarter, obviously from December 31 to March 31, the measurement dates, as Logan referenced, the forward screen traded up and flattened significantly. The cash through '09 prices, as we all know, increased somewhere in the mid 20 percentage points, and the 2010 through 2013 prices were up in the mid teens on a percentage basis.

A couple last comments on the income statement, the effective tax rate came in on an adjusted basis at 27.6%, right in the middle of our expected range. When we say adjusted there, if you go to the reconciliation slide in the back of the slide deck, you'll see this is consistent with the way we've presented it in the past. We excluded two items this quarter. One is the after tax marked to market charge. The second is a discrete tax item, a $2.9 million charge due to the fact that the State of West Virginia decreased their tax rate. As you may remember last year in ’07 during two quarters, we had a one-time or a discrete gain when the State of West Virginia increased their tax rate. It’s a bit counterintuitive. They increased their tax rate, which results in the carrying value of our deferred tax assets increasing. That increase gives rise to a tax benefit. And, therefore, we pulled that out, if you recall, last year in two separate quarters as an unusual item. Earlier this year, actually, West Virginia decreased the rate by a little bit, thus decreasing the carrying value of our deferred tax assets, thus resulting in a charge here. So we pulled that out as an unusual item in our adjusted EPS.

Turning to EPS next, lastly, excluding those two items, marked to market charge in the West Virginia discrete item tax, $1.37 based on 41 million basis shares and $1.28 based on 43.9 million diluted shares.

If we could turn back to slide 12 just to round out and talk a little bit about cash, the major item on the cash flow statement of course always is the use of cash to settle our derivative contracts. As you’ll see over on the right-hand side of this chart, in the red, $52 million this quarter, in addition to the $7 million to settle the cash flow hedges that we talked about a little while ago. And as you'll see there, the comparable amount in the prior quarter sequentially was $43 million.

A couple other items on the cash flow statement, capital expenditures, as I said before, Helguvik spending is now all on the cash flow statement. What you see on the Nordural expansion line now is all Helguvik, $7 million during the quarter. Other cap ex for the company, including spending on the Grundartangi plant, is in the normal cap ex line, about $9 million for the quarter. That's versus a budget for the year, as we discussed with you in detail during the last call of $75 million.

Lastly, I would just point out on the balance sheet, cash now stands just shy of $370 million, about $368 million. It grew from the end of December obviously, despite the cap ex, some interest and tax payments we make during the first quarter. And if you had a chance to look at the cash flow statement itself, you've seen a build of just shy of $20 million in working capital. All of that is due to the run up in the LME price.

And with that, I'll turn it back to Logan.

L. Kruger

Thanks, Mike. Just in summary, if you look on slide 13, strong market conditions continue. The Helguvik groundbreaking of the new project has started in the second quarter. Capital projects in the U.S. for incremental production are in place and are ongoing. We've invested in anode capacity in China. We've also moved our Jamaica refinery project with China Minmetals to a full feasibility study, which will take about the next 18 months, and we continue to pursue other global project pipeline items.

At this stage, I'd like to take the opportunity to invite you to ask some questions. Roxanne.

Moderator Thank you. Our first question is from David Lipschitz with Merrill Lynch.

D. Lipschitz Can you just quickly tell us what your calculating EBITDA? I know you usually give it in your presentation slides, but you didn't give it in this slide deck.

M. Bless You know what, David, we'll have to get that to you. It's not a number that we normally calculate for management purposes. You can do it based on our old basis, which is we've given you the roadmap in the past. I don't have it on hand, but we can certainly crank it and put it out there on the Web site if it's of interest.

D. Lipschitz Yes.

M. Bless Same methodology as we’ve used before. Obviously you can get the reconciliation charts, as you correctly referenced, from the back of at least the last sales side conference presentation, I believe we did it in. Yes. Shelly is saying yes.

D. Lipschitz Thank you.

Moderator Our next question is from Sam Martini with Cobalt Capital.

S. Martini Can you give a little bit more information on the carbon anode investment in south China? I apologize if you went through this in depth. I had to jump off for a minute, but just what are you putting in, what are you getting out? I’m assuming this is all going to – I don’t know if this is future for Helguvik or for Grundartangi current or anything. And then any just updates on kind of what you’re seeing in the carbon anode market globally would be helpful.

L. Kruger I’ll take a bit of the first part, and the Wayne and Mike will jump in. The facility is a two-phased project to produce the name plate capacity is around about 180,000 tonnes of anodes. We’ve taken a 40% position in this. We've been studying this for some period of time. The first phase is already in place and producing. I think Mike correctly – our investment is tens of millions of dollars.

M. Bless That's correct.

L. Kruger We're very happy with the quality of the anodes. We've tested them. We've reviewed them, and we see this as a strategic, as with other sources of supply of anodes, for the longer term for both Grudartangi and Helguvik. So I think that's the strategy. I don't know if Wayne and Mike.

W. Hale I mean just to your point, we've had the carbon reviewed by an independent party, and they are of very good quality and actually we have, as you recall, a test batch going to Grundartangi as we speak.

M. Bless I think the only other thing I would note, Sam, is that this new plant is a clone of one that the same operator has built a couple of years ago, has been operating successfully, has been producing quality anodes for the marketplace. And so while there's always a risk, we thought the risk here was, given the fact that, number one, it does mimic a plant that's been operating. And two, that our money went in, literally, as Logan referenced, as the first line came on-stream. The risk was nothing near sort of a normal greenfield risk, a plant kind of risk.

L. Kruger In the Guanxi province, Sam, as you know. We've been working there for some time.

S. Martini So about 0.6 tonnes anode per tonne aluminum, is that fair?

M. Bless Yes.

W. Hale Fair enough.

M. Bless Yes. That's close enough. Yes.

S. Martini And you'll get about 70 to 75 out of this thing when it's all said and done?

M. Bless That's what our equity stake is, Sam. That doesn't preclude us, obviously, from having an off-take that's greater than that. But I think you should look at that as a minimum of what we should get.

S. Martini And how bad has anode gotten? I mean has it gotten worse even from Q4, and what are you seeing for prices out there?

L. Kruger I think, Sam, the drive to source and keep reasonably consistent supply of strategic materials is going to be tested for everyone. It's part of the supply side risk, I think, and so we have had longer term and medium term contracts in place with multiple suppliers. But this one way where we have, can I say, better impact on what comes out and it gives us opportunities to defray our risk.

M. Bless And the spot market, to your question, Sam, has kind of stayed in there. To the best of our knowledge, it's kind of gone sideways over the last 90 days. As you know, the reference points are hard to find because it's such a thin market that a true third party merchant anode market is very thin.

S. Martini So this gives us some good visibility, as much or more than anything.

M. Bless You bet.

L. Kruger Correct.

S. Martini Thank you.

Moderator Our next question is from Mark Liinamaa with Morgan Stanley.

M. Liinamaa Could you go over your commentary with the Big Rivers unwind again? I want to make sure I understand the power situation there going into the rest of the year.

L. Kruger Sure. Just let Wayne take it. I'll make comment.

W. Hale Sure. I'll just talk about it again. The unwind is being reviewed by the Kentucky Public Service Commission now, and as I indicated, these discussions and the review publicly involves many people and many constituencies. And as a result, we had formally thought that this could be wound up and completed in the first half of this year. Now, however, it appears that it may move over into the second half of the year. And, as a result, if you recall, our unpriced portion of our power contract that has essentially been closed for the first half of the year with the exception of 5% and so again recognizing this potential, we're going to be out talking with EON and other providers to understand what power is available to close this position in the second half.

M. Liinamaa And does this create any sort of risk at all?

L. Kruger — I think the only risk is what is the price, but we've been doing this for the last period of time, so you know; it's just the pricing. I don't think it's a sourcing issue.

M. Liinamaa — So it's still a very, from your perspective, a very manageable situation relative to current operation.

L. Kruger — I think that's your question, yes. It's just a pricing issue.

M. Liinamaa — Good. Thank you.

Moderator — Our next question is from Oscar Cabrera with Goldman Sachs.

O. Cabrera — If you could, I missed part of the estimation you guys were giving on Helguvik. I understand the expansion there is between $5,100 to $5,300 a tonne. Now we had talked about a range from $4,500 to $5,000, and you said that at the top of the range, that would include an anode plant. So I just want to make sure that these numbers that you were giving us today reflects your partnership that you've gone into and how much do you think you can save in terms of cost. And then the second part of that, you also were referring to $6,600 a tonne. Can you just go over that again, please?

L. Kruger All right, Oscar. I'll try and set up the sequence and ask Mike, I think, and Wayne as well. I think we've always said that the new greenfield site, Helguvik, is not going to have a carbon plant. I don't think we've ever indicated we're going to have a carbon plant. If you misheard that one, our apologies, but it's never going to have a carbon plant.

Secondly, it's 100% owned by us as well. The approach on the project is no different to what we've been saying for the last year or so. It's going to be built in phases, and the phases are no different to our approach in the way we dealt with Grundartangi. The first phase initially was said to be 150,000 to maybe 180,000. We're now indicating at the higher end of that range. The capital investment for that range for the first phase, because you're pre-invested for the whole pipeline of up to 360,000 tonnes of capacity for a year, is about $1.2 billion. At the end of that, you do the arithmetic, you'll come out at about $6,600 per annual tonne of capacity. Completing all the phases to the full capacity of 360,000 tonnes by 2013, 2015, period will take that capital cost down to an average of about 5,100 to 5,300, and you correctly previously indicated somewhere between 4,500, but that goes back about a year, and we've now recognized that part of the impacts are these ongoing costs, including things like the aluminum which is a big number, steel prices, etc.

The project is south of Reykjavik, and we’ve got all the experience we’ve learned in Grundartangi obviously to apply to this project. I don’t know if Mike or Wayne want to add anything.

M. Bless — No, I guess, other than to repeat Logan’s point and just add a little detail. Oscar, as you remember, we did talk about 4,500 to 5,000, I think Logan was right, maybe about a year ago. We updated that to right around 5,000 when we spoke about it the last couple of times. The 5,100 to 5,300, as Logan said, for the whole pipeline, as you would normally expect with a project like this, has a contingency element in it. So the actual cost of that pre-contingency is less. We think it’s prudent to have the contingency for all the reasons that you normally have one on a project like this, and we think our contingency is kind of at the right quantum for the type of project we’re taking. That puts it into, I think, a context and brings it current. There’s a lot of work that Wayne’s team has done to get to this point.

L. Kruger — Any comments, Wayne?

W. Hale — No. I think you guys captured it well.

O. Cabrera I appreciate that, and then if you could just remind us. You said you were spending about $200 million for that in 2008. What kind of sequence should we be looking at until you start production at the end of 2010?

L. Kruger I think for the capital for the remaining two years, 2009 and 2010, those are your most intensive years in the field, as you would know. I would take at this point in time, until we update anymore, about 50% of the additional capital will be spent in each one of those years.

O. Cabrera Great. Thank you very much.

Moderator Our next question is from Dave Gagliano with Credit Suisse.

D. Gagliano First of all, just to follow up on Oscar's question, I was wondering if you could just clarify a little bit more on the Helguvik, the breakdown of the $1.9 billion in total capital by year from 2009 to, say, 2012. I didn't quite get that 50% comment.

L. Kruger David, we haven't got a breakdown that we are happy to give, but on Phase I, up to $1.2 billion. That will take the period '08, '09, and '10: $200 million in 2008, and then evenly split over '09 and '10. As you know, as the engineering develops and the schedule develops, you'll have fluctuations, so that's our best numbers that we can give you at this point in time.

D. Gagliano Sort of $350 million and $350 million in 2011 and 2012, is that fair?

L. Kruger No. David, $1.2 billion, maybe we've missed this one; $1.2 billion for the first phase up to 180,000 tonnes. That gives you the 6,600 per annual tonne of capacity for the first phase. That obviously goes down as you introduce a lower capital investment for Phases II and III.

D. Gagliano Right. I'm sorry. I was thinking Phase II and III in total gets you to $1.9 billion, so incremental is $700 million in 2012 and 2013.

L. Kruger Correct. Yes. We're targeting 2013 to 2015. Obviously we'll update you, you know, in the past, an additional, this is all coming from geothermal, so it does come on in incremental amounts, David. You know that and you've actually seen it, so I think that's important to understand. As these things develop, we'll update everyone.

D. Gagliano Fair enough. Moving on, just to switch over to the electricity rate increase question, if you do need to absorb the 17% rate increase, I'm just trying to wrap some numbers around it. What would be the total impact on your cash costs at Ravenswood for the incremental increase?

L. Kruger David, I'm going to ask Mike to perhaps answer that one.

M. Bless Yes. I have two comments. One, we'll answer the question by not answering it because, as you know, David, we don't quote cash costs. And two, but you know there are estimates out there for what our current power tariff at Ravenswood is. And two is to put some color around it, as you know, we, right now, are operating at Ravenswood through a lot of hard work that Wayne's team has done in the state under the so-called experimental rate, where at lower LMEs, the increases that have been imposed over the last 18 months are not forgiven forever, but are excused until metal prices go back up. We've talked about this many times before, obviously, and so you know we would hope and expect, I guess I would say, that that regime would continue. Though, it doesn't automatically continue. With a lot of hard work, we're hopeful that we can get it to continue, and so we need to all – obviously at the current metal prices, we're paying at the higher tariff rates based on the last two increases, but we do have that downside protection.

D. Gagliano Good. Thanks very much. I appreciate it.

Moderator Our next question is from Justine Fisher with Goldman Sachs.

J. Fisher The first question that I had was just a clarification on the prices. So is there always – there's always a one-month price lag for you guys versus the LME?

M. Bless Not much. The reason we quote it, Justine, is I guess, Wayne, much of our sales flows that way. I wouldn't say all, but much.

W. Hale A predominant amount is.

J. Fisher So the 117—

M. Bless In the U.S. anyway.

W. Hale Right.

J. Fisher So the 117 for the first quarter was, I guess, I mean it was significantly below the average. Should it be closer to the average going forward, or is that just in quarters where there's a massive swing in the LME price?

M. Bless There you go. If it was flat, then it wouldn't matter, right? But if it's up or down, for the sales in the U.S. anyway, most of those are made and we're no different than the rest of the industry in that respect.

J. Fisher Then I didn't see in the press release, so forgive me if I missed it, but the breakout of the impact of currency, because there's been some massive swings in exchange rates here. I was wondering, Mike, if you could break out the different, I guess the currency factor on cost in Iceland.

M. Bless Yes, indeed, and it was only – we didn't break it out because it wasn't material. It was about one million dollars, Justine, to the positive, that hit the bottom line. Because, obviously in the U.S., we're producing in dollars, selling in dollars. In Iceland, we're obviously selling in dollars and must of our costs, including electricity, remember, is in dollars. And we don't have any alumina there because of the tolling, so really all you're talking about is sort of the local krona based costs, those obviously being payroll and local taxes and local services and stuff like that.

J. Fisher Right. That makes sense. I didn't think about the fact that the power is all based on the LME.

M. Bless That's it.

J. Fisher — If you guys were to see an impact of currency, going forward, it might be on the capital costs.

M. Bless — It would be on the capital cost, and maybe you're bringing – it's an excellent. I'm sorry to cut you off, but we're doing a lot of thinking about it now. In fact, we have, and we talked about this last time, in advance of précising our capital costs and timing for the new project, we did go, when the market spiked a little while ago, and bought, against our operating costs, forward about 13 months. Shelly's group and the folks in Iceland caught the market reasonably well, and so we bought an average price of, you know I would say, close to 80, maybe even a little bit above, a little bit below, high 70s on a krona dollar basis against the operating costs. Now that we have the cap ex more defined, we are looking very carefully at how we will approach the capital costs for the new project. And as we announced or discussed in the past, of those numbers that Logan and Wayne were citing, roughly a third are krona based.

L. Kruger — Just to add to what Mike said, we're going to approach it no differently to taking some currency or risk out of the project, as we did for Phase V at Grundartangi, if you remember.

J. Fisher Then the last question I had was just about potential supply responses that we might be seeing to the current price rise in aluminum. And I know that we really saw a lot of mothball smelters come online over the last couple of years because of higher prices, but it seems as though there's little propensity for more to come on, but I was wondering if you even BHP, that's seen a comeback in South Africa. Are major producers or any new producers trying to increase production anywhere else in response to these prices?

L. Kruger I think the situation has been around for two years. I think we've seen reasonably attractive prices, so on the supply side response, everyone is running their plants at full utilization, so there's actually a supply side risk because everyone is running at 95% of service ability. In terms of the plants that have closed down, it's unlikely that I can see, and my colleagues can comment. I can't see a restart of existing closed plants. A lot of them have actually sold off key parts of their major equipment anyway, so they're really in the process of being decommissioned. Some of these happened in China and elsewhere, so I don't see it. Wayne may have some observations, but I don't see it, Justine.

W. Hale No. I think you make a good point. Those plants that are available have been decommissioned to the point that they are no longer restartable. Otherwise, they'd be in the market.

M. Bless Yes. You can read the industry analysts, and they'll say the same thing. There's a real live example in the marketplace right now. We don't like to cite the names of our peers, but there's a small plant in the U.S. that is currently for sale. It's a 90,000 tonne line. The operators, I just probably cited who they are – have obviously chosen not to restart it. And I think the scuttlebutt in the industry that the most likely, Wayne, result is for that facility to be bought for the equipment, either by an operator or more likely by sort of a broker type and part it out. So perhaps that's a real live answer to your question.

J. Fisher I heard Google bought a smelter. Seriously, it was one of the only places that had enough electricity for their service. Anyway, thank you.

L. Kruger I think also where's the power going to come through. I think you understand the challenge.

J. Fisher Thanks.

Moderator — Our next question is from Terence Ortslan with TSO Associates.

T. Ortslan — I'm just running up some numbers here. Could you remind me again please for 2008 what's your SG&A going to be and your depreciation and amortization and the cap ex one more time. Thanks. You probably mentioned it but I missed some of them.

M. Bless — No problem. The SG&A, as I referenced, we're still comfortable with the estimate that we gave on the last call, which is about $12 million a quarter. It can be lumpy, but that's still a good number on an ongoing basis. Cap ex, two parts I would answer that in. First, and this is both consistent with the guidance that we gave a couple months back, the non-greenfield Iceland plant cap ex, so for the rest of the company, including the existing plant, Grundartangi in Iceland, is about $75 million for the year, including sort of our normal amount of maintenance and sustaining cap ex in the $20 million $30 million range, and the rest being the expansion and ROI projects, about which Wayne spoke in detail last time.

Then last, D&A, about $85 million, let me break that into two parts. About $70 million is fixed asset depreciation and the rest is amortization, the remaining intangible asset due to the power contract. That's the annual rate. As we talked about last time, that amortization will go away upon the signing of the cancellation of the existing power contract at Hawesville and the signing of the new one, so that's kind of a moving target. If we didn't, per Wayne's comments, sign a new contract until the end of the year, it would indeed be $15 million, but it'll be pro rata, pretty much pro rata for when we close this new contract.

L. Kruger — I think, Terence, I would just add an item to remember is we're now going ahead with a full feasibility study on Jamaica, and obviously it's 50/50 with our joint venture partners, and we will be obviously expensing that as we go forward. As we develop more information, we'll obviously bring that to the table.

T. Ortslan — Just one question on your slide seven, sorry, to just round it up, slide seven, the composition of the fourth quartile cost curve. Is that number of smelters or tonnes of capacity that you have on that bar chart, out of curiosity? It says number of smelters, but it doesn't seem to make sense.

L. Kruger — I think that this one really to try and--

M. Bless — No, it's mistyped.

L. Kruger	Terry, good catch – is trying to point out where the new smelter capacity in China is falling in terms of the cost curve.
M. Bless	Yes. Sorry about that. That's certainly tonnes.
T. Ortslan	And what is the tonne, by the way? What is that number, the tonnage number, roughly?
L. Kruger	I will have to look it up, but probably somewhere in the order of 14 million tonnes, 12 million to 14 million, depending.
M. Bless	Of the total, this is right straight out of CRU.
T. Ortslan	Twelve to fourteen million tonnes be in the fourth quartile?
M. Bless	Total China. No. Total China.
T. Ortslan	China, I know that number, okay. Thanks, guys. Thanks very much.
Moderator	Our next question is from Tim Hayes with Davenport & Company.
T. Hayes	A question on the more macro question for Logan. What's your feeling about South Africa? How bad might the power cuts or the smelter cuts

be? I think we're still about, what, 10% of running or has been cut in the three smelters in the region. What's your feeling might that – you know, how much more could that be over the next several years if there's truly a structural power problem in the region?

L. Kruger I think, to go to the last part, I think there is a structural problem. It's not only impacting South Africa. If you read the literature, and you travel there, but it's impacting Botswana, Zimbabwe, and even to Zambia. The solutions for the short-term to try and bring some peak load on gas, turbines, and oil or diesel will help, but the internal consumption of South Africa continues to go up, so the minimum that Eskom, the national provider is set is a 10% reduction. But it hasn't guaranteed that and will have ongoing blackouts or reductions, as it goes forward. So it's imposing that. The second part, which it's trying to impose, is obviously price on the domestic users particularly, and that of course is not doing too well.

I don't see from visiting there and talking to people who in the know that a new power station north of Johannesburg will come into being much before 2015. So this is not a problem that's going to go away in the next year or 18 months. Obviously all the users are working at ways of reducing consumption, but you've also got the growth in demand as well, so I think the two, it's quite an ongoing problem.

We've modeled only a 10% reduction in our look at the numbers. We haven't taken anything in addition. I think that's part of your question. We have no view on that. We'll see how it plays out.

T. Hayes Then moving to China, we've heard a lot of talk that some steel mills may be shutting down around Beijing. Any idea if any aluminum smelters in that area would shut down, and if so, any estimate on what kind of tonnage might be affected?

L. Kruger We haven't picked up any aluminum smelters, but I think the steel ones are being reported. It's a good question. We haven't seen anything, so we've got no view on that. I think just generally we said to China, we've looked at what China may produce for a year, and we say somewhere under 15 million tonnes, close to 15 million tonnes. I'm looking at Shelly and she's nodding her head, so it's in that order. I think people have realized that China will not continue to race ahead, as it was over the last maybe three years.

T. Hayes Thank you.

Moderator Our next question is from David Lipschitz with Merrill Lynch.

D. Lipschitz — My question has been answered. Thank you.

Moderator — Our next question then is from David Rosenberg with Oaktree Capital Management.

D. Rosenberg — I was wondering. You gave the sequential changes in costs from Q1 to Q4. Can you do the same thing year-over-year from Q1 last year to Q1 this year?

M. Bless — Sure. No problem. Let me pick out the big ones. I mean before I get into the costs, obviously the price itself has the biggest single impact, as it always does. Again, assuming that the market moves on both our revenues and, ultimately, our gross profit and operating profit and the rest. Let me give you a couple pieces of key data there. The actual price that we realized.

D. Rosenberg — Up a little bit.

M. Bless — I'm sorry, David?

D. Rosenberg — Price was up a little bit, it looks like, from your press release, the average price.

M. Bless Quarter-to-quarter?

D. Rosenberg Year-over-year, 115 to 117.

L. Kruger No, dollars per tonne here.

M. Bless Yes. Exactly right. Anyway, let me go on to the cost and answer your question. The biggest factors there were not dissimilar to what we just had. The raw materials, about a $7 million negative variance Q1 to Q1 last year. Of that, I'll just give you a little bit more breakdown. Anodes for Grundartangi were about three. Carbon in the U.S. was a bunch more, and then fluoride and a few other little things. Alumina, third party purchased alumina at Ravenswood and Mt. Holly, about $2 million worse. Domestic power, about $5 million worse, that was mostly electric power. Mt. Holly of that was one million dollars, and the rest, Hawesville and Ravenswood. A variety of op ex, principally in the U.S., about $4 million negative variance. Just looking through, those are the major cost elements.

Pardon me, going the other way, importantly, same theme as quarter-to-quarter are what we call the controllable operating expenses at

Grundartangi, i.e. non-power, were favorable by $7 million quarter over prior year's quarter.

D. Rosenberg I'm trying to understand then because it sounds like, if you look at average prices up slightly, volumes were up slightly, costs weren't up dramatically, yet EBITDA is down meaningfully. And I'm trying to figure out what I'm missing, unless it's – maybe it's just mostly SG&A, but—

M. Bless SG&A was six or so, yes, six of it.

D. Rosenberg Yes. Maybe that was it. Okay.

S. Lair David, are you looking at prices as a one-month lag?

D. Rosenberg I'm just looking at what you guys reported in … average realized price.

L. Kruger Hopefully that helped you, David.

D. Rosenberg It did. Thank you.

Moderator Our next question is from Wayne Atwell with Pontis Capital Management.

W. Atwell — Can you explain your thinking going forward on hedging? I know originally when the company was put together, you had relatively high cost with assets primarily in the U.S., and you were at the high end of the cost curve. With your smelter in Iceland now, you're in much better shape compared to the rest of the industry. Are you going to continue to sell metal forward, or as this runs off, are you going to sell flat and not have the forward hedge position?

L. Kruger — Wayne, I think we've been fairly consistent over the last couple of years. We review our status, as we do, and most people do, I'm sure, looking at the market. We want to and wish to remain exposed for the balance of our tonnage to the market, so we have no plans, but I'd just say that we do look at it. But we have no plans to put in place additional hedges. I think that's the question.

M. Bless — Yes, and just to – based on your question, Wayne, I'm sure you do understand, but just implicit in your question, maybe – we have not sold a tonne of metal forward in the last couple of years.

M. Bless — Yes, so we've just been working off the book that we have had, as you referenced, was put in place when the company was a different size and a different cost structure. And, as Logan said, we've been consistent that we think our investors want us to have exposure to the market. We think it's the right thing to do. You never want to say never, but given everything we see right now, as Logan said.

L. Kruger — We like the exposure for the balance of the tonnage, Wayne.

W. Atwell — So essentially, you're going to let your hedge book run off and you're not hedging anymore. And then the second question, we talked about the Ravenswood power situation. Do you have any other power issues that you're concerned about?

L. Kruger — I think the answer is we're obviously working on the longer-term solution for Hawesville but that is a fairly complex process, but it's progressing. We have a power contract in place with about a 27% exposure, which we have dealt with for a number of years.

I think Mt. Holly, we hope that the introduction of the new coal fire power station will help maintain a steady power price there, but again impacted by what coal fuel costs will be. Obviously at Mt. Holly, they're going to bring on the Santee Cooper will bring on the new power station, coal fired again, next year. I think, overall, that's what helps reduce the cost, I think on a tradeoff of coal versus natural gas, the choice is obviously to stay with the coal.

Obviously at Grundartangi, we've got power contracts in place that go through for a long time, and they're LME based, and are quite competitive. It's an issue that we work on all the time, and we see if we can improve it for Ravenswood, we've got the rate case coming this year. More importantly for us is to continue the experimental LME based rate arrangements. That gives us downside protection that obviously is a good system for everyone. It's pretty common practice across the world, as you know.

W. Atwell Thank you.

Moderator Our next question is from Sam Martini with Cobalt Capital.

S. Martini Just a follow up: In terms of the kind of off the run costs, specifically freight, maybe nat gas at the refinery, anything that's not kind of power or bought alumina, anything sneaking up that you're starting to get concerned about being very tight? You mentioned fluoride caustic anything else that you are starting to really think you have to scramble to get that we should be paying close attention to?

L. Kruger — I think, Sam, the answer is every single cost element gets the attention, but just to deal with a couple, we've got contracts in place for aluminum fluoride, and so we've tied that up. Obviously we continue to look ahead and that's one of the reasons we went the route of securing our own source of supply and in the joint venture for carbon for anodes.

The second part on the natural gas, we've always had a proactive hedging strategy in place, and for the balance of the year, I think we're hedged at about 35%, 36% of our needs, mostly Gramercy, but there's a concern point, you know. We see gas costs at $10 a million BTUs. So that's one when we see the market is favorable, we will take some of the risk out of our production cost. Gramercy continues to produce well, so we are … impact that we obviously look at.

S. Martini — What about on the freight side? I hear barge rates are up a lot. Do these things – this is, I think, we're offsetting some meaningful benefits. Are we seeing prices up or capacity costs up even more than we thought?

L. Kruger — I think on the freight barge and ships coming in, we basically have put in place contracts that will come up on that. We also work with our suppliers very carefully trying to make sure that our sources of supplier are closest to our needs, that being obviously Ravenswood and Mt. Holly. So far, that's been quite successful. But again, your question, Sam, is to the $115 oil, what's that going to be. We did mention going towards the end of last year that although our alumina pricing projects for Ravenswood and Mt. Holly were going to improve this year, that has all been taken up by increased freight rates I think you understand that we haven't seen the benefit of the alumina pricing because the freight rate actually eaten up that benefit.

S. Martini Right. Thanks, Logan.

Moderator We have a question from Marty Pollack with NWQ Investment Management.

M. Pollack This is following up on Wayne Atwell's question regarding the strategy on hedging. I'm just wondering. The price, as you look at the forward curve, how much of that in fact is sort of the influence on your thinking? And at the same time, what would be the average price that you project in, let's say, the next two or three years?

L. Kruger Let me try and stand back and answer this, and I'll get my colleagues to comment. I think first of all we look at all the forward prices. We look at the fundamentals, where is the supply coming from, what's the demand like. I think it remains supply side risk, which has been demonstrated very well in the first quarter of this year. And then we look at what it is, but looking at that in this robust market, we feel have been exposed to the aluminum price is good for the company, so we don't want to add to our present hedge position.

In terms of what that price may be, I think you have to go and look at all the analysts and take them all, and that's our advice to everyone, we look at all of those and we say, here's a range of numbers that you may wish to consider. But on a long-term price basis, I think most of the average is around about $2,400 maybe $2,500 or $2,600 per annual tonne. This number we may have been talking six months ago around $2,100. So I'm trying to indicate that the market and the way people are seeing cost push supply side risk and demand growth, these numbers have changed quite a lot in the last six months. Mike or Shelly can even comment, if you'd like.

M. Bless — No, nothing further.

L. Kruger — Hopefully that's helps paint a picture for you.

M. Pollack — I guess what I would just follow up, I mean, in affect, looking at the nature of the project and the cap ex, unless you thought it seems that $2,400 was really, expect a much bigger price, maybe something like a copper type move. It seems that the current price level is fairly good. I mean, can I assume there's just a lot more optimism on your part that it's too much to give up here the opportunity maybe to see the price up to $1.50 plus, something like that. I mean is that in a sense part of the way you're thinking about it?

L. Kruger	We don't give thoughts on the pricing. We say look at what people are talking about. There are people that are talking $3,500, $4,000 a tonne. I think for our planning purposes, Marty, to be clear, we certainly don't use anywhere near that. We go look at our projects like Helguvik, and see where its average cash cost is going to fall in the continuum of cost producers. And we know that it's going to be well in the lower half of the cost producers. But again, there are discussions around this in the press and the analysts. We don't take a view and just say, yes, here's where we think the long-term is indicated by the analysts, and we then go off and do our planning based on somewhat more conservative numbers.

M. Pollack	Thank you.

Moderator	There are no further questions, if you'd like to continue.

L. Kruger	No. Thank you very much, everyone, for joining us today. We look forward to talking with you again at the next quarterly call. Thank you.
Moderator	Ladies and gentlemen, that does conclude our conference for today.