

Alcoa Corporation

Opportunity knocks: Alcoa to consolidate AWAC assets with acquisition of AWC

Reiterate Rating: NEUTRAL | PO: 31.00 USD | Price: 26.32 USD

AWC's largest shareholder is supportive

On Sunday (25-Feb-24), Alcoa (AA) announced an agreement to acquire all of the outstanding shares of Alumina Limited (AWC) of Australia. The all-share transaction, which would see 0.02854 of an AA share exchanged for each AWC share, values AWC's equity at around \$2.2 billion (bn). This is a 13% premium to AWC's market value at announcement, and a 5% premium to our estimated AWC net asset value (NAV). AWC's assets are a 40% interest in the AWAC JV (60% AA). To us, AA's consolidation of AWAC, which operates the bauxite mining and alumina refinery assets that are critical to AA's core smelting assets, has strong industrial logic. AWC's largest shareholder, Allan Gray Ltd, at 19.9%, has agreed to sell its' shares to AA. While we like the transaction's logic and BofA Commodities is bullish aluminum longer-term, this is balanced by transaction-related EPS dilution and near-term aluminum cautiousness. Reiterate Neutral rating.

Dilutive to near-term EPS and NAV per share

We assume the deal closes 30-Sep-24 as currently envisaged, and we calculate a 47% increase in the number of AA shares to 261 million (mn). We factor in transaction costs, G&A for a planned Australian Stock Exchange Chess Depository Interest listing of AA shares, and potential synergies, and adjust 2024E, 2025E and 2026E EPS to 1.16 from \$1.26, to \$4.09 from \$5.61, and to \$5.47 from \$7.51. We reduce our price objective (PO) to \$31 from \$33 per share. We see the deal closing given key share-holder support and AA's unique ability to benefit as the 60% owner and operator of the AWAC JV.

Details of the agreement and AWC at a glance

AA and AWC entered into an exclusivity and transaction process deed, under which they intend to finalize and enter into a scheme implementation agreement. The transaction is subject to, among other things, the satisfaction of certain customary conditions, regulatory and AWC's shareholder approvals. AWC's sole asset is a 40% interest in the Alcoa World Alumina and Chemicals (AWAC) JV, in which AA is the operator and holds a 60% interest. AWAC assets are mostly bauxite mines and alumina refineries, and a 55% interest the Portland aluminum smelter in Australia. Benefits to AA include a simplified governance structure, greater operational flexibility and increased strategic optionality.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	4.93	(2.27)	1.16	4.09	5.47
GAAP EPS	(0.56)	(3.65)	1.16	4.09	5.47
EPS Change (YoY)	-28.2%	NM	NM	252.6%	33.7%
DPS	0.40	0.40	0.40	0.40	0.40
Valuation (Dec)					
P/E	5.3x	NM	22.7x	6.4x	4.8x
GAAP P/E	NM	NM	22.7x	6.4x	4.8x
Dividend Yield	1.5%	1.5%	1.5%	1.5%	1.5%
EV / EBITDA*	3.0x	12.5x	4.9x	2.8x	2.3x
Free Cash Flow Yield*	7.2%	-9.3%	-0.7%	17.2%	26.0%

* For full definitions of *IQmethod*SM measures, see page 6.

29 February 2024

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Stock Data

Price	26.32 USD
Price Objective	31.00 USD
Date Established	29-Feb-2024
Investment Opinion	C-2-7
52-Week Range	23.07 USD - 55.74 USD
Mkt Val (mn) / Shares Out (mn)	4,726 USD / 179.6
Free Float	98.8%
Average Daily Value (mn)	164.78 USD
BofA Ticker / Exchange	AA / NYS
Bloomberg / Reuters	AA US / AAN
ROE (2024E)	3.7%
Net Dbt to Eqty (Dec-2023A)	14.8%
ESGMeter TM	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

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Refer to important disclosures on page 7 to 9. Analyst Certification on page 4. Price Objective Basis/Risk on page 4.

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iQprofileSM Alcoa Corporation

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	2.9%	-2.7%	2.9%	8.5%	10.2%
Return on Equity	18.4%	-8.7%	3.7%	12.4%	14.6%
Operating Margin	5.5%	-3.3%	5.6%	14.2%	17.6%
Free Cash Flow	342	(440)	(33)	814	1,228

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	0.9x	NM	2.2x	1.3x	1.3x
Asset Replacement Ratio	0.8x	0.8x	0.8x	0.9x	1.0x
Tax Rate	91.8%	NM	41.8%	30.0%	30.0%
Net Debt-to-Equity Ratio	6.8%	14.8%	14.5%	5.3%	-5.9%
Interest Cover	6.5x	-3.2x	5.5x	13.7x	17.9x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	12,451	10,551	11,246	12,232	12,829
% Change	2.5%	-15.3%	6.6%	8.8%	4.9%
Gross Profit	2,239	738	1,594	2,646	3,105
% Change	-25.3%	-67.0%	116.0%	66.0%	17.3%
EBITDA	2,224	536	1,355	2,412	2,886
% Change	-20.0%	-75.9%	152.8%	78.0%	19.6%
Net Interest & Other Income	33	(241)	(203)	(191)	(191)
Net Income (Adjusted)	890	(405)	233	1,078	1,443
% Change	-31.4%	NM	NM	362.4%	33.8%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	59	(773)	250	1,080	1,445
Depreciation & Amortization	617	632	676	638	601
Change in Working Capital	(903)	(262)	(48)	(69)	(118)
Deferred Taxation Charge	257	(54)	0	0	0
Other Adjustments, Net	792	548	(360)	(235)	(100)
Capital Expenditure	(480)	(531)	(550)	(600)	(600)
Free Cash Flow	342	-440	-33	814	1,228
% Change	-35.5%	NM	92.5%	NM	50.7%
Share / Issue Repurchase	(478)	1	2,200	0	0
Cost of Dividends Paid	(72)	(72)	(80)	(104)	(104)
Change in Debt	3	55	291	0	0

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	1,363	944	898	1,608	2,731
Trade Receivables	778	656	640	670	703
Other Current Assets	3,109	2,805	2,645	2,640	2,701
Property, Plant & Equipment	6,493	6,785	9,150	9,112	9,111
Other Non-Current Assets	3,040	2,968	3,328	3,563	3,663
Total Assets	14,783	14,158	16,661	17,593	18,910
Short-Term Debt	1	79	79	79	79
Other Current Liabilities	3,003	2,951	2,796	2,819	2,859
Long-Term Debt	1,806	1,732	2,023	2,023	2,023
Other Non-Current Liabilities	3,401	3,550	3,480	3,414	3,350
Total Liabilities	8,211	8,312	8,378	8,335	8,311
Total Equity	6,572	5,846	8,283	9,258	10,599
Total Equity & Liabilities	14,783	14,158	16,661	17,593	18,910

* For full definitions of iQmethodSM measures, see page 6.

Company Sector

Non-Ferrous-Mining

Company Description

Alcoa (AA) is a vertically integrated aluminum company, involved in bauxite mining, alumina refining, and aluminum smelting, in addition to cast aluminum products and some energy assets. Revenue in 2022 was \$12.5bn..

Investment Rationale

We rate AA at Neutral. We are bullish aluminum, but cautious in the more immediate term. Further, AA is in a period of transition (cost reductions) that we think will take longer than previously expected. We like AA's first quartile costs in bauxite/alumina. But its aim to move to first quartile in aluminum is challenged in our view. AA also aims to be the lowest carbon emitter in the industry. It is well positioned given its proprietary technology Elysis, set to begin commercialization in 2024..

Key Drivers

2024E 2025E 2026E

Stock Data

Average Daily Volume 6,260,498

Quarterly Earnings Estimates

	2023	2024
Q1	-0.23A	-0.92E
Q2	-0.35A	0.32E
Q3	-1.13A	0.84E
Q4	-0.56A	0.71E

Model Changes

Exhibit 1: AA key estimate changes – Please note that our updated estimated assume the acquisition of AWC closes on 30-Sep-24
We reduce 2024E to 2026E EPS

(US\$m, US\$/sh)	2024E			2025E			2026E		
	Old	New	Var.	Old	New	Var.	Old	New	Var.
Net sales	11,231	11,246	0%	12,232	12,232	0%	12,829	12,829	0%
SG&A	205	204	-1%	220	214	-3%	205	199	-3%
DD&A	676	676	0%	638	638	0%	601	601	0%
Adj EBITDA	1,354	1,355	0%	2,406	2,412	0%	2,880	2,886	0%
Diluted EPS, Adjusted	1.26	1.16	-8%	5.61	4.09	-27%	7.51	5.47	-27%
Operating Cash Flow	520	517	nm	1,423	1,414	-1%	1,836	1,828	0%
FCF	-30	-33	12%	823	814	nm	1,236	1,228	-1%
Capex	550	550	0%	600	600	0%	600	600	0%
Net Debt (Cash)	908	1,204	33%	209	494	136%	-891	-629	nm
Bauxite									
Production (M dmt)	38.9	38.9	0%	38.5	38.5	0%	38.1	38.1	0%
Alumina									
Production (kmt)	9,975	9,975	0%	9,500	9,500	0%	9,500	9,500	0%
3rd party shipments (kmt)	8,960	8,960	0%	8,750	8,750	0%	8,400	8,400	0%
Intersegment shipments (kmt)	3,840	3,840	0%	3,750	3,750	0%	3,600	3,600	0%
Total shipments	12,800	12,800	0%	12,500	12,500	0%	12,000	12,000	0%
External realized price (\$/mt)	350	350	0%	356	356	0%	367	367	0%
Cash costs (\$/mt)	329	329	0%	324	324	0%	329	329	0%
Aluminum									
Primary aluminum production (kmt)	2,250	2,250	0%	2,250	2,250	0%	2,250	2,250	0%
Total shipments (kmt)	2,550	2,550	0%	2,500	2,500	0%	2,500	2,500	0%
Avg price realization (\$/mt)	3,094	3,094	0%	3,565	3,565	0%	3,817	3,817	0%
Cash costs (\$/mt)	2,667	2,667	0%	2,760	2,760	0%	2,850	2,850	0%

Source: BofA Global Research, company reports.

BofA GLOBAL RESEARCH

Price objective basis & risk

Alcoa Corporation (AA)

Our price objective of \$31 for AA is based on 4.5x 2024E EV/EBITDA, 3.5x 2025E EV/EBITDA and 1.0x net asset value (NAV), with each value equally weighted. The 4.5x 2024E EV/EBITDA target multiple is below the global aluminum producer peer average around 5x to reflect our view for an extended turnaround to return to higher-grade bauxite in Western Australia. The 4.5x is also below AA's historical trading average (since 2016 separation) of 5x. The 3.5x 2025E EV/EBITDA multiple is lower than the 2024E multiple to account for time value and significantly higher aluminum price forecast versus spot. The 1.0x price to NAV (P/NAV) target multiple is in line with our broad North American metals and mining coverage.

Downside risks to our price objective are 1) aluminum price weakness, 2) extended delays in getting its bauxite mine approvals in Western Australia, 3) remaining pension liabilities, 4) rising costs for raw materials including electricity, oil, caustic soda, coke, and pitch, 5) power contract negotiation risk (electricity is a large cost component), 6) power disruption risk and other unforeseen weather-related risks, 7) political, regulatory and country risks, 8) unfavorably currencies changes including in the BRL, CAD, EUR, ISK and NOK, and 9) the removal of protective tariffs in key markets.

Upside risks to our price objective are 1) higher aluminum prices, 2) better-than-expected cost containment, 3) global demand growth, and 4) deal to acquire Alumina Limited (AWC) of Australia does not complete.

Analyst Certification

I, Lawson Winder, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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BofA Securities is currently acting as Financial Adviser to Alumina Ltd in connection with the proposed transaction for Alcoa Corp to acquire 100% of the ordinary shares on issue in Alumina Ltd via a scheme of arrangement, which was announced on 26 Feb 2024. The proposed transaction is amongst other things subject to approval by shareholders of Alumina Ltd and Alcoa Corp. This research report is not intended to provide voting advice, serve as an endorsement of the proposed transaction, or result in the procurement, withholding or revocation of a proxy.

North America - Metals and Mining Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Agnico Eagle Mines	AEM	AEM US	Lawson Winder, CFA
	B2Gold Corp	YBTO	BTO CN	Harmen Puri
	B2Gold Corp	BTG	BTG US	Harmen Puri
	Barrick Gold	GOLD	GOLD US	Lawson Winder, CFA
	Cameco Corporation	YCCO	CCO CN	Lawson Winder, CFA
	Cameco Corporation	CCJ	CCJ US	Lawson Winder, CFA
	CMC	CMC	CMC US	Lawson Winder, CFA
	Endeavour Mining	YEDV	EDV CN	Harmen Puri
	Endeavour Mining	EDVMF	EDVMF US	Harmen Puri

North America - Metals and Mining Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Endeavour Mining PLC	XEDVF	EDV LN	Harmen Puri
	Franco-Nevada	YFNV	FNV CN	Lawson Winder, CFA
	Franco-Nevada	FNV	FNV US	Lawson Winder, CFA
	IAMGOLD	YIMG	IMG CN	Lawson Winder, CFA
	IAMGOLD Corp.	IAG	IAG US	Lawson Winder, CFA
	Ivanhoe Mines	YIVN	IVN CN	Lawson Winder, CFA
	Ivanhoe Mines	IVPAF	IVPAF US	Lawson Winder, CFA
	Lundin Mining	XLPRF	LUMI SS	Lawson Winder, CFA
	Lundin Mining Corp	YLUN	LUN CN	Lawson Winder, CFA
	Lundin Mining Corp	LUNMF	LUNMF US	Lawson Winder, CFA
	MP Materials	MP	MP US	Lawson Winder, CFA
	Newmont Corporation	NEM	NEM US	Lawson Winder, CFA
	Newmont Corporation	XNCRF	NEM AU	Lawson Winder, CFA
	Nucor	NUE	NUE US	Lawson Winder, CFA
	Pan American Silver	PAAS	PAAS US	Lawson Winder, CFA
	Teck Resources	YTECK	TECK/B CN	Lawson Winder, CFA
	Teck Resources Ltd	TECK	TECK US	Lawson Winder, CFA
	Triple Flag Precious Metals Corp.	YTFPM	TFPM CN	Lawson Winder, CFA
	Triple Flag Precious Metals Corp.	TFPM	TFPM US	Lawson Winder, CFA
	Wheaton Precious Metals	WPM	WPM US	Lawson Winder, CFA
NEUTRAL				
	Alamos Gold	YAGI	AGI CN	Harmen Puri
	Alamos Gold	AGI	AGI US	Harmen Puri
	Alcoa Corporation	AA	AA US	Lawson Winder, CFA
	Cleveland-Cliffs	CLF	CLF US	Lawson Winder, CFA
	First Quantum	FQVLF	FQVLF US	Lawson Winder, CFA
	First Quantum Minerals	YFM	FM CN	Lawson Winder, CFA
	Freeport-McMoRan	FCX	FCX US	Lawson Winder, CFA
	Hudbay Minerals	YHBM	HBM CN	Lawson Winder, CFA
	HudBay Minerals	HBM	HBM US	Lawson Winder, CFA
	Reliance Inc.	RS	RS US	Lawson Winder, CFA
	Steel Dynamics	STLD	STLD US	Lawson Winder, CFA
UNDERPERFORM				
	Centerra Gold	YCG	CG CN	Lawson Winder, CFA
	Centerra Gold	CGAU	CGAU US	Lawson Winder, CFA
	Eldorado Gold	EGO	EGO US	Harmen Puri
	Eldorado Gold	YELD	ELD CN	Harmen Puri
	Kinross Gold	KGC	KGC US	Lawson Winder, CFA
	New Gold Inc.	YNGD	NGD CN	Harmen Puri
	New Gold Inc.	NGD	NGD US	Harmen Puri
	Nexa Resources	NEXA	NEXA US	Lawson Winder, CFA
	Royal Gold	RGLD	RGLD US	Lawson Winder, CFA
	SSR Mining Inc.	SSRM	SSRM US	Lawson Winder, CFA
	SSR Mining Inc.	YSSRM	SSRM CN	Lawson Winder, CFA

iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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Disclosures

Important Disclosures

Alcoa (AA) Price Chart



AA — Restricted — Review — PO

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Non-Ferrous Metals/Mining & Minerals Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	58	53.70%	Buy	26	44.83%
Hold	24	22.22%	Hold	10	41.67%
Sell	26	24.07%	Sell	13	50.00%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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