

**ALCOA CANADA**

**Notes for a keynote address by Mr. Jean-Pierre Gilardeau  
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**The Future of Aluminum in Québec: A Reality Check**

**Chambre de commerce de Québec  
Québec City, April 19, 2005**

**EMBARGO 12:30 p.m., April 19, 2005**

**CHECK AGAINST DELIVERY.**

Mr. President,  
Distinguished guests of honour,  
Dear customers and suppliers,  
Employees and members of our communities,  
Ladies and gentlemen,

First, I'd like to thank the Chamber of Commerce for having invited me to speak to you today of issues that I feel very strongly about.

The aluminum industry in Québec is going through a critical moment in its history:

- On the one hand, unprecedented growth opportunities will be offered to us in the next few years;
- On the other hand, the orientation spurred on by the Government of Québec's new energy policy will be a decisive factor in the future of our companies and that of our regions.

Today, my goal is very simple: I wish to share with you my vision of the aluminum industry in Québec.

My address will cover the following points:

- First, an overview of the opportunities offered to our industry in the years to come;
- The place of Alcoa in this expanding universe;
- Québec's assets serving to benefit from this future;
- And lastly, the major decisions we will have to take collectively as regards energy.

Let's start with the future prospects of aluminum throughout the world.

From the outset, I would say that we are going through a pivotal moment marked by the combined effect of five great upheavals: demography, globalization of exchanges, urbanization, natural resources, and lastly, science and technology.

**Demography.** Every year, 80 million inhabitants will join the world population. In 2007, 40% of the world population will live in China and India. In 2015, one billion more people will live in the cities and 300 million more will earn over \$20,000 per year. That same year, 22% of the G7 population will be over 65 years of age.

**Globalization.** The abolition of trade barriers will entail transformations that will sweep away entire industries and drive others to new heights. By 2015, world trade will increase from 25% to 40% of the global GDP. The development of new markets will produce new unparalleled opportunities and technological leaps. Simultaneously, market volatility and political risk will grow.

**Urbanization.** Around 2007, more people will live in the cities than in the country. In fact, cities will count 60 million new residents every year! But we all know how cities constitute non only a factor of social and economic development, but also an environmental challenge. As many as 200 million new cars are expected to take to our roads. Imagine the impact!

**Natural resources.** Energy demand will continue to grow, which will impact the availability of base materials as well as their cost. Meanwhile, this will cause considerable growth as regards technologies contributing to the reduction of the production of greenhouse gases. Consequently, preference will be granted to lighter materials.

**Science and technology.** The necessity of producing more and more, and at better cost, will afford a clear advantage to industries that build on innovation and flexibility. The same goes for leading-edge technological materials that offer a broad range of possibilities, while being eminently recyclable.

What do all these issues I've listed have in common?

Every one of them opens up countless opportunities for the development of the aluminum industry throughout the world. We believe that our metal is a metal of the future. The qualities and recyclability of aluminum make it a material of the future, which, in principle, could/should contribute to the creation of a solid economy in Québec and in its regions.

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Which brings me to my second point: What is the position of Alcoa in this context of accelerated development?

Alcoa is an enormous international complex that possesses the human and financial resources required to meet these colossal challenges.

Alcoa is first and foremost 131,000 employees working in over 350 plants in 43 countries throughout the world.

Alcoa is \$24 billion in sales in 2004.

Alcoa is also 700 researchers who are dedicated to R&D and who, with a budget of over US\$100 million, work at the very frontiers of technology.

Alcoa is a world leader in the aeronautics industry. Our products are namely used in the fabrication of the new Airbus A380, the largest commercial plane in the world, and in several of Bombardier's planes, in the fabrication of Rolls Royce and Pratt & Whitney

aircraft engines, in parts of the Boeing 737 and C-17, and in many other aeronautical applications.

Alcoa is a world leader in the automotive industry. Our different alloys enter into the fabrication of several parts of the most popular Chrysler, Nissan, Audi, Volkswagen, General Motors, Subaru, and Toyota models.

Alcoa is a world leader in the commercial transportation industry. Our products namely enter into the production of wheels that equip a large part of the truck fleets in North America.

Alcoa is a world leader in the construction industry. In addition to considerably enhancing their appearance, our architectural products contribute to increasing the strength, resistance and longevity of buildings throughout the world.

Alcoa is a world leader in the area of mass consumerism. Our products are used in the packaging of food, pharmaceuticals, beer, sodas, and almost all the range of consumer products on every continent.

I could go on like this for a long time. Our products are so diversified that they are an integral part of the daily lives of the inhabitants of almost all of the countries on the planet.

I believe that, as mentioned earlier, the arrival of hundreds of millions of new consumers and the creation of hundreds of new cities will have a determining impact on the consumption and therefore the production of aluminum.

Now let's talk about Alcoa in Québec:

- Alcoa Canada first means an head office in Montreal;
- aluminum smelters in Bécancour, Deschambault-Grondines and Baie-Comeau;

- a rod plant in Bécancour;
- a Reynolds food packaging plant north of Montreal;
- a Howmet aluminum casting plant in Laval that serves the aeronautics industry;
- distribution centres for our clients;
- close to 5,000 employees and an annual turnover of over \$2 billion;
- and, as you have just seen, it is also a great deal of processing activity, not to mention our other plants elsewhere in Canada.

Alcoa is a good company that is well established in Québec and that is seeking growth to take advantage of a promising future.

May I digress for a moment regarding the announcement made last week in Baie-Comeau. Our efforts to enhance our performance are leading us to constantly review our processes and methods. It is in this framework that last week, we announced an early retirement program for our managers and union member employees at the Baie-Comeau smelter. The goal is to reduce our workforce by 200 jobs. This measure aims at enhancing the productivity and competitiveness of this plant. We are evolving in a global context where everything must be done to successfully compete with other aluminum smelters throughout the world that namely profit from much lower energy and labour costs. In this context, we have no choice but to reduce our costs if we wish to survive and to attract capital to our older smelters.

Now, does Québec have the assets required to benefit from this future?

The answer is yes. Without a shadow of a doubt. And here's why:

- In Québec, we already have the most important companies in the world in the aluminum sector.
- We have renewable energy to seize these opportunities as well as considerable potential for development.
- We have a web of high-performance plants.

- Here, we have the most important critical mass of knowledge and expertise in the area of aluminum in the world:
  - world-renowned engineering firms such as SNC-Lavalin, Bechtel, Hatch, Roche, to name a few;
  - equipment manufacturers: manufacturers of travelling cranes, specialized mobile equipment, smelter equipment, etc.;
  - raw materials, goods and services suppliers;
  - universities and research centres in a variety of areas;
  - skilled labour.

The real question is: Will Québec be able to take advantage of the expected economic growth?

This time, my answer is more balanced. I would say that it depends. The good news is that it depends on us and on the decisions that we will take, more particularly as regards energy.

Just like other companies, aluminum smelters establish themselves and develop wherever conditions are favourable. An aluminum smelter requires massive investments. Building, modernizing or extending one of our plants always costs several hundred million dollars. These investments are based on a long-term perspective, a horizon of at least 30 years. No one would invest such sums without a minimum of certainty as to what the future has in store.

In our area, one of the most important expenditures is energy costs, which in fact represent a third of the total operating costs of an aluminum smelter. In the past, our great advantage over our competitors was the rates and availability of electric power. If this advantage is threatened, it is, in my view, less and less likely that a new aluminum smelter will establish itself in Québec.

Now I wish to summarize for you the reasons why I believe that the aluminum industry can still have a promising future in Québec:

- First, let's establish that the current price of energy in Québec is higher in comparison to the price our industry pays in other countries. In 2003, the average rate paid by the world's 200 or so aluminum smelters was 30% lower than Hydro-Québec's "L" rate. Assuming that its increases are predictable and controlled, at this rate, an aluminum smelter may be able to modernize its facilities. Ultimately, it could consolidate a small plant by increasing its capacity. However, it is not very likely that a new aluminum smelter could be implemented here under these conditions.
- Hydro-Québec sells its electric power, at a regulated rate called the "L" rate, to any company needing more than 5 MW. Hydro-Québec recovers its expenses with the "L" rate. Hydro-Québec is the first to admit this and has done so publicly on several occasions to the Régie de l'Énergie, specifically at the last hearing on the Suroît project.
- Among the companies whose production rests on the "L" rate, we are clearly the company that entails the least production costs for Hydro-Québec. We are connected to Hydro-Québec's large distribution networks. The location of our plants is no coincidence. Have a look at a map of the province. Note the corridors marked by the passage of Hydro-Québec's large power networks. Our plants are located very close, if not directly under these networks. Our aluminum smelters feed on "raw energy", that is electric power that stems directly from Hydro-Québec's power stations, and that has therefore not been processed. Hence, there's no need for long-term assets to process this power before delivery, as is the case for Hydro-Québec's other customers. Evidently, among all of Hydro-Québec's customers, specifically the "L" rate customers, aluminum plants buy the product that is the least expensive for Hydro-Québec to produce and that affords the best return in this client category. In short, Hydro-Québec brings in good

profits with the “L” rate and even more so if the power is provided to a customer such as Alcoa.

- Some will claim that we have “special rates”. Yes, in the past, about 15 years ago, we entered into agreements with previous governments. These agreements allowed our industry to firmly establish itself in Québec. In addition, they were signed at a time when Hydro-Québec and the government were seeking large reliable clients to fund the major expansion projects such as the Manic or James Bay projects. Québec had to sell important blocks of this new available energy to solid clients providing long-term guarantees. Thus, our industry was put to contribution to allow Québec to build the works we are so proud of today... Year in, year out, Alcoa pays Hydro-Québec an electric bill of roughly \$400 million. We are their largest customer and we have never missed a single payment. Despite all that has been said and written, Hydro-Québec has admitted that these special contracts have allowed it to recover its expenses. Today, the rates paid in accordance with these contracts are very close to the “L” rate. In short, a good “deal” for both Hydro-Québec and our industry.
- Others claim that the last MW we will produce or buy will cost more to produce than the revenues stemming from the “L” rate. Given this, some conclude that all our electric power should be sold at this new rate. In my opinion, such reasoning doesn’t hold water. We believe that Hydro-Québec should sell its power at its average price, like it has always done. Power that is produced using old facilities costs almost nothing to produce, given that the facilities are almost totally amortized. This great advantage for Québec must be preserved. The power we will produce tomorrow or that we buy today is more expensive, but this is only true in the case of this new power. Therefore, the fair rate is and should be the average price, that is the price established on the basis of Hydro-Québec’s total actual cost, rather than the highest possible price. This average cost approach would allow Hydro-Québec to accomplish its projects, preserve its profitability and develop its full potential. To do so, Hydro-Québec must control its expenditures, as we must all do, and limit its rate increases while preserving its profitability.

Now we must remember that the aluminum industry in Québec is:

- \$7 billion invested between 1991 and 2003;
- \$1 billion spent every year for goods and services in Québec;
- over \$1 billion paid in wages;
- over 15,000 direct and indirect jobs;
- an hourly salary rate that exceeds the average manufacturing wage rate by 45%;
- \$300 million per year in income and various other taxes;
- \$550 million paid to Hydro-Québec, over \$170 million with the start-up of the Alouette extension;
  - On this score, Alcoa is Hydro-Québec's largest customer, as mentioned earlier, with an annual electric bill of more than \$400 million.

In fact, a kWh sold to our industry represents 17 cents in direct and indirect spinoffs for Québec—much more, therefore, than Hydro-Québec can generate with exportations, given the whole chain of added value that we provide for every kWh processed into aluminum.

And what of the risks associated with exportation! Dozens of electric power stations are under construction in the north-eastern United States alone. What will happen to the exportation price when these new power stations will be in operation? To ask the question is to answer it.

Which brings me to my last point: What can be done to profit from the spin-offs of this important global evolution I mentioned earlier? What are the major collective decisions we must take as regards energy?

First, I think that the government has taken the right decision to review its energy policy. The current policy was the object of way too much interpretation.

A commission is studying the issue. The exercise has begun. Several ideas have been put forward to develop a new policy serving the interests of Quebeckers.

In my view:

- Many agree on one thing: we must totally bank on hydroelectricity to ensure our security of power supply. As we speak, and for generations to come, it is probably Québec's greatest natural resource.
- While highly prioritizing hydroelectricity, several players have underlined the need to ensure, over time, a certain diversity of our sources of power supply. Namely, wind power has retained our attention. I believe that a society is justified in being concerned with the diversity of its sources of supply.
- The importance of hydroelectricity in Québec's economic development has also met with widespread consensus. Several players have voiced their concerns as regards the illusion behind massive exports of our electric power—a very short-term strategy of which the impact on our economic development could prove to be disastrous, particularly in our regions. In this room are representatives namely of Baie-Comeau, Bécancour and Deschambault-Grondines where Alcoa operates aluminum smelters. These people know very well that we can not build a strong society by exporting our resources and related jobs.

This sets out the importance of the regions in what I would call Québec's genetic code. That's just the way we are here: a few large urban centres and several regions. Thanks to the price and the abundance of our electric power, we have had the chance to develop large industries within our regions, industries that support their economic, social and cultural development. It must be underlined that ours is a rather unique situation.

On this score, I believe that everyone acknowledges the role played in the regions by major industries, including Alcoa, that is the role of an economic driving force. In order to continue to play this role, it is vital that the large industries benefit in the long term from energy rates that at least allow for their maintenance and better still, their development. What is needed are rates that are competitive, stable and predictable over time, and a supply, now and in the future, that is guaranteed. It is vital.

Québec's new energy policy constitutes an excellent opportunity to consolidate the development of our regional economies. As the trustee of our main collective asset, Hydro-Québec must play a strategic role in the development, in our regions, of large industries that support the fulfillment of the local populations. Our largest public corporation must be profitable, but it can not be relegated to the role of a government cash register. Its glorious past, its great expertise and the abundance of the wealth that it manages on our behalf, all plead in favour of an active role in the development of our regional communities and in the future of their generations to come.

Alcoa wants to be part of this future. As a society, we must find the means to profit from the important economic growth that will be available to countries who will have positioned themselves to reap its benefits.

In the aluminum industry, one of the sectors *par excellence* that holds a future, Québec has all the aces it needs to win. Québec's energy policy is one of the most important tools supporting our efforts so that we may bequeath to our children a future that lives up to their ambitions.

It is with the utmost confidence that Alcoa wishes to pursue in this direction.

Thank you for your attention.