Alcoa Corporation

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BY EMAIL

October 27, 2022

Mr. Matthew Chamberlain
Chief Executive Officer
London Metal Exchange
10 Finsbury Square
London EC2A 1AJ
United Kingdom
discussionpaper@lme.com

RE: Alcoa's Response to the LME Discussion Paper on Russian Metal

Dear Mr. Chamberlain:

We write to you today in response to the LME Discussion Paper on Russian Metal issued on October 6, 2022 (the "Discussion Paper").

As you will recall, Alcoa Corporation ("Alcoa") first wrote to you on September 29, 2022, prior to the LME's issuance of the Discussion Paper, in order to express our serious concern that Russia's invasion of Ukraine threatens to distort aluminum market pricing and raises a systemic risk to the reliability of the LME aluminum contract. In that letter (enclosed as Annex A for ease of reference), Alcoa urged the LME to act quickly to delist Russian origin brands in order to protect the reputation and viability of the LME aluminum contract.

In view of the significant moves in LME inventory levels in recent days, we are even more convinced that the LME must act now to immediately delist Russian metal. From October 3 to October 26, LME aluminum stocks on warrant increased by 74%. While we are without sufficient information to determine whether this is indicative of a rush to deliver Russian metal in advance of the closing of the current LME consultation, a Reuters news article on October 18, 2022, reported significant deliveries of Russian metal into LME warehouses (see https://www.reuters.com/markets/commodities/exclusive-glencore-delivers-russian-origin-aluminium-into-lme-system-sources-2022-10-18/). Following these developments, we urgently wrote to you again on October 18, 2022, seeking increased transparency related to the quantity of Russian origin metal in inventory (enclosed as Annex B for reference). We are still awaiting your response to that request.

We reaffirm the positions outlined in our prior letters. In addition, Alcoa wishes to highlight the following:

1. A Predominance of Russian Stocks Would Create Risk for the LME Aluminum Contract. In the "Summary" section of the Discussion Paper, the LME states: "[i]n parallel, the LME has been closely monitoring the usage and throughflow of Russian metal on the LME, to ensure that

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LME warehouses do not see a significant inflow of unwanted Russian stocks, posing a risk of creating a disorderly or unfair market." While Alcoa certainly agrees that a significant near term inflow of Russian metal could create upheaval in the market, we wish to point out that there is also a significant risk of systematic, ongoing deliveries of Russian metal in 2023 and beyond. Whether LME inventories accumulate quickly or more gradually, the result is the same – a growing predominance of unwanted Russian stocks in global inventories that would threaten the viability of the LME aluminum contract.

2. Analysis of the LME's Three Key Lenses for Evaluation. In the "Background and actions to date" section of the Discussion Paper, the LME outlines three key lenses which it has used to evaluate the appropriateness of continuing to allow Russian brands to be listed: (i) ethical, (ii) compliance with government sanctions, and (iii) usage trends of Russian metal:

(i) Ethical. Alcoa made the proactive decision in March 2022 to cease buying raw materials from, or selling our products to, Russian businesses. While this impacted our business, we remain convinced that it was the right decision to make. Russia's unprovoked war against Ukraine, which began in February 2022, has caused a significant humanitarian crisis and an energy crisis that is acute in Europe. Several other industry participants have publicly announced similar bans on the delivery of Russian-origin metal, and our discussions with commercial customers indicate that this position is widespread throughout the industry.

In the Discussion Paper, the LME asserts that individual companies should make their own determination regarding whether to accept Russian metal, and further that the LME impacts other market participants when it changes its brand lists because those market participants can no longer sell that brand on the LME. However, Alcoa notes that the LME already requires its listed brands to be audited and to receive certification for upholding specific ethical and sustainability requirements.

In addition, Alcoa notes that the LME has always retained the ability to delist brands. The LME is not obligated to serve as the market of last resort for all brands ad infinitum. As our own decision announced in March 2022 makes clear, aluminum industry participants have been aware of these issues for an extended period, and many have already announced their own plans to address the disruption caused by Russia's invasion of Ukraine. At some point, market participants that have affirmatively decided not to make adjustments to their own business must bear the risk of holding metal that cannot be delivered to the LME.

(ii) Compliance with government sanctions. In this section of the Discussion Paper, the LME describes previous cases where it took decisions to delist, or in some cases not to delist, particular brands following the imposition of tariffs or government sanctions. One example of concern for Alcoa was the LME's April 2022 decision to ban the delivery of Russian metal into UK warehouses only, following the imposition of significant tariffs by the UK. Given the global nature of metal flows generally, and the LME warehouse system more specifically, Alcoa questions the effectiveness of a selective delisting in the UK only.

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By taking such an action, the LME risks distorting the metal flows of specific brands in its warehouse system. This risk would be present even if there was no Russian metal present in UK warehouses at the time that the LME issued the ban.

One important point that the LME did not address in the Discussion Paper is the banking considerations for market participants who might be forced to pick up and sift numerous warrants in order to prevent taking delivery of unwanted Russian metal from the warehouses. While these considerations are not directly related to government sanctions, Alcoa believes that it is unlikely that banks will be willing to finance this activity. We further note that many banks have indicated that they will not finance Russian metal or insure Russian shipments, significantly reducing the value and marketability of Russian stocks.

(iii) Usage trends of Russian metal. While this section of the Discussion Paper focuses on the historic usage of Russian metal, Alcoa believes that these trends will change significantly in 2023 as many purchasers refuse to take delivery of Russian metal. We acknowledge the LME's charts showing Russian metal in warehouses at historically normal levels; however, we see a real risk that - whether through a sudden influx or sustained deliveries – Russian brands will become the predominant metal on the exchange if the LME does not act urgently to delist Russian metal. This risk is especially acute today given the historically low inventory levels. As discussed above, from October 3 to October 26, LME aluminum stocks on warrant increased by 74%. This data is alarming and led us to write to you on October 18 seeking increased transparency of Russian metal in inventory, both on and off warrant (see Annex B enclosed). We reiterate our request that the LME begins daily disclosures of this information.

3. Alcoa Strongly Advocates for Option C1. Alcoa believes that it is imperative that the LME act quickly and decisively to prevent a situation where Russian metal becomes the dominant brand in the LME warehouse system. If such a situation occurs, it will be very difficult to unwind and the consequences to market participants and to the reputation and reliability of the LME aluminum contract could be severe. For these reasons, Alcoa urges the LME to implement action "C1 Apply the suspension immediately and for all Russian metal". Any proposed action which includes an advance notice period would open the door for metal to be rushed into the warehouse system, potentially creating (as the LME duly notes) the very problem that the LME intended to prevent. As noted above, industry participants have been aware of this impending market situation for several months, and Alcoa considers that the current LME consultation itself, including the associated news coverage, is a sufficient notice period for any related LME action. Further, all Russian metal should be included in the suspension, regardless of production date, as market participants have no way to ascertain how much Russian metal has already been produced and may be sitting in non-LME inventories around the world. As a result, selectively applying the suspension only to metal produced after a particular date would not address the risk that the LME is seeking to mitigate by implementing the suspension.

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4. Shortcomings of Options A and B. Alcoa supports option C1 as most likely to mitigate the risks identified in the Discussion Paper, and we do not believe that the other listed options could effectively achieve the LME's stated objectives. If the LME were to maintain its current position, Option A, it would be simply ignoring the risk that significant volumes of Russian metal will be placed in warehouses. Apart from the dangers of such a circumstance noted above and in our previous letters, Alcoa sees a risk that this metal may become subject to future government sanctions. While this is a risk that is always present at some level, Reuters reported on October 12, 2022, that the Biden administration is actively weighing potential sanctions on Russian metal (https://www.reuters.com/markets/commodities/us-considering-complete-ban-russian-aluminum-bloomberg-2022-10-12/). In the event that significant deliveries of Russian metal into LME warehouses are followed by sanctions issued against Rusal, the market could be faced with large volumes of dormant stock, potentially distorting pricing mechanisms and impacting orderly market function. Alcoa believes that Option B is also unsatisfactory for the reasons identified by the LME regarding the difficulty in identifying and managing the necessary thresholds. In our view, the implementation of Option B would not provide a meaningful solution to market participants but would only serve to prolong the current uncertainties that gave rise to the Discussion Paper.

In sum, Alcoa urges the LME to immediately delist all Russian brands, regardless of the production date of the underlying metal, in order to maintain the reliability of the LME aluminum contract and ensure that it properly reflects the actual supply and demand fundamentals of the aluminum industry.

Sincerely,

Kelly Thomas

Kelly Thomas
EVP & Chief Commercial Officer

Enclosures:
Annex A – Alcoa Letter of September 29, 2022
Annex B – Alcoa Letter of October 18, 2022