ALROSA Q3 & 9M 2013 IFRS Results

Conference Call Summary

December 5, 2013

ALROSA speakers

Igor Kulichik – *CFO*

Sergei Mezhokh – *Head of Investor Relations, Foreign Affairs and Analytics*

Presentation

Sergei Mezhokh

Good day everyone, welcome to the ALROSA's conference call on the Q3 2013 results. I am Sergei Mezhokh, Head of IR, and I will make few introductory notes. Our call is going to be led by our CFO Igor Kulichik who will be assisted by Anastasia Misharina, Head of IFRS reporting, and myself. We have prepared several slides for you which are uploaded to IR section of our website.

Before we start, I'd like to remind you that some information provided during this call may include forward looking statements that involve risks, uncertainties and assumptions. If the risks or uncertainties ever materialise or the assumptions prove incorrect our results may differ materially from those expressed or implied by such forward looking statements. We assume no obligations and do not intend to update any such forward looking statements. Now I'm passing a word to Igor.

Igor Kulichik (translated)

Ladies and gentlemen, welcome to ALROSA's Q3 and 9M 2013 results call. Let me start with an update of recent events that have taken place since our previous call.

On the 27th of September ALROSA and Rosneft signed an agreement for the sale of ALROSA's gas assets in the Yamalo-Nenets Autonomous District and oil and gas assets in Yakutia for $1.38 billion. We expect to receive $1.25 billion in payments for Geotransgaz and Urengoyskaya Gazovaya Company by mid-December. The remaining payments for the oil and gas assets in Yakutia are to be received in the course of 2014. The cash proceeds from the sale of gas assets will be used to repay our existing short-term debt.

Our headline event was of course the public offering of 16% of the Company's shares on the Moscow Exchange. The proceeds from the offering amounted to $1.3 billion. This has become the largest offering by local issuer with a listing on the Moscow Exchange. The offering was also the world's largest in the mining sector since June 2011 and the first public offering among the Russian government-owned national resource companies in seven years.

Following the offering, ALROSA’s free float increased from 7% to 23%. The share of the Russian Federation in the Company’s share capital decreased from 51% to 44%. Yakutia’s share went down from 32% to 25%. As to any further privatization plans by the shareholders, it is important to mention the shareholder agreement signed between the Russian Federation and Yakutia to maintain collectively ownership over 50% of the Company’s shares until at least 2018.

Talking about our dividend policy, I’m happy to inform you that just at the end of the last week the Supervisory Board approved a new dividend policy of the Company which establishes dividends at the level of at least 35% of ALROSA’s net profit under IFRS.

Let us now move on to the results of the reporting period. Diamond mining over 9M 2013 grew by 6% to 27.1 million carats. The primary drivers behind its growth were the acquisition of Nizhne-Lenskoye in 2013, improvements of ore quality at Jubilee pipe and increased production at Mir underground mine.

Rough diamond sales increased in Q3 2013 by 57% year-on-year to 8 million carats. Overall, in 9M 2013 ALROSA sold 27.2 million carats of diamonds, up 22% year-on-year.

Our revenue in the reporting period reached RUB 121.4 billion, up 16% year-on-year driven by higher diamond sales in carats by 22% year-on-year.

Prices in the diamond market over 9M 2013 were 8% lower than in the same period last year. This explains why our revenue growth in rouble terms was slower than our sales growth in carats. Cost of goods sold was up by 27% over 9M 2013 mainly due to sales being higher by 22%.

9M 2013 EBITDA reached RUB 51.3 billion, up 6% year-on-year. EBITDA margin, however, was down from 46% to 42% on the back of no price jolts in the diamond market in 2013.

Our 9M 2013 net profit was down 8% year-on-year mainly due to FX loss and higher interest expense.

Total Capex in the reporting period was RUB 23.8 billion, up 12% year-on-year as we continued with our underground mine construction program as well as important technical upgrade initiatives.

Winding up my presentation of our financial results, I would like to give you an update on our debt portfolio. Our total debt at the end of Q3 2013 stood at $4.6 billion of which $1.4 billion was short-term debt to be repaid in the course of the remainder of 2013. Let me remind you that we see as the main source for a short-term debt repayment the proceeds from the sale of our gas assets that we expect to receive by mid-December. Our end-of-year debt, therefore, is expected to be at the level of $3 billion.

On this optimistic note let me announce that we are now opening our Q&A session and will be happy to take your questions.

Questions and Answers

Sergei Donskoy – *Société Générale*

Good evening, thank you very much for the presentation. I have two questions if I may. Firstly, if I'm not mistaken you mentioned at one of the previous presentations that you planned to reduce your inventories of rough diamonds this year by around 1.5 million carats. By our estimates, your production and sales for the first nine months of this year match almost exactly, so I wonder do you still plan to sell 1.5 million carats from inventories in Q4 and what volume do you target actually for Q4, if it can be quantified at this point somehow. Secondly, what price dynamics for rough diamonds do you see in Q4 relative to Q3? Thank you.

Igor Kulichik (translated)

As for our inventory reduction plan, we need to make some clarifications here. Yes, we did mention that we are planning to reduce our inventory by 1.2 to 2 million carats but most of that reduction is to happen in 2014. We will probably see at the end of 2013 the same level of inventory that we currently have and the main volume of reduction is to occur over 2014. As for Q4 forecasts, they are very optimistic. We have seen good sales in October, November and December and we have no doubt that we will be able to meet our revenue targets in Q4. As for prices, it is well known that in 2013 we have seen a somewhat lower level than we saw in 2012. The price committee last met on September and there was just a small reduction in price at that time. We haven't made any decision on any change in prices in Q4 and we are unlikely to make one before the end of this year.

Mark Mobius – *Templeton*

I have a question regarding the gem-quality diamonds. Do you have a plan to promote the ALROSA brand to the retail community, and in that connection, trying to imbed into the gem-quality diamonds identification similar to what is used by the South African miner De Beers?

Igor Kulichik (translated)

As for making ALROSA a brand in the jewellery market, we have similar to De Beers quite an experience there, although not a very happy one. De Beers went even further than us and opened several jewellery shops with their brand name on them. We stopped just before that. We didn't go into that. Our experience is that brand promotion and being in the jewellery business is very different from our core business. It's very different from mining and beneficiation. Currently, we proceed from a postulate that building a fully vertically integrated company from mining to retail is not possible and not efficient. And just to reiterate, according to our strategy we focus on our core business which is mining, beneficiation and sale of rough diamonds.

George Buzhenitsa – *Deutsche Bank*

Good evening gentlemen, thank you for the conference call. I have a couple of questions. First is on SG&A. I can see that you have made some progress with respect to cost savings on SG&A front. I am wondering, do you think this is an optimal level that you have achieved for SG&A in Q3 and can we extrapolate it for the periods going forward, or you still see a scope for improvements on the SG&A front going forward? Second question is on Capex. Could you please provide guidance for 2014 and also since you have targets for revenues, if you can of course, will you be able to provide a revenue target for 2014?

Igor Kulichik (translated)

Talking about cost management, we are in the middle of our journey here. We have started looking at cost management some three years ago and currently managed to achieve some good progress. That is also true of SG&A that you have mentioned. It wouldn't be right to say that we are looking for any further dramatic decrease in those costs but we understand them very well and we control them. As for the Capex for 2014 that would probably be the heaviest Capex that we are going to see that year. What we currently have in our 2014 budget is some RUB 38 billion and as we have mentioned in our roadshow presentations, 2014 would be the peak year in terms of Capex and thereafter you would see a gradual reduction because our investments in underground mines would finish.

Yuriy Vlasov – *JP Morgan* (translated)

A question on how you report the average price for gem-quality diamonds. Looking into your presentation on slide 6, the average price for gem-quality diamonds is $213.5 per carat, whereas for Q2 you give the number of $219.5 per carat. If I look into the presentation prepared for Q2 and H1 2013 results, on slide 5 there I see that the price mentioned there is $191.4 per carat. Can you please explain the difference?

Sergei Mezhokh

Well, Yuriy, the major difference is actually that ALROSA sells different types of diamonds from quarter to quarter and to look at just average prices, getting them by dividing our revenue on carats, can seem misleading. Therefore, for the purpose of transparency, every quarter we recalculate our average selling prices as if we have been selling the same product mix during the period we present on the slide. Considering that each quarter we present different periods, therefore, the average price for same product mix is different. But actually you better look not at the absolute figures but the dynamics of the figures because in our understanding they characterise the market trend. Otherwise, you can face a situation when the average price goes up but the actual price, i.e. the market dynamics, goes in another way.

Maria Gancheva – *Mitsubishi*

Good afternoon and thank you very much for your presentation today. Just a brief question on your liquidity profile; you've mentioned already that you expect your payment for the gas assets sale to happen mid-December. In addition, my question will be the amounts raised from the SPO – is that going to go into repaying maturing debt? My other question related to that is do you find necessary or are you considering any further bond issuance within next year? Thank you.

Igor Kulichik (translated)

Unfortunately, the funds from the SPO were not received by the Company but rather by the Russian Federation's and Yakutian budgets, so the 1.3 billion is not something that we received. On a more serious note, we have already received the proceeds from the sale of a small stake of 2% and we used that to reduce our debt portfolio. The remaining 1.3 billion of our short-term debt will be repaid somewhere between the 15th and 20th of December when we receive the proceeds from Rosneft. Talking about our plans for next year, we have a 10-year bond maturing then which was issued in 2004 and is maturing in 2014, so we might consider issuing another instrument to refinance that. That could be a five- to seven-year Eurobond or those could be facilities from our partner banks. We are yet to see what that is going to be in terms of instruments.

Maria Gancheva

That's very clear, thank you very much. Just to follow up, my last question – in terms of your payments to be received from Evraz, is there any delay or everything is according to plan?

Igor Kulichik (translated)

Evraz is performing on its obligations in terms of its payments for Timir. We have no worries or concerns as to why they wouldn't fulfil their obligations in 2014 as well.

Neri Tollardo – *Morgan Stanley*

Thank you very much for the presentation. One quick question, are you able to disclose how many carats of inventory you have currently on your balance sheet? Thank you.

Igor Kulichik (translated)

Our inventories have not seen any significant change from the last disclosure date and are in the range from 17 to 18 million carats.

Dan Yakub – *UBS*

Good afternoon, just a couple of questions on the mining side of things. What is the current stripping ratio, let's say, weighted average across all of your open pits, or maybe you can list the stripping ratio for each of those. What is the outlook in terms of your ten year mining plan, what will be the stripping ratio going forward into the future. The second question relates to your underground plans. I think you're aiming to mine from 25% underground going up to about 35% into the future. As you go deeper underground, as you're mining from depth greater than you're mining now, do you expect to mine diamonds that will be smaller or do you expect there will be no change in the actual product mix as you go deeper underground? Thank you.

Igor Kulichik (translated)

As for your question on the stripping ratio, we'll follow up to you on that with information across all of our pipes. But there is an important factor that has to be understood here. All the pipes that we currently operate are at active operation stage and have been mined for a long time. Therefore, the ratio of extracting empty ore would be minimal there. Just to reiterate, we will follow up to you on that with the table across all of our pipes, not to read them out now. As for underground mining you are entirely right. We are currently producing some 25% from the underground. We are targeting on 34% by 2020. As for the quality and quantity of diamonds that are to be mined from there, our geologists have a very good understanding of what we should expect from there. And we don't expect any significant changes going forwards from the current mix.

Boris Krasnojenov – *Renaissance Capital*

Good afternoon, gentlemen. I have a question regarding your sales and production volumes in Q3. Could you please provide some colour? We see that sales volumes of gem- quality rough diamonds are down 22% quarter-on-quarter. Industrial rough diamonds up 37% quarter-on-quarter. Is it because of the increase of production of rough diamonds and drop in production of gem-quality diamonds? Sorry if I just missed on the presentation, but I couldn't find the breakdown of production volumes between gem-quality and industrial rough diamonds. Thank you.

Igor Kulichik (translated)

Well, that is not a very useful exercise to compare quarter-on-quarter sales in carats for gem-quality and industrial quality diamonds because our marketing experts and sales people would sell what they think to be the fittest for the current market environment. So sales volumes of gem-quality and industrial quality diamonds could fluctuate throughout the year very significantly. The only reasons for that are the market and the marketing. There are no other hidden reasons behind that.

Nicolay Sosnovskiy – *VTB Capital*

Hello, thanks for the presentation. The majority of my questions have been answered already but I've got a small one actually. I remember maybe months ago Lukoil was commenting on their Grib pipe and that the asset is about to start producing at the end of this year. What is your view on this particular mine and is there any chance that it might end up in ALROSA's portfolio as a national consolidator of the industry in Russia? Thank you.

Igor Kulichik (translated)

We know this asset quite well and we follow it. Yes, Lukoil is targeting to commence production and beneficiation early next year and in the next year they are targeting to already sell from there. We discussed with Lukoil a potential sale of that pipe about a year ago. But our geologists find it difficult to assess exactly what raw material is there in that pipe. So we decided not to rush, basically to let Lukoil start production there, see what comes out of that pipe, see how it develops and then to consider the potential purchase of the asset.

Nicolay Sosnovskiy

So, theoretically, if the actual production proves the good quality of material, you would reconsider buying the deposit?

Igor Kulichik (translated)

Yes, we say that openly if the asset proves to be interesting and if we agree on the price then we are prepared to discuss with Lukoil the purchase of this asset.

Alexander Morin – *Sovlink*

Good evening. Thank you for your presentation. I have two questions about your target debt for 2014 and the level of total debt to EBITDA for 2014. Thank you.

Igor Kulichik (translated)

As we have mentioned, we see our debt at the end 2013 slightly below $3 billion. Our budget for 2014 envisages the same level of debt at the end 2014 $3 billion. We see the level of debt to EBITDA of 1.5 as quite comfortable and we intend to stick to that going forward.

Sergei Donskoy – *Société Générale*

Just one small follow-up on production and sales in Q3. You put on the stockpile approximately 1.9 million carats. How much of this do you plan to release during Q4 approximately? Thank you.

Igor Kulichik (translated)

I would like to reiterate that it is not a useful exercise to compare production and sales on a quarter-by-quarter basis. Talking about 2013, we expect end-year inventory to remain at the current level that I've mentioned, i.e. 17 to 18 million carats. I would also like to reiterate that the numbers of mining and sales on a quarterly basis do not correlate because they depend on the decisions that our marketing experts make on a daily basis.

Thank you very much for your attention. If you have any further questions you can also follow up with us, we'll be happy to answer.