Speech by Graham Kerr, Chief Executive Officer, South32

BMO Capital Markets Global Metals and Mining Conference

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It's great to be presenting at the BMO Annual Global Mining and Metals Conference for the third consecutive year.

We recently announced our half year results for FY19.

I'll start today by taking you through the highlights, before moving to our short and longer-term outlook, including the progress we have made in reshaping our portfolio as we position South32 for the future.

As always, I draw your attention to the important notices on Slide 2.

To our highlights. A strong operating result and higher commodity prices helped deliver improved earnings and returns to shareholders in the half.

Underlying EBITDA increased by 20 per cent, Underlying earnings increased by 18 per cent, free cash flow from operations was $718 million and we closed the period with a net cash balance of $678 million.

Our strong financial position allowed us to announce a fully franked interim dividend of 5.1 cents per share and a fully franked special dividend of 1.7 cents per share taking total dividends declared for the half to $344 million.

These returns come in addition to the $167 million returned to shareholders during the half through the continuation of our on-market share buy-back program.

Of our $1 billion capital management program, the remaining $127 million is expected to be returned to shareholders by mid-April depending on market liquidity and value with our on market share buy-back.

Over the past six months we've made real progress reshaping our portfolio, completing the acquisition of Arizona Mining and Eagle Downs, advancing greenfield exploration partnerships, and progressing the divestment of South Africa Energy Coal.

Before discussing our sustainability performance, I'd like to address our approach to tailings management.

Our thoughts are with the family members, friends and colleagues who have lost or are missing loved ones as a result of the tailings dam collapse near Brumadinho in Brazil.

This is an industry changing event.

The industry needs to rebuild trust and increase transparency about the risk that exists, but also push hard to have a common reporting framework so companies that are doing well, or better, can be clearly identified and shareholders can ask questions about the ones that aren't.

Moving to our sustainability performance and starting with safety.

We are working hard to create a workplace where we can guarantee everyone returns home safe and well at the end of every shift.

Our total recordable injury frequency and employee occupational illness rates both showed encouraging trends in the past six months and we've seen a significant improvement in the proactive identification and reporting of potential significant events.

Greenhouse gas emissions are tracking below target and we are progressing climate resilience assessments at our operations.

While we haven't included the figures on our slide here today, we also continue to make progress towards our diversity objectives in our workforce and leadership teams as we strive to create an inclusive workplace which reflects the communities where we operate.

Moving to our operations. A strong operating performance, higher commodity prices and robust cost control ensured our operating margin remained elevated at 38 per cent.

We achieved another production record at Australia Manganese and significantly improved longwall productivity at Illawarra Metallurgical Coal where we've increased production guidance by 7 per cent to 6.5 million tonnes.

We continued to benefit from our long alumina position. However, the elevated prices in the alumina market and higher pitch and coke prices placed great pressure on our aluminium smelters as the LME price declined by 9 per cent in the period.

At our Hillside smelter in particular, we continue focus on the costs we can control around labour to ensure the smelter is set up for sustainable success through the cycle.

We have commenced consultation to restructure the business with the aim of reducing controllable costs and improving Hillside's resilience to volatility in commodities markets.

Separately, we continue to negotiate with Eskom to deliver a power contract that will underpin the long-term sustainability of the operation.

For the full year we have lowered or maintained unit cost guidance at all operations and expect Group volumes to rise by 5 per cent in FY19 and by 7 per cent in FY20 as our operations deliver more consistent production.

I now want to touch on a couple of our key commodities including manganese.

We had a shift in our view around 24 months ago that has played out in the past 12 months. With grade degradation in China and an increase in the intensity of use in steel making, the supply response has had to come from South Africa with ultra low-grade ore.

As a result, the cost curve has steepened. With no substitutes available through scrap, and the next phase of South African supply to come from underground, we think the industry economics for manganese are very attractive and that GEMCO is the best asset in the industry.

Moving to alumina where we have a 3.4Mt long position into the third-party index market, we haven't changed our long-term view of price despite the recent impact of supply disruptions.

Looking forward we expect aluminium demand to pick up in the second half of 2019 following a soft 2018, as demand from autos improves providing additional demand for alumina.

Given the finely balanced nature of alumina supply into aluminium we expect prices to be supported in both the near and the longer term as deteriorating Chinese bauxite supply and the cost of importing ore from West Africa or South-East Asia will continue to steepen the cost curve.

Our Worsley refinery in Western Australia which is in the first quartile of the cost curve is expected to see further benefits to costs in the second half of this year as we consume less caustic soda and high-priced inventory rolls off

Our non-operated Alumar refinery will benefit from the same dynamic in caustic soda prices while a reduction in bauxite costs, relating to its index linked pricing mechanism will provide a further tailwind to costs.

Moving to our portfolio, we continue to develop a pipeline of opportunities to compete for capital, with a bias towards base metals.

We constantly review our portfolio having started life four years ago with a collection of assets and no brownfield or greenfield options.

We continue to unlock opportunities in some of these businesses.

In Brazil, our partners have approved a pre-feasibility study to extend life of mine at MRN with a lower capital cost option.

At Worsley Alumina, we've commenced several improvement initiatives that are expected to support a sustainable increase in production to nameplate capacity.

At Illawarra, we advanced the Dendrobium Next Domain project into feasibility.

And we moved closer to approval to explore the Southern Areas at GEMCO.

We are also working hard to reshape our portfolio.

During the half year we completed the acquisition of Arizona Mining, adding the Hermosa project's high-grade zinc-lead-silver resource and prospective land package to our portfolio.

We also completed the acquisition of a 50 per cent interest in the Eagle Downs Metallurgical Coal project and assumed operatorship.

Eagle Downs embeds another attractive development option within our growing portfolio in a commodity where we see strong long-term fundamentals.

I'll provide more on both development projects shortly.

Our process to divest South Africa Energy Coal remains on track with binding bids expected by the end of this financial year.

In terms of building longer dated options, we believe in growing value by the drill bit.

We are committed to greenfield exploration and are currently advancing partnerships in Australia, Europe and the Americas.

We have maintained our option with Trilogy Metals for the third and final year of the agreement to potentially increase our interest in the Upper Kobuk Mineral projects in Alaska.

We can earn a 50 per cent interest in the high-grade Arctic polymetallic resource and a large Copper target known as Bornite.

Both properties have existing foreign resources with Trilogy completing a Preliminary Economic Assessment on the Arctic project in April 2018.

The option to earn a 50 per cent interest can be exercised any time before 31 January 2020 by committing $150 million to the joint venture.

Moving to Hermosa, one of the world's most exciting base metals projects.

Work has commenced on project studies and early stage surface infrastructure.

We have undertaken further resource drilling to increase our knowledge of the orebody and remain on track to declare a maiden Mineral Resource for the project by the end of June this year.

We have also identified a series of regional exploration targets that will form part of an initial exploration program on the broader land package.

Our FY19 capital expenditure guidance for Hermosa has been lowered from the preliminary $100 million estimate to $70 million, with the reduction largely reflecting the reclassification of $20 million of expenditure from the initial Arizona Mining budget to capitalised exploration as we increase our knowledge of the Hermosa resource.

We also completed the acquisition of a 50 per cent interest in the Eagle Downs project during the period, giving us control of a fully permitted, partially developed metallurgical coal mine, with a 1.1 billion tonne resource in Queensland's Bowen Basin.

We have commenced feasibility work on the underground longwall project and expect to make a final investment decision with our JV partner during the second half of the 2020 financial year.

Our capital management framework remains unchanged.

We will continue to drive return on invested capital by optimising our portfolio making disciplined capital allocation decisions and prioritising a strong balance sheet to ensure we retain flexibility through economic cycles allowing us to return excess capital to shareholders.

This approach has served our shareholders well.

We have a strong $678 million net cash position and with payment of our fully franked interim and special dividends, and completion of our currently approved capital management program in the second half, we will have returned $2.4 billion to shareholders over the last three years, the equivalent of 20 percent of our market capitalisation.

To conclude, we are reshaping our portfolio, pursuing opportunities within our existing operations, and advancing and cycling greenfield options to grow value per share.

The ordinary and special dividends announced at half year, and continuation of our on-market share buy-back demonstrate our strong financial position and commitment to our capital management framework.

We are well positioned entering the second half of the year. Net cash is $678 million and Group volumes are expected to rise by 5 per cent in the 2019 financial year as our operations deliver more consistent production.

We are well placed after a solid start to the year to continue to reshape our portfolio and build the foundations for future value creation.

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