

## **Speech by Mike Fraser, Chief Operating Officer, South32**

### **2019 Mining Indaba**

4 February 2019

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Good morning everyone.

I'm pleased to be here again at the 2019 Mining Indaba.

It's been a significant 12 months for our industry here in South Africa. In February last year, I noted that we were already seeing positive signals for the revitalisation of our industry and that we looked forward to a constructive dialogue with our political stakeholders.

Today, we can say that we have indeed had that constructive dialogue and that the collaborative working style of the Minister of Mineral Resources and his team has resulted in considerable progress in the last year.

We now have agreement on the Mining Charter and its implementation guidelines, which has provided much-needed policy certainty in South Africa.

However, we still need clarity on the matter of continuing consequences as it refers to renewal of mining rights, which is a material issue for the industry. We hope that the constructive dialogue will continue and bring a resolution of this matter.

Today I'll talk briefly about South32 and the changes we've made to our business in the last year, both globally and here in South Africa, before looking at the role of Eskom in securing our national competitiveness.

But first, let me give you a brief overview of South32's business.

We have operations and development projects spanning four continents and we have a primary listing on the Australian Securities Exchange, a secondary listing on the Johannesburg Stock Exchange and a standard listing on the London Stock Exchange.

Here in Southern Africa we have sizeable energy coal, manganese and aluminium operations with almost 8,000 employees.

Since South32 was formed in 2015, we have remained focussed on our purpose – to make a difference by developing natural resources, improving people's lives now and for generations to come.

In the 2018 financial year, we paid almost US\$170 million in taxes and royalties in South Africa and Mozambique.

Globally, we spent over US\$20 million on community investment, with eighty-five per cent of that investment made here in Southern Africa.

## **Reshaping our portfolio**

The last 12 months have been significant for us at South32, as we have continued to review and reshape our portfolio with a bias to base metals.

The global shift towards a low carbon economy is driving use of renewable energy, electric vehicles and batteries.

Our industry is responding, by working to ensure continued supply of the commodities the world needs in a more sustainable future. In addition, we are working to reduce our own carbon footprint, for example we recently installed a three mega-watt solar farm at our Cannington operations in Queensland.

We are positioning South32 for the next phase of commodity demand growth by creating a pipeline of development opportunities in commodities that we believe will have strong fundamentals into the future.

In August last year, we completed the acquisition of Arizona Mining which added the high-grade zinc, lead and silver Hermosa development option to our portfolio as well as a prospective land package.

We also acquired a 50 per cent interest in the Eagle Downs metallurgical coal project in the Bowen basin, Queensland, and have exercised the third-year option with Trilogy Metals targeting a high-grade copper extension in Alaska.

We have also entered into several exploration agreements with junior partners for projects in Australia, the Americas and northern Europe.

The strength of our balance sheet has always been a priority, and we remain committed to our capital management framework where we:

- Maintain safe and reliable operations and an investment grade credit rating through the cycle
- Distribute a minimum 40 per cent of Underlying earnings as ordinary dividends
- Allocate excess capital among the competing options of:
  - Investment in the business
  - Acquisitions
  - Greenfield exploration
  - and our capital management program

This disciplined approach has enabled us to return US\$483 million to shareholders in the December 2018 half year, through the payment of US\$316 million in dividends and US\$167 million through share buy-backs.

## **Broadening ownership of SAEC**

In the last 12 months, we commenced managing our South Africa Energy Coal operations as a stand-alone business within the South32 portfolio, with its own management team.

This allowed us to simplify the way we work by collapsing our regional model to create a single set of global functions that work directly with our operations. The simplification of our organisation is expected to deliver a US\$50 million annual cost saving to mitigate further industry wide inflationary pressure from the 2020 financial year.

We also commenced a process to broaden ownership of our South Africa Energy Coal business and we expect to receive binding bids in the June 2019 half year.

Our intention is that South Africa Energy Coal becomes black-owned and operated, as we believe this will best support the long-term sustainability of the business while also supporting South Africa's transformation agenda.

We believe coal demand will remain resilient in nations with relatively new coal power plants or those with planned additional capacity. These are typically integrated operations with low cost deposits near the plants.

South Africa is one such location, which creates future demand for our South Africa Energy Coal business.

Divesting our thermal coal position in South Africa to a black-owned business will enable South Africa Energy Coal to more effectively compete for new supply contracts and mining rights. We are also working to define a mechanism for communities and employees to share in the value generated by the business – in keeping with the spirit of the Mining Charter.

South Africa Energy Coal is a large and complex business, with a sizeable resource base, existing coal processing and logistics infrastructure, and a significant position in the world class Richards Bay Coal Terminal. Thousands of employees and contractors directly depend on the business, with more indirect jobs and local businesses having a vested interest in its long-term operation.

We are investing R4.3 billion in the Klipspruit extension project, but additional investment will be required to sustain production and deliver on the potential of the resource base.

It is imperative that we identify an owner with the necessary mining expertise and financial backing to ensure the business remains sustainable.

South Africa Energy Coal plays a critical role as a major supplier of coal to Eskom and we fully understand the importance of ensuring continuity of supply over the long term.

We have a strong working relationship with Eskom, both as a supplier and a customer. But we, like many others, are concerned that its challenges have increasingly threatened the sustainability of its business.

Eskom continues to deal with those challenges, and it is encouraging that the process of renewal is underway with the full support of the President and the Minister of Public Enterprises.

Eskom's Board and CEO Phakamani Hadebe have made excellent progress in recent months, but there is critical work which must be completed to stabilise Eskom's business. The forthcoming recommendations from the Presidential Task Team will inform the work which has to be done, and the timing.

We see a number of priority actions in the short term, including:

- An equity injection from the shareholder to recapitalise Eskom
- An aggressive cost reduction program in all areas of the business

Eskom's twin challenges of overstaffing and a shortage of key technical skills within its workforce must also be addressed, with gaps in capability to be remedied with training as a matter of urgency to improve technical performance.

We support views that Eskom should be broken up to ensure appropriate management focus on each of its core areas and believe this work should commence in parallel with the short-term measures.

Check against delivery

South Africa's future economic growth and the fulfilment of its development aims are inextricably linked to the sustainability of Eskom. But Eskom's current situation is the single biggest risk to South Africa's economy.

In the near term, potential tariff hikes and supply interruptions present a challenge to energy intensive industrial users, as they risk a fall in output coupled with increasing costs.

Urgent action on stabilising Eskom can help minimise interruptions to customers while avoiding tariff hikes, which is key to ensuring industry remains competitive and continues to employ millions of South Africans.

The government has focused on increasing foreign investment as a key component of a long-term re-industrialisation of South Africa that can boost jobs and business opportunities.

However, the price of electricity is a key factor in South Africa's ability to compete for investment in industrial development.

When compared to other countries, the cost of power weighs on South Africa's bid to increase foreign direct investment and impacts existing industry.

The current scenario risks a downward trend in the proportion of electricity sales derived from industrial customers – a reduction that Eskom cannot afford and that increases the likelihood of further tariff hikes for all.

These consequences can jeopardise South Africa's economy, reduce enterprise development and slow the creation of jobs.

Industrial development is long-term in nature and requires stimulus to bring investment that will add sizeable, consistent demand and predictable revenue for Eskom.

Eskom's consideration of an industry tariff has potential to boost efforts to attract foreign investment but to be effective, the tariff must be designed and implemented with this goal in mind.

It is imperative that this tariff reform takes places urgently to protect industry in the near-term.

It goes without saying that all parties must work together to ensure Eskom's stability. As an industry, we stand ready to assist by sharing our collective experience and expertise.

Over the longer term, Eskom needs a business model which will retain key industrial customers, who are already large domestic employers, while also supporting South Africa's competitiveness on the global stage.

Eskom is the engine of South Africa's economic growth. A robust national power utility that is sustainable over the long term will benefit everyone.

I wish you all a successful Mining Indaba and thank you for your attention.

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