

The Melbourne Mining Club – Melbourne, Australia
Leigh Clifford, Chief Executive – Rio Tinto
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Mining: the way ahead

I'd like to thank the Melbourne Mining Club and the Victorian Minerals and Energy Council for organising this event.

This afternoon I will talk about the mining industry, the changes taking place, the performance of this industry and, specifically what's happened in Rio Tinto. I will touch on the future, especially China, because it's having such an impact on our industry.

Metals are an integral part of our lives, and demand continues to grow with GDP. But, eventually, exhausted deposits must be replaced. If you look at something like copper as an illustration, what we need is effectively an Escondida Phase Four expansion every year. Under normal circumstances, the growth in copper means that we're going to need projects of that nature every year.

So, what I'm really saying in essence is, it's an industry which is growing, and very much related to the prosperity of the world. But the nature of the industry has changed quite considerably. If we look at the structure of the industry in 1990 - and you can see the market capitalisations at that time - what you can see is that the three major mining companies comprised about 20 per cent of the global mining sector at that time.

When we look at 2002, those three major companies comprise about 40 per cent. We shouldn't be surprised by this consolidation because we're seeing it occurring in oil, pharmaceutical, autos, and steel. But nonetheless, it's the way of the world.

But then, we look back over the last 30 years at the profitability of the mining industry. When you look at the resources industry over those 30 years, it looks pretty good. About eight per cent as a real annualised shareholder return over those 30 years.

But it masks something - an under-performance by the minerals industry, when you take out the oil and gas sector. So what we've had is the minerals industry being characterised by a good performance by some, and certainly underperformance by a number.

Fortunately, for those of you who are Rio Tinto shareholders, and I hope that that's an increasing number; Rio Tinto's performance over those 10 years has been very solid. If you compare our total return against the ASX All Ordinaries over three, five, and ten years, you can see that Rio Tinto shareholders have done pretty well. Boringly solid and predictable, I'd like to say, under these circumstances, of the sort of controversy that we've seen over the last couple of years.

If I showed a similar story against the S&P 500 or the FTSE, it would be somewhat comparable. Against the HSBC Global Mining Index, which comprises 137 mining securities in 26 companies, over those 12 years, you've also seen an out-performance by Rio Tinto.

Well, what's driven that success? Firstly, I think we've had a reputation for prudent investment and disciplined investment in terms of the projects we've been involved in. We've been able to achieve, over the last 12 years, a six per cent per annum growth in our production. That's not a target - it's an outcome, of seeing value-creating opportunities. And we have, going forward, a number of high quality projects which will lock in that growth for the next three or four years.

I might add, when you look at those five projects described there, they will all be margin-enhancing, and given that we have a cash margin in the high 20s, I think you can see the quality of those opportunities.

A number of factors have contributed to that performance. A major one has been the Group's performance in Australia during the 1990s. We've had a more competitive industrial relations regime, initially in Western Australia, and more recently, federally. And we've had a more engaged workforce as a result of some of the changes that have occurred. Let me just go through some examples.

I think anyone who's been associated with the mining industry would remember well the history of industrial disputation in the Pilbara and Hamersley was certainly amongst that. This chart demonstrates the hours lost in the early 1980s through to 1993 - 1993 being when we introduced the All-Staff workforce. We no longer see those headlines and certainly from my experience there, we have a more engaged workforce, and I might add, a better-remunerated workforce.

The removal of those barriers has unleashed a raft of improvements. This illustrates the performance of our rail division in terms of productivity, and as you can see, it's been a dramatic increase over the space of about 14 years. We have now merged the rail operations of the Robe River Joint Venture and Hamersley and the Pilbara Rail Company is now raiing greater than 100 million tonnes of iron ore per annum.

Ultimately, though, what about the productivity of Hamersley? As this graph demonstrates, there's been a five-fold increase in productivity over the last 20 years. We've done that at the same time by squeezing more out of our capital. Effectively, we've been able to drive our plant and equipment harder and obviously that's been a contributing factor to the economic performance of Hamersley.

We've been able to do that without compromising safety. I think this is a real credit to the organisation. I'll talk a little bit more about that later. We can show similar stories for our aluminium businesses where productivity lifted dramatically during the 1990s. And even Bell Bay, which is a 1950s smelter that was revitalised in the 1990s, is a profitable operation.

I think you're all very well aware of the coal industry, and the years of what I'd call profitless prosperity. We had a growth in demand of six to eight per cent per annum, but an industry that under-performed.

And this is an illustration of what's transpired at Mount Thorley and I was there yesterday and I'd have to say it's certainly impressive. Productivity, ultimately in the coal industry, is about moving the overburden, and as you can see there, the overburden removal has improved dramatically. We're producing the same output of coal but we're also doing it with one shovel instead of two, two loaders instead of three, fifteen trucks instead of twenty-one.

There's a similar story at Blair Athol, our major coal mine in Queensland and that performance in the late 1990s. That improvement in productivity was also accompanied by more difficult mining conditions as we mined through the old workings of the previous operations at Blair Athol.

All of this has contributed to a change in culture in our operations and I think it's important to realise that it's across the breadth of our operations in Australia.

The performance that you'd all be aware of in Rio Tinto has been simultaneous, or has been concurrent with drops in real prices. So, in effect, the economic performance of the Group has not been a consequence of price, but of productivity.

And we've done this throughout with an improving safety performance. We're very proud of our performance in safety. It is far from where we want to be, but I think it's nonetheless an outstanding performance.

And we've also acquired businesses in the course of those years and we've been able to improve the safety performance of those businesses. We have a very demanding set of what we call minimum safety standards, if you like 'the gold rules', and we implement those in our operations globally.

Also, our definition of lost time injuries involves not only our employees, but also all contractors who work for us and we demand that the measure be on the basis that an employee is able to return to work and do the full job they are normally employed to do. So, we are quite demanding in terms of what we categorise as a lost time injury.

I talked a little earlier about consolidation in the industry and obviously associated with that consolidation with a company like Rio Tinto is a consequence of a wider diversity of product, and that's been built up over time, and wide market diversity. Obviously that shields us from some of the variations that occur and, as you can see, our sales are spread pretty evenly between Europe, North America, Japan and emerging - and I'm going to talk a little bit later about it - China. But as a consequence of this diversity, what is basically a cyclical industry, in the case of Rio Tinto it's a lot less cyclical because of the diversity of our products and markets.

We also have a concentration of our assets in Australia and North America. Now at times, people are concerned about the mining industry, as they say, North America, that's Canada, around 15 per cent and USA at 25 per cent and, Australia are basically high wage cost countries. But the reality is the mining industry of today is about capital productivity and about employee productivity. We're very comfortable where we operate. The rule of law, the familiarity with mining, the certainty of contracts are all contributing factors to the success of our businesses, if you like, political stability.

We also have what I'd call an outstanding reserve base. Now bear in mind this is our reserve base, not our resources. For instance, in coal, we have resources substantially greater than this. But I think you can't ultimately beat access to high quality, long life, and low cost assets. We've built a position second to none.

Ultimately we've got to replace some of those assets and I'm pretty pleased, as we said in our half-year results, about the broad range of exploration opportunities we've got. Exploration is characterised by, as a number of geologists who are here would know, by more disappointments than successes. But I'd have to say we've got probably one of the best suites of exploration opportunities for some time. And it's certainly a very focused exploration effort. Obviously we have our ongoing focus of what I'd call near-mine exploration and over the years that has made a significant contribution in the case of Hamersley and even Argyle.

I want to talk now a little bit about China, because the opportunities and, to some degree, the threats for our business, or challenges, in the minerals area are quite considerable and perhaps, longer term, even Russia.

If we look at China, it is certainly emerging as a major consumer of minerals and here is an example of aluminium and copper and iron ore. It is becoming a major player. And nowhere is it illustrated better than in the case of steel and iron ore imports.

I'd have to say that in 2002, the statistics that our people tell me - I'm concerned about in case they're wrong - they're strong double-digit growth rates. And certainly we're seeing iron ore imports extremely strong, because China has very limited iron ore of its own and poorer quality iron ore, and as a consequence, demand for iron ore is considerable.

We've had long links with China. First, exporting iron ore in the early 1970s. We established the Channar joint venture in the late 1980s and most recently announced our joint venture with Baosteel and the involvement of Shougang in the Hismelt project in Western Australia. Shougang is also our partner in an exploration project in Peru, which is showing early promise.

I thought this table here illustrates some of the opportunities that really exist with metals. As you can see, the left hand scale is a log scale and as the GDP of China improves the demand for aluminium is probably going to follow that traditional curve and be substantial. Certainly we see that at the

moment. And I think the more we look at it, the more pleased we are with our decision to invest in an alumina project in Queensland, in Gladstone. And, as you know, we have plans that ultimately could lead to Rio Tinto being a six million tonne per year alumina producer, in about a decade or so.

A similar story with copper, and I suppose you come to the conclusion that China has the same potential maybe, in terms of its impact on Australia's raw materials business, that Japan once had.

Well, what about growth in Rio Tinto? As I said, growth is an outcome of economic opportunities, not a target in itself, and currently we have nine, or involvement in nine major projects around the world under construction. And five of these are in Australia, where this investment totals US\$1.7 billion. We're very pleased with how they're going. The West Angeles project is being formally opened this weekend and our Hail Creek and alumina projects are well underway. Northparkes is more modest, but nonetheless it's going to improve the performance of that business long term.

So, in conclusion, we see there are many paths to creating shareholder value within the Rio Tinto Group - certainly capacity expansion as illustrated by our expansion over the last 40 years at Hamersley, or improving our asset performance, that is building on our existing base. By asset performance, I mean, as an illustration, we have 750 large off-highway trucks around the world. If we can get the bottom 375 performing like the top 375, we can improve the performance of our business.

Technology - all of you would be aware of what we're doing in HIs melt, but our upgraded slag project at QIT in Quebec, which is a high titanous slag, has really made that a premium product in that business.

Obviously, there are mergers and acquisitions, but increasingly that's becoming very competitive.

Greenfield projects like Hail Creek and the alumina project, and anyone who has been associated with Rio Tinto, or CRA, is well aware of how long and diligently we've looked at those projects.

And exploration, Diavik is a classic illustration of an exploration success.

So I hope you feel that Rio Tinto is well placed to capitalise on the emerging opportunities, both within Australia and globally and maybe I'll leave it there and I'd be happy to answer any questions.

Thank you very much.

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Questions and answers

HOST: Thanks, Leigh. We have about 10 minutes for questions, so perhaps I may take the first question and we'll move it on from there.

QUESTION: **Leigh, your investment in Terex relative to Caterpillar, Komatsu and Euclid - why did you do it and how has that progressed and what value do you see in potentially a vertical integration?**

RLC: Sorry, we don't have investments in Terex. What we do have is a global approach to purchasing. Now I'm not sure if that's exactly what you're asking. When we purchase, if you like, the 20 per cent of items that comprise 80 per cent of costs, we involve our managing directors of our business units globally and they negotiate, sometimes on a global basis, sometimes on a regional basis, with our major suppliers.

It's not centralised, but it's coordinated and obviously we use the size of our market to hopefully enable a better deal. I'm not sure if that's what you asked, but we're not involved in Terex or Euclid.

QUESTION: **If my eyes weren't playing tricks, I didn't see any exploration opportunities in Australia on the map that you displayed, Leigh. Would you comment on that?**

RLC: We obviously have some exploration activities that are at earlier stages. We do have, as I said, near-mine exploration, certainly around Argyle and in the Hamersley Ranges and we have spent a fair bit on exploration recently around Ranger, which has contributed to a slight extension of that operation.

We do have exploration activities, but I'd describe it as early stage exploration. To some degree, it depends where you're lucky enough, or you happen to have an opportunity. Those are the ones which we've been very public about. As you know, exploration is a number of years in the gestation period.

QUESTION: **At 'Diggers and Dealers', the Newmont camp were talking about their interest in joint venturing with some of the smaller juniors in Australia.**

What's Rio's position in terms of getting some of the juniors to actually work with them to find ore bodies?

RLC: We have had a long history of farming into exploration opportunities not only of juniors but of majors also. For instance, in Turkey at the moment, we're involved with Anatolia Minerals in the Copley deposit and you'd be aware of our partnership with Aber in the Diavik diamond project. So, as a principle, we are certainly open to the opportunity.

QUESTION: **You mentioned a couple of times in your speech about HIs melt. Could you elaborate a little on the program you see ahead of that process development?**

RLC: Yes. Well, a number of people here have been associated with HIs melt over many years and we've been involved in that project over the last 20 years. About two years ago, we shut down the pilot plant that had run for a number of years in Kwinana. We're very satisfied with the performance of that. And we are now in the permitting stage and hope to have in operation by, I think it's early 2004 - what I'd call a semi-commercial stage operation, which will really test the scale up of that plant: 800,000 tonnes of pig iron, investment about US\$210 million, our partners are, as I said, Shougang, the iron and steel company near Beijing, Nucor in the US and Mitsubishi Corporation. This will be the next real test, but I'd have to say the pilot plant was extremely successful and that's what gave us the confidence to go ahead.

QUESTION: **Leigh, what would you see to be the threats to China retaining the growth rates on an ongoing basis?**

RLC: Well, I'm not an economist, but I suppose those who are who I've listened to talk about the management of the state owned enterprises, which tend to have high debt and in many cases maybe are not economic. But the social consequences of making those adjustments are quite considerable.

The Chinese recognise that and I think are trying to manage their way through that. I suppose that is the most significant issue.

I'm giving a talk elsewhere and one of the statistics I quote are the number of people employed in the Chinese coal industry. It produces a little over a billion tonnes and there are six million people employed in the coal industry. So you can appreciate the fact that maybe even though wages are relatively, or very low,

some of those projects are not economic, but whole communities are dependent upon them. So I suppose that's the major challenge they face.

QUESTION: **My question is related to the previous one. I'd be interested to know what you see as the major threat for Rio Tinto's growth in the future and to what extent environment, safety and community issues play a role in that?**

RLC: Well, I think firstly any company in any industry that is not conscious of workplace health and safety is going to find difficulties. The community expects that any employee who goes to work in a company like ours will return home uninjured for every day of their working lives and I think that's not unique to the mining industry.

I think we've also got to recognise that communities have a voice and they want to be heard, be they indigenous communities in developing countries, or communities in the Hunter Valley, or Gladstone, or what have you. And they expect to be heard. I think companies are extremely conscious of that.

I wouldn't want to go into what I see are the threats to Rio Tinto, but what I would say, in the metals industry, certainly China poses a threat, or a challenge if you like, in a number of areas. It's impacting on steaming coal. It's certainly impacting on aluminium and zinc.

I think we've also got to recognise that Russia has enormous reserves of low cost hydro-power and is obviously going to be a player in the aluminium business. But fortunately, both China and Russia are short of alumina, so I think we're quite well placed in that regard.

QUESTION: **You touched upon an issue that I wanted to mention, which was Russia. Clearly a company the size of Rio has some ideas, some views on doing business in those former Soviet countries. What do you see as probably the biggest barriers to western companies being successful in that type of developing environment?**

RLC: I suppose firstly I'd say about the former USSR, don't imagine that it hasn't been explored. Now I'm not saying it's been explored with the best technology, but the former USSR had a large number of geologists, and because of the Cold War period, certainly spent a lot in terms of trying to find strategic metals and others.

I think the greatest barrier - and it's not unique to China - is, if you like, corporate governance, the rule of law, the security of title, the sanctity of contracts.

Putting that to one side, obviously countries have got to have a competitive taxation regime, the ability to repatriate profits, et cetera. Let's face it, Russia and others are in competition with countries like Australia and Canada, et cetera, for the savers' dollars, or the investors' dollars.

QUESTION: You mentioned China with some very impressive growth rates in terms of aluminium and copper and all of the minerals and metals and so on, that the mining industry is associated with. But to date, the record of mining companies actually investing in projects in China is not that good, going back over a period of 20-25 years, thereabouts.

I just wondered if you'd care to comment on Rio Tinto's attitude, given its very strong trading relationship with China and the investments that the Chinese have in fact in some of your activities.

RLC: Well, firstly, you've got to have the opportunity and then I think you have to recognise that the host government, be it a central government or a provincial government, has to be welcoming of that investment. Then the regime that I referred to, discussed in the previous question, has to apply.

I'd have to say that if we look back in history, the Australian minerals industry has done extremely well out of its relationship with Japan and Korea, supplying those developing industrialising economies with materials they didn't have.

I think that's certainly going to be an opportunity for Australia going forward in China. It remains to be seen whether there will be a desire on the part of the Chinese, or an opportunity for new minerals projects. I wouldn't want to close out that opportunity, but at the moment, I don't see any on the immediate horizon.

I'd also have to say that when you look at China, anything that you might contemplate, we have to recognise the infrastructure limitations and therefore it would have to be high value commodities or minerals that we might invest in.

QUESTION: You've mentioned China as an opportunity in terms of iron ore and alumina. Is it not a threat as well though? I guess, you know, they may be the biggest consumer, but they also have managed to attract quite competitive pricing. Is that then a threat in itself, because they get a competitive price and we may actually see prices under pressure?

RLC:

It will be interesting if you had a number of the steel producers in this room from Europe, or Asia, they would say the consolidation of the mining industry is a threat.

I'd have to say it's a competitive environment out there. It's a good market and I'd say that I haven't seen a real concern, but I'd have to say that I think that given the magnitude of the demand and what I'd call increasing demand by investors that minerals companies make prudent investments and are disciplined in their approach to investment, then I think the future augers pretty well.

So those issues always arise, but, as I said, if you're asking some of the consumers, they'd see it the other way around.

Thank you very much.