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Delivering value through the cycle

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Check against delivery

I am very pleased to be here and to have this opportunity to speak to you today.

I acknowledge the Traditional Owners of this land, the Whadjuk people of the Noongar nation, and I pay my respects to their elders, past and present.

2016 marks the 50th anniversary of our first iron ore shipment to Japan, and the Pilbara business we have built and the value we have delivered over five decades is something of which we are very proud.

Our global iron ore business is headquartered here in Perth and Western Australia will continue to be dominant in Rio Tinto thinking.

Today I will be sharing some thoughts about Rio Tinto's continuing history of operational excellence through the cycles.

A robust vision, a clear and consistent strategy tier one assets and tier one people have enabled us to deliver enormous value to our shareholders and will continue to do so into the future.

As managing director of Rio Tinto's Pilbara iron ore mines, I will mainly focus on our Pilbara mining operations.

As always, I will start with safety.

In everything that we do, the safety of our people remains Rio Tinto's most important value.

We saw marked improvement in safety across our iron ore operations in 2015 as the all injury frequency rate decreased by 32.9 per cent from 2014. We are working diligently to reinforce this trend and to not rely on past successes, or lose our focus.

The most important part of our safety focus is our strategy to eliminate fatalities, for which we have adopted a critical risk management framework. This programme is aimed at embedding critical controls across our operations. It involves every person identifying the critical risks in a given task and verifying appropriate critical controls are in place before starting the activity.

To date, we have done over 50,000 verifications. That's 50,000 opportunities to prevent a fatality.

We are also continuing our efforts to support and promote mental health, wellbeing and resilience in our workplace, recognising that personal health and safety goes beyond the physical to include emotional and intellectual wellbeing. We are taking active steps to support our employees, looking outside the box for ways we can improve.

One example is our peer support programme, which has 450 trained peer supporters to provide confidential support to their colleagues to help deal with stress and promote wellbeing.

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Ultimately, we believe that safe organisations are successful organisations. They are workplaces that are productive, that deliver great business results, and where employees feel truly engaged in the safety culture.

Rio Tinto continues to demonstrate its ability to deliver value through the cycles, even in today's tough market conditions. It's a great privilege to manage one of the world's greatest businesses.

We believe that a tough market is a great opportunity for the best operators to excel.

Our Pilbara operations are world class, integrating 15 mines feeding 4 port terminals via 1,700kms of privately owned heavy freight railway. The Pilbara system is the key value driver in our overall iron ore portfolio, which in 2015 delivered outstanding results, including:

- FOB EBITDA margins of 60 per cent and an average of 65 per cent EBITDA over the last 10 years;
- We are the lowest cost producer in the Pilbara with a cash unit cost of US$13.80 per tonne in the second half of 2015;
- Underlying earnings of $3,952 million; and
- An 11.2 per cent increase in global iron ore production and shipments, compared to the previous year.

As an owner-operator, we have an intimate knowledge of where the opportunities for improvement lie and our first mover advantage of developing our Operations Centre in Perth and implementing autonomous technology have been instrumental to our continued success.

Increasing our productivity, reducing operating costs and working capital and delivering incremental volume expansions from high quality projects continues to enhance our capacity to generate free cash flows.

In 2015, we reduced working capital by 83 per cent year on year. We also delivered a 20 per cent productivity improvement, meaning more tonnes for every hour worked.

We are not stopping there. Our pre-emptive actions have held us in good stead to date and we will continue to take decisive action. We have announced further cost management measures and significantly reduced our capital expenditure.

I will speak more on this later in my presentation.

Over the past decade, we saw a remarkable period of unprecedented growth in demand where a significant proportion of the world's population had started on the path to development and prosperity through urbanisation, particularly in China.

This was a demand driven market that created very attractive prices, encouraging existing participants to grow rapidly as well as new supply entrants.

Today, we are going through a transitional phase, as the pace of growth in China settles into the new normal. However, we are seeing some positive signs - inventory levels are reducing and urbanisation in Asia still has a long way to go.

We expect about 220 million new urban residents in China over the next fifteen years, with a further 260 million in India and the ASEAN countries. There are other signs. For example, China's 'one belt one road' strategy aims to promote connectivity between countries adjacent to the historical Silk Road and support the export of China's infrastructure construction capacity and with it, a demand for steel. I remain optimistic.

The market is in the process of rebalancing between supply and demand. The tail-end of expansion tonnes are entering the market but are being matched by high-cost tonnes exiting the market:

- Last year, we saw about 130 million tonnes exit the contestable market, of which 35 million tonnes was from China;
- 110 million tonnes of new low-cost seaborne supply entered the market in 2015;
- Looking forward in 2016, we estimate that around 75 million tonnes of new supply will come onto the market and this should be offset by further supply exits.

While the iron ore price is well below the unprecedented peaks of the China boom, it is hovering around the long-term average and the fundamentals for iron ore demand remain strong.

Rio Tinto is the lowest cost producer on the curve and the demand for our high-quality products continues to be robust and attracts a premium.

We are continuing to focus on taking the necessary strategic and tactical actions to maintain our position

Complacency is not an option.

Our business plans for the future and the key elements of our strategy have remained consistent.

We have a constancy of purpose to concentrate on the things that we can control to meet today's challenges and position us well for the future.

We focus on:

- Safety and wellbeing
- Production at the right cost
- Maximising our portfolio value; and
- Value driven investment

For the past three years, we've had a particular focus on production at the right cost and maximising our portfolio value appropriate to the current market conditions.

We have made transformative decisions that have fundamentally changed the cost structure of our business.

But, in the broadest sense, the value equation encompasses much more than costs.

It also includes, for example, the sophisticated manner in which we plan and develop our assets, the way we integrate and maximise the value of our logistics chain and the way we build relationships with customers, communities, Traditional Owners, and government.

I'll now talk about production at the right cost.

We have moved away from an expansion phase and are transitioning to 'steady state' operations. This is where we have an opportunity to focus even more on costs and this requires discipline and accountability across every part of our organisation.

'Production at the right cost' is about maximising margin through safely delivering quality tonnes at the lowest sustainable cost.

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We have made disciplined cost management a daily habit for us and a critical component of our long-term strategy.

Each of our sites has a dedicated cost room where they monitor spend and review a pipeline of opportunities weekly. Our Executive Committee, of which I am a member, attends a weekly meeting at our cash generation office in Perth to monitor and vet these results.

In 2015, we tracked over 400 individual improvement initiatives across our sites.

This relentless focus on improvement, delivered a 20 per cent increase in productivity over 2015, meaning more tonnes were produced for fewer hours worked and the iron group has already delivered over US$428 million in savings in 2015 and over $1.1 billion since 2012. Some highlights are:

- Reduction in the Pilbara cash unit cost to US$13.80 per tonne in the second half of 2015, a 26 per cent reduction on Half 2 2014
- 83 per cent year on year decrease in working capital levels, including
    - $129 million reduction in warehouse inventory over 2015 including tyres, conveyors, diesels, explosives, parts etc. from $385 million to $256 million; and
    - 65 per cent reduction in bulked stocks from 12.8mt to 4.4mt.
- There was a 13 per cent reduction in $/tonne of total material moved (A$ real 2015) from Half 2 2014 to Half 2 2015
- $60m major HME component operational expenditure saving over life of the fleet
- And $95m in 2015 HME capital deferrals through rebuilds, second hand purchases, extension of asset life.

An example of our capital deferrals has been a project to extend the engine life of our haul truck fleet past 28,000 hours. Two years ago it was 22,000 hours. We are now working to extend it even further through a combination of technology and operating initiatives.

Individual sites also have their own initiatives. I will touch on a few.

At our Tom Price operations, the Drill and Blast team found that a few small changes - like changes in the drill bit size and targeting the right ground conditions - reduced the safety risk through improved manoeuvrability. At the same time, this approach reduced drill and blast costs by about 17 per cent, equivalent to $320,000 for 2015.

In another case, after extracting learnings from work done to reduce truck servicing times, our Mobile Equipment Maintenance team replicated these learnings on our Hitachi EX3600 diggers. Reducing the service time from around 18 hours to less than nine hours has increased digger availability by 1.33 per cent.

Even the small things are contributing, like our Robe Valley team saving $22,000 by sourcing replacement gym equipment from camps being decommissioned around the business.

We run the business for cash and focus on margin and long term, sustainable results.

Our cash unit costs are already where others would like to be – and we aren't finished yet.

We optimise the system of mines, rail and ports as a whole and our Operations Centre in Perth is the nerve centre of this system.

This facility brings together controllers and schedulers from pits, plants, rail, ports and utilities for our Pilbara Operations to work together in a control room and adjacent office block in Perth, using technology and co-located expertise to provide whole system visibility, whereby at any time we can see the location of every train, truck and dig unit and the throughput of our ports and plants.

We communicate and monitor in real time to execute daily operating plans; we are able to maximise tonnes through the system and ensure customer quality and shipping parameters are always met.
We are able to respond to opportunities and challenges with the most up-to-date information available, meaning better, smarter, faster decisions at every level.

We also run high value initiatives – 12 week focused projects with big audacious goals with teams of talented employees across all levels of the organisations – to 'pick to pieces' various individual elements of the system to achieve better performance.

Let me give you a couple of examples.

FasTrack 35, one of our high value initiatives in 2015, is an example of the types of improvements we drive. In this case, pit, plant and rail controllers worked hand-in-hand with site operations, scheduling and planning teams, and our sales and marketing teams. FasTrack reduced average rail cycle time from 42 hours to 35 hours across the system by optimising the way we use our rail network with improvements:

- in the way ore is delivered from pit to stockyards;
- The time required and consistency of volume and measure when loading trains;
- average train speed;
- and coordination of trains through yards and dumpers.

These all contributed to minimising wait time for trains and substantially increased the capacity and flexibility of our system.

Another high value initiative was Project Everest. Some of the great achievements from this project were seen at our oldest mine, Tom Price, which saw a step change in production from its previous nameplate capacity of around 28 million tonnes per annum to delivering over 32 million tonnes production in 2015. This was done while delivering outstanding safety performance and slashing costs. Again, this focused on the value chain, this time within the mines.

In 2016, we already have several high value initiatives underway aimed at potential break through improvements- payload gains on haul trucks; Optimised dispatch for load and haul operations; and excellence in shut management.

We are seeing early results from these and others across the system.

We also tackle the value proposition with our product mix.

Our Pilbara Blend products are a great example. Their value is crucial to our business and to our customers, and they are the most recognised iron ore brand products in the Asian Steel industry. Pilbara Blend fines are the most quoted product in the formation of the Platts 62 per cent index, which is often cited as a reference for the iron ore price.

Anecdotally, some of our customers refer to the Pilbara Blend as the USD equivalent in the iron ore industry referring to its reliability and consistency.

What does all this mean?

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It means that by taking a system-wide, focussed approach and engaging people who understand how they contribute value, we maximise our output, minimise waste and promote best practise, enabling us to deliver the quality product that our customers want.

The final point that I'm going to cover in detail today is our focus on deriving full value from the investments we have made in our assets and infrastructure. We adhere to a disciplined capital allocation framework and continually evaluate our portfolio and potential growth options so that we can fully utilise our infrastructure when the time is right to invest.

We completed the Pilbara infrastructure project on time in 2015 with the capital cost for rail and port components coming in below initial estimates.

Our recent brownfields developments are another example of our efficient capital allocation. They helped provide additional tonnes at a very attractive capital intensity of about US$9 per tonne.

The ramp-up of our Nammuldi Incremental Tonnes project is a current focus, as it delivers low phosphorous ore into the Pilbara Blend. Production started in the fourth quarter of 2015 and construction has begun on the second phase. This will take production from 5 to 10 million tonne per annum capacity by Q4 of this year.

This investment in Nammuldi Incremental Tonnes, which takes ore from the Silvergrass deposit, is preparatory for further Silvergrass development. This approach has allowed us to minimise capital intensity of the project by using an established plant, Nammuldi Below Water Table, and leveraging construction resources and engineering and design work to be rolled over from our Nammuldi Below Water Table Plant to enable commencement of some Silvergrass-related initiatives. These include the starting dewatering set-up work, and working to double the capacity of the Nammuldi Below Water Table plant.

You'd be aware of our early and long investment in the suite of Mine of the Future initiatives, through which we are also realising value.

An example of using technology to drive value is our development of RTVis™, a three-dimensional visualisation software that analyses in-ground data.

RTVis™ has led to greater ore recovery through improved boundary identification, more accurate drilling and blasting and reduced costs in explosives. It has also improved waste classification, dig rates and field task planning.

Automation technology is a key element of this strategy, with which you would be familiar, across drills and trucks and we continue to see demonstrated improvements from these advancements.

Our West Angelas site is the only fully autonomous production drill site in the world, with 7 autonomous drills. We have already seen demonstrated productivity improvements, including a greater than 10 per cent Use of Availability through reduction of operational delays and interruptions.

Our autonomous haulage system (AHS) is deployed across 3 sites in the Pilbara and comprises 71 trucks with

- 19 at Hope Downs 4
- 30 at Nammuldi
- 22 at Yandicoogina

Tied in with the other productivity improvements we have made, this technology is game-changing.

In conclusion, the iron ore business Rio Tinto operates today is very different to the one that began more than five decades ago, and I'm sure it will be very different again in another fifty years.

The key to our business is the direct engagement with the people who work for us and keeping them engaged, motivated and informed, whether through high value initiatives, cost rooms, or other activity at work.

It takes smart and committed people to drive change and deliver results, and leaders who provide direction with clarity and purpose. As we pursue value through our strategy, we are showing that we have great capability in both.

This is a great business and our discipline, long term view, Tier 1 assets and people have positioned us to deliver results.

We will continue to transform our business so that it will continue to deliver industry-leading returns through the cycle, focusing on:

- Forever improving safety
- Driving shareholder returns through disciplined cost management
- Improving the productivity of our system
- And delivering value through smart growth and investment decisions.

This is a long distance event, not a sprint. It takes discipline, resiliency and strength.

It is an environment in which Rio Tinto excels.

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