Management's Discussion and Analysis

Our capital expenditures for 2005 are expected to total approximately $180 million, including approximately $19 million for the DOZ expansion and $17 million for other long-term development projects. We expect to fund our 2005 capital expenditures with operating cash flows and available cash. Capital expenditures are estimated to average approximately $145 million per year over the next five years.

In November 2004, a joint venture in which we own a 50 percent interest completed the sale to a real estate developer of a parcel of land in Arizona where the joint venture previously was engaged in a copper mining research project. Our share of net cash proceeds from the sale totaled $21.6 million. In December 2004, Atlantic Copper completed a sale of its wire rod and wire assets and received $18.3 million cash.

In 2001, we sold $603.8 million of 8 1/4% Convertible Senior Notes due 2006. The terms of the notes required that we use $139.8 million of the proceeds to purchase a portfolio of U.S. government securities to secure and pay for the first six semiannual interest payments. We sold $6.7 million of these restricted investments in 2004, $46.6 million in 2003 and $47.9 million in 2002 to pay interest. Conversions of these notes allowed us to sell $15.1 million of our restricted investments during 2004 and $27.0 million during 2003 (see below).

In July 2003, we acquired the 85.7 percent ownership interest in PT Puncakjaya Power owned by affiliates of Duke Energy Corporation for $68.1 million cash, net of $9.9 million of cash acquired. PT Freeport Indonesia purchases power from Puncakjaya Power under infrastructure asset financing arrangements.

Financing Activities

We completed several financing transactions over the last several years to improve our balance sheet and debt maturity profile and enhance our financial flexibility. We are continuing to review opportunities to use a portion of future operating cash flow to reduce debt in advance of scheduled maturities and to further improve our debt maturity profile. In January 2004, we completed a tender offer and privately negotiated transactions for a portion of our remaining 8 1/4% Convertible Senior Notes due 2006 resulting in the early conversion of $226.1 million of notes into 15.8 million shares of FCX common stock. We recorded a $10.9 million charge to losses on early extinguishment and conversion of debt in connection with these conversions. The $10.9 million charge included $6.4 million of previously accrued interest costs, resulting in an equivalent reduction in interest expense. In June 2004, we called for redemption on July 31, 2004, all of the remaining $66.5 million of 8 1/4% Convertible Senior Notes. During July, all remaining notes were converted into 4.7 million shares of FCX common stock. As of July 31, 2004, all of the 8 1/4% Convertible Senior Notes, which totaled $603.8 million at issuance in 2001, had been converted into 42.2 million shares of FCX common stock.

On February 3, 2004, we sold $350 million of 6 7/8% Senior Notes due 2014 for net proceeds of $344.4 million. We used a portion of the proceeds to repay $162.4 million of Atlantic Copper borrowings and to refinance other FCX 2004 debt maturities. Atlantic Copper recorded a $3.7 million charge to losses on early extinguishment of debt to accelerate amortization of deferred financing costs. Interest on the notes is payable semiannually on February 1 and August 1 of each year, beginning August 1, 2004. We may redeem some or all of the notes at our option at a make-whole redemption price prior to February 1, 2009, and afterwards at stated redemption prices. The indenture governing the notes contains certain restrictions, including restrictions on incurring debt, creating liens, selling assets, entering into transactions with affiliates, paying cash dividends on common stock, repurchasing or redeeming common or preferred equity, prepaying subordinated debt and making investments. During the second quarter of 2004, we purchased in the open market $9.7 million of the 6 7/8% Senior Notes for $8.8 million, which resulted in a gain of $0.8 million recorded as a reduction to losses on early extinguishment and conversion of debt, including related deferred financing cost.

On March 30, 2004, we sold 1.1 million shares of 5 1/2% Convertible Perpetual Preferred Stock for $1.1 billion, with net proceeds totaling $1.067 billion. Each share of preferred stock was initially convertible into 18.8019 shares of our common stock, equivalent to a conversion price of approximately $53.19 per common share. The conversion rate is adjustable upon the occurrence of certain events, including any quarter that our common stock dividend exceeds $0.20 per share. As a result of the common stock dividends discussed below and a quarterly dividend paid on February 1, 2005, each share of preferred stock is now convertible into 18.9794 shares of FCX common stock, equivalent to a conversion price of approximately $52.69 per common share. In February 2005, our Board of Directors authorized a supplemental dividend of $0.50 per share payable on March 31, 2005, which will result in another adjustment to the conversion price in March 2005. Beginning March 30, 2009, we may redeem shares of the preferred stock by paying cash, our common stock or any combination thereof for $1,000 per share plus unpaid dividends, but only if our common stock price has exceeded 130 percent of the conversion price for at least 20 trading days within a period of 30 consecutive trading days immediately preceding the notice of redemption. We used a portion of the proceeds from the sale to purchase