

A Macro-view on South African Thermal Coal for the World Export Markets

Introduction

Distinguished guests, ladies and gentlemen, it is a great pleasure to be here today at Coaltrans South Africa 2006.

Today I am going to be talking about three key topics. Firstly I will kick off with a broad macro view of the coal and energy markets and take a look at supply and demand historically and in the future. My second topic is investing for the future in South Africa. And thirdly I will finish off with the opportunities deriving from BEE activities and our ongoing commitment to this area.

Topic 1 Overview of Supply and Demand

Without doubt, the world's appetite for energy is increasing. Last year, global energy consumption grew 4.3% and in volume terms it was the largest ever annual increase in consumption. Quite a remarkable feat, given that the global economy was only running on 3 cylinders. The outlook for further strong growth is positive, with Japan recording 4 straight quarters of growth after more than a decade of stagnant economic performance. The Eurozone has a long way to go but German business confidence is at the highest level for 14 years. In the US we continue to see the economy record solid growth.

Key to the outlook for coal is what is happening with competing fuels. If we look at oil, it sustains its bull run with renewed concerns about security of supply, refining capacity and China's voracious appetite continuing to support high prices. Both pipeline gas and LNG prices have risen significantly in not only Europe but also in Asia and the US. Recent gas supply disruptions from Russia have raised security of supply concerns for some customers. Looking to Uranium, we have seen the spot price more than triple in the last two years. All this is a good macro environment for coal.

On top of all of this we continue to see coal fired power stations being built. China has added 90 GW of capacity in the last two years, several of these are coastal – equivalent to the total UK installed capacity. This requires an additional 200Mtpa of coal. India has announced plans to add 35GW in the next 5 years, many of these also coastal. Plans are in place for further US coal fired power stations and coal is definitely on the agenda in Europe with announcements of new plants or conversions being considered in the Netherlands, Germany and Italy.

Globally, the resurgence in the popularity of coal fired power stations has been driven by security of supply concerns, the relative economics of coal as a fuel and the evident advances in clean coal technology and combustion efficiency.

If the industry and governments can continue to work towards the effective implementation of clean coal technology, you could argue that the future never looked so bright for coal.

Supply

Let me now turn to the coal supply side. There have been significant changes in the pattern of supply of seaborne coal over the last decade. If we look back at 1995 we would see that Australia was the world's largest exporter of thermal coal, followed closely by South Africa. These two countries made up almost 45% of total exports. Following Australia and South Africa came the US, yes the US as the next largest exporter. Smaller players at the time included Indonesia, China, Colombia and Russia.

But a lot has changed since then. Firstly, Indonesian exports have quadrupled and have now surpassed Australia (which almost doubled exports) as the world's largest exporter by volume of thermal coal with around 120Mt exported in 2005. To put this into context, this is more than Australia and South Africa combined exported in 1995. Secondly, China and Colombia have both emerged as major players having tripled exports. Russian export growth has also been impressive having roughly doubled.

In comparison, South African exports have shown very modest growth of 25%.

Clearly missing from the league table is the US which has all but disappeared from the export market.

This leads me to the key lessons that I think we can learn from the supply side.

Firstly, the relative attractiveness of basins will continue to change. Some will come, some will go and the markets that they are best suited to will shift in parallel with freight rates, customer needs and competing basin actions. Secondly for a basin to maintain its relevance in the future will require significant capital investment in mines and infrastructure, a low delivered cost base, support from government and a secure investment environment.

Demand

On the demand side there have been equally interesting developments. In 1995, the imports into the Atlantic markets and Pacific market were roughly even. Over the last decade however

the Pacific market has grown at approximately twice the rate of the Atlantic and the split is now about 60:40 in favour of the Pacific.

During the last decade, Japan has maintained its position as the largest importer, the UK has quadrupled imports and the Americas has gone from a small 6Mtpa importer to a major import destination consuming close to 36Mt. Finally in 1995, neither India or China were importers of thermal coal.

Over the next decade, the markets of India, China and the US are expected to feature strongly. If this growth eventuates it has the potential to alter the coal flows away from the traditional markets of Western Europe and North Asia.

So what does this mean for South Africa? Well firstly, we have some catching up to do on the export side. And that is the next topic I will cover. The second implication is that these future expansions need to be consistent with and match changing trade patterns, customer needs and the global nature of the industry. I will cover this in my third topic when I speak about how we have worked with BEE companies and what we have to offer.

Topic 2: Investing for the future in SA Coal Industry

As many of you may have seen in the press recently, BHP Billiton is progressing the feasibility study of a very significant new investment in our Douglas-Middelburg coal complex. This investment, totalling several hundred million dollars, will ensure the longevity of production from this complex and enhance the long term sustainability of Ingwe's current volumes.

With the underground reserves at Douglas Colliery nearing completion and limited export life at the stand-alone Middelburg mine - both of which are joint ventures with Xstrata - the project aims to maximise export potential from combined Douglas/ Middelburg reserves including pillar reserves at Douglas Colliery. In addition to ensuring a longer export life, it will also satisfy the 10 million tons a year contract that Ingwe has with Eskom until 2034.

The project is still in the feasibility phase, but if given the green light, it would use the lower-strip ratio areas available at Douglas to replace mined-out areas and high-strip ratio areas at Middelburg Mine. It would replace the current operation at Douglas Colliery. A new coal processing facility would replace the current facility and existing opencast equipment would be used to replace the underground mine.

In terms of the industry, I cannot speak on behalf of our competitors but the expansion of Richards Bay Coal Terminal certainly sets the scene for significant growth of the country's already large position as a supplier of thermal coal into the international markets.

There has been a lot of activity around the Richards Bay Coal Terminal, or RBCT. As a major shareholder in the port, Ingwe waived its rights to 3.7 million tonnes of the original planned Phase V expansion of RBCT. This was done to enable new entrants into the port with the proviso that at least 50% of this tonnage would reside with BEE companies.

This has now been superseded by the recent announcement of the revised expansion, now 20 Mtpa, taking the port from 72 to 92Mtpa with preference going to BEE producers.

The expansion from its existing 72 million tonnes per annum (Mtpa) to 92 Mtpa includes the original Phase 5 expansion, which has been underway for some time. The total cost will be approximately R1 billion, and the expansion is expected to be completed by July 2008. The precise phasing of the incremental export tonnage is subject to colliery and rail infrastructure developments and will be determined once the projects that will utilise the increase in terminal capacity have been identified. Initial estimates, however, indicate that the full rail and mine capacity will only be available after 2009.

Key highlights of the expansion are:

- Special provision will be made to encourage a new generation of coal exporters by earmarking up to 4 Mtpa for emerging BEE exporters.
- South Dunes Coal Terminal, which will be a two thirds HDSA controlled company, will take up 6 Mtpa of the expansion.
- 10 Mtpa of the expansion capacity will be opened up for subscription to all (with an emphasis on empowerment) to facilitate the transformation of RBCT, in line with the continuing transformation of South Africa's coal industry under the Mining Charter.

The subscription capacity of 10 Mtpa will be made available through new shareholding or through commercial usage arrangements at internationally competitive rates, as this expansion is in line with the lowest cost coal port expansions globally. This has been made possible by the RBCT shareholders, who are underwriting the expansion and relinquishing their pre-emptive rights to the expansion capacity.

We as shareholders are excited about the expansion and believe it reflects the spirit of transformation in South Africa. The additional tonnage will be mostly allocated to BEE companies and thereby opens up opportunities for BEE coal mining companies who have not previously been able to export coal.

The extra capacity could bring around R6 billion per annum of foreign currency into South Africa and has the potential to earn around R1 billion per annum for Spoornet. Such infrastructure expansion will help to support the government's objective of 6% GDP growth.

The RBCT shareholders have committed themselves to the transformation of the Terminal and are pleased to be part of this process. Existing RBCT shareholders will fund and make available up to 4 Mtpa exclusively to emerging BEE exporters in order to assist small BEE coal mining companies to enter the export market. Further, approximately 85% of goods and services required for the project will be sourced from local suppliers.

Ingwe, and indeed all the shareholders of RBCT, are strong supporters of this initiative. This is really a very significant development in delivering transformation through the entire value chain associated with export coal. It's fair to say that transformation of the port has been a hot topic over the last few years and the latest developments are indicative of the commitment of the current owners and users to this process.

Topic 3 BEE Opportunities and Commitment

I think it's fair to say that Billiton and later BHP Billiton have for a long time understood the need to uplift and empower previously disadvantaged individuals in South Africa. To this end the organization has been progressive and pro-active rather than simply allowing legislation to dictate the pace of transformation. To us, it's a business objective that makes business sense.

Over 250 million tonnes of saleable coal reserves have been transferred to BEE companies over the last 7 years. I think you will agree, Ladies and Gentlemen that by any measure, that is a significant number....

Without a doubt, the transaction that springs to mind was the creation of Eyesizwe Coal. This groundbreaking deal, co-engineered with Anglo Coal which was conceptualized as far back as 1998 and after much work and negotiation, the first major black controlled and managed coal group was created in late 2000.

Part of the success of the company has a lot to do with the unique mix of assets that was put together to form the core of Eyesizwe. The stability of the Eskom cost-plus operations allowed a significant amount of financing to be injected into the company, whilst a fledgling export business was boosted by the inclusion of extensive export quality reserves and ownership in Richards Bay Coal Terminal .

But good assets are only part of a story. The management team at Eyesizwe, ably led by Mr. Siphonkosi, has established an excellent track record. Eyesizwe's central involvement in the recently announced Kumba transaction is the result of these efforts.

Ingwe, as an ongoing minority shareholder, has supported and mentored Eyesizwe through its growth from a young company into what will be the controlling shareholder of the largest listed BEE company on the JSE. And of course, we'll continue to be supportive of the growth of NewKumba in the future.

Whilst Eyesizwe certainly was a flagship transaction for us, Ingwe has continued to execute BEE transactions, albeit on a smaller scale, over the last few years.

In 1998, Ingwe facilitated the start-up of a small colliery headed by Ayanda Bam to be later known as Kuyasa Mining. This was given added impetus in 2002 with the sale of the Delmas underground mine and associated infrastructure including a washing plant to Kuyasa. It was a mature operation at the time of selling but the structure of the deal has allowed the new owners to extract value and grow the business and establish a good track record.

Endulwini Resources has also been a company with which Ingwe has had a strong relationship. Over a period of 6 years, Ingwe has sold approximately 33Mt of reserves to Black Wattle Colliery (51% owned by Endulwini resources) to expand and extend their initial operations. The most recent sale was clearly the most significant being that of the Pegasus reserve of approximately 12Mt of high quality export coal. This demonstrated Endulwini's success in building a sustainable business and Ingwe's desire to see the momentum being maintained

More recently, in 2005, Ingwe completed the sale of Zululand Anthracite Colliery (more commonly known as ZAC) to a consortium comprising of Australian junior miner Riversdale Holdings and a 26% BEE grouping. The deal was an excellent outcome for all involved.

The mine life is likely to be significantly enhanced in the hands of new owners through the exploitation of small pockets of reserves that would otherwise have been difficult for Ingwe to

exploit. The broad-based HDSA grouping is exceptionally representative of the community in which the mine operates. One has to bear in mind that ZAC is the major employer and provider in the area, so ongoing sustainability is just as important as beneficial ownership and the potential to extend the mine life has met with lots of support from the community.

Finally, Ingwe has been involved in numerous Reserve / resource transactions over the last 12 months: these have not really been publicised but we do believe them to be innovative and interesting for the following reasons:

Firstly: attractive resource positions that have been sold in their entirety to BEE controlled companies on favourable commercial terms

And secondly: on a number of these transactions, coal buy-back arrangements for a large portion of the saleable coal have been already entered into ; this provides a significant financing opportunity for a new player on the back of strong counter-party creditworthiness and allows them to raise finance more efficiently to start up the operations

In the last year we have executed 11 of these deals with a further 4 in the final stages of being negotiated.

Pillar 2: Future

So what does the future hold for Ingwe's remaining empowerment aspirations? I suppose that this is what everyone wants to hear today! However, at this point I will defer to our CEO, Chip Goodyear who is fond of saying, "we make many things in BHP Billiton, but crystal balls are not one of them!"

Ingwe is well on its way to meeting the charter requirements of 26% beneficial ownership through the use of credits from its historical transactions and a strategy is in place to achieve ultimate compliance. But our approach is to aim higher than the minimum legal requirements.

As a dynamic organization, Ingwe continually reviews its portfolio, which gives the organization the potential for opportunities to advance HDSA involvement particularly through ownership transfer. I think many of you are aware that we are currently exploring the divestment of our Koorfontein mine. This is a significant operation currently producing in excess of 3Mtpa of export quality coal with access to significant further resources. The associated infrastructure will also have significant value, particularly for a new entrant into the industry. In addition, 1.5

Mtpa of RBCT throughput capacity will also form part of the transaction. There is a strong desire on the part of Ingwe to favour bids with at least a 51% empowerment component.

Expressions of interest have recently been received and at some point this year we hope to be able to make an announcement in this regard.

We also use an approach of giving people control of their own destiny but with tacit support from the organization. Resource deals with innovative payment structures and associated coal buy-back arrangements are an excellent example of this.

We do not have a formula for the future. This is an exciting environment which is evolving and growing ever more sophisticated every day – Ingwe will adapt and adopt the most appropriate way to deliver in this environment that is both beneficial to our shareholders and the stakeholders of this country.

Pillar 3: “Majors” assisting emerging BEE producers

So how can the SA coal majors, for want of a better term, assist emerging BEE coal producers and those associated with the coal industry? This is the 3rd area I would like to touch on. Ingwe can and does play a role in BEE development with a particular focus on the procurement, logistics and marketing pipelines.

We believe in the broadest-based grass roots empowerment of communities. This involves encouraging the growth of an entrepreneurial economy through medium enterprise development and procuring from BEE suppliers who support our value chain. It's important to note that this does not involve a compromise on quality or service. One of the results of this focus is the establishment of a BEE support centre in Witbank to foster BEE procurement development. For the 2005 financial year, BHPB's BEE procurement spend was over R1.6bn out of a total of approximately R6.5bn.

BHP Billiton is one of the largest traders of physical coal in the world and the organization has a large global team which is continually looking for new markets and better ways to serve our customers. Equity coal only makes up a portion of this supply and as such, we continually look for opportunities to enhance our marketing efforts and provide operational flexibility to our operations.

As I mentioned before, Ingwe has entered a number of asset / resource sales with committed buyback arrangements; however, we will continue to look at coal-buyins, both on a short term

and long term basis from existing producers and from those who are seeking to start new operations.

The scale of Ingwe production means there is always an opportunity to trade in some third party coal to provide flexibility to our own operations in terms of their target production versus stretch production targets.

Ingwe is sometimes accused of being “short” of coal since it is continually in the market looking at buy-in deals. But this is not the case: Indeed, buying in 500,000 tons in a year amounts to less than 2% of Ingwe’s capacity to export coal. I think you will agreed that this a rounding error in any ones terms....! However, this flexibility is important to an organization such as ourselves.

Ingwe and BHPB wants to assist small BEE producers through its logistics and marketing strength. We believe there a number of opportunities such as driving further efficiencies in the logistics chain, providing global marketing support for those producers who do not wish to bear this burden and partnering with BEE producers on commercially attractive opportunities.

Conclusion

In concluding I would like to say that the broad macro environment is positive for coal. Competing fuel prices are high and coals advantages as a stable, secure, reliable and cost competitive fuel is leading to more coal fired power stations being built than most people would have imagined 5 years ago. Over the last decade, the relative performance of the different basins around the world has changed and South Africa needs a pro-investment climate to keep up.

Ingwe and BHP Billiton recognize that beneficial ownership is only one aspect of a charter that has 9 pillars of transformation embodied in it. Rest assured that a lot of time and energy is spent addressing all nine of those pillars to ensure a composite and balanced approach.

Ingwe and BHPB will continue to drive transformation at every level and we look forward to the day when reference to BEE companies or “White” companies will not be the norm but the exception and our industry will rather be made up of South African companies, managed by South Africans, employing South Africans and benefiting South Africans.

