What Do Investors Want From a Gold Mining Stock?

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by

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Good Morning Ladies and Gentlemen.

When I was invited to talk to you here today the organisers told me that I can talk about any subject under the sun, except about my own company.

I therefore decided not to talk about Gold Fields Limited - not to tell you that Gold Fields is one of the most innovative gold mining companies, with the most exciting project pipeline, and one of the best cash producing and dividend paying pedigrees in the industry.

The topic that I want to focus on today is actually something that, surprisingly, many of us have not given much thought to over the past few years. And that is what do investors want from a gold stock?

In coming to the views that I am sharing with you today I’ve personally spoken to 72 investors in one-on-one sessions so far this year. And they’re not necessarily investors in Gold Fields today, but they are large funds that tend to show the way. My views also incorporate a number of other independent interviews and surveys conducted on my behalf with several leading gold investors, as well as a recent JP Morgan survey of over 200 investment funds from around the world.
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What is going on in the gold sector?

Well, let’s try and answer this question. I remember when we launched this product via the World Gold Council.

When we introduced the inaugural product, the so-called GLD, which now makes up about 60% to 70% of the total holdings in gold ETF’s, we set ourselves some targets. We thought that if over a 5 to 10 year period we could get sales of 500 tonnes, that would be a home run.

As you can see we’ve hit that and gone way beyond it. In fact, there are currently 12 gold ETFs available to investors, with a further 8 similar products. These funds have a total combined market value of ~US$120 billion and hold a massive 2,500 tonnes.

The good news: ETFs have made it easy to invest in gold and have brought many new investors into the gold fold. ETF’s have exceeded all expectation and that must be good for gold.

However, there is also a downside for stocks: 1) investors have often bought ETFs instead of stocks and 2) ETFs have contributed to a widening gap between the gold price and stock performance. For gold stocks, ETFs are a double-edged sword.

Obviously the simple way for people to get into gold is just go and buy the ETF. It’s simple to understand and you don’t have to worry about stock selection etc.
The ETF craze has been given further impetus as the investor universe in gold stocks has changed. Ten years ago we used to have more professional gold investors. Today we have generalist investors and emerging market investors who want to get gold into their portfolio. What’s the easiest way to get in? Just get the ETF.

Now, I don’t think we can blame all of the ills of the gold sector on ETFs because the total gold market capitalisation is about $400 billion, which is still significantly more than the combined ETF market value of about US$120 billion.

But you can see from recent trade volumes that there has been a pronounced move into ETFs rather than into major gold equities. It has cannibalised some investment away from the gold stocks.

The challenge now for gold stocks is how to provide investors with leverage over the gold price and to attract some of the incremental investment into gold equities.
Why do people want to buy gold stocks?

They want to get leverage to the gold price.

They want to see that, with a rising gold price, there is more than a one-to-one relationship between the gold price and earnings.

And effectively they want us as managers to optimise our assets and make sure that we give superior returns. I don’t think this information should surprise anyone in this room.
There are two types of companies that you can really look at to determine what measures investors are looking for. If you are running a single asset mining company, the metrics are growth in production volumes, margin expansion and capital optimisation. In other words, you want to keep showing that you can increase the return on the mine and that you can increase the cash flow available for shareholders at a particular gold price.

Now, if you’re a large publicly listed company with a portfolio of mining assets, what else would you do? You’d look to leverage the balance sheet and make sure that you can enhance your returns by borrowing money and gearing up the equity returns that you get as a consequence. I think that’s common cause.

Dividends. Are dividends important? Some people say they aren’t. JP Morgan just did a survey which they put out just before I left to come here – their poll of investors indicates that about 40% of them say dividends are important and about 40% say that reinvesting cash flows to give superior returns is important.

In my mind, if you look at the poor performance of gold stocks over the past ten years it is important that we offer a high dividend yield. It not only helps to differentiate us, but it demonstrates discipline. Investors want to see that if you get all of these things right, and you get a nice gold price kick, then you get a multiplier effect like we used to see in the gold sector some years ago. That's what investors are looking for.
As you all know the gold price over the past few years has risen strongly and maintained these strong levels of late. Five years few of us would have predicted current price levels.

This makes the performance of gold equities so disappointing. We have significantly underperformed the gold price.

Often when I go into investor meetings, this graph gets pulled out and I get asked: “What’s going on?”
…so how has the industry performed against the key criteria?

- Grow production volume
- Provide balance sheet leverage with debt
- Expand margins
- Return free cashflow through dividends
- Optimise capital
- Enjoy positive ‘rating multiplier’ effect

To get to the bottom of this let’s look at how the industry has performed against these key measures over the last decade?
Gold production. If you look at the eight majors (listed on the slide), we make up just over a third (35%) of the industry’s current production of about 60 million to 70 million ounces.

I’ve been going to investor conferences over my last 15 years at Gold Fields and there’s one consistent theme in the presentations of all of the large gold producers, including us - that production is going to the moon.

But if we had actually met all our production promises over the last five years then we would not have dropped output on a compound annual basis by 2% between 2006 and 2011.

Even though the gold industry as a whole has gone up somewhat - by 3% p.a. over this period - it’s not come from the major producers. Other producers have instead increased production by 6% p.a. since 2006 though most of this growth has come since 2008.

These trends are also evident in a geographic breakdown of production, which has dropped in all of the more mature markets such as South Africa, Australia, Peru and the USA, where annual production declined by ~5.3Moz since 2006. Emerging markets, notably China, Mexico, Russia and Colombia, have added a combined ~7.6Moz of additional production since 2006.
So the growth in production hasn’t come from the go-to stocks used by investors when they want to allocate some funds to the gold space. We’ve got to ask ourselves why not when the gold price has increased by 21% p.a. over those five years.

A lot of it comes down to the fact that Gold is becoming scarce.

It’s not so easy to find gold any more. Certainly from an exploration perspective we know how difficult it is to find new deposits.

Central banks, as you will see later, are buying, not selling. ETFs are increasing. Demand is increasing. But supply isn’t keeping pace.

There’s one more issue - back in the days when the gold price was $200, $300, $400 an ounce - the average grade that was being mined was often higher than the average grade of our reserves. But that is no longer the case and as a result we haven’t really grown production volumes. In fact, we’ve gone the other way.

That is why I believe investors are right to be sceptical of claims that over the next five years production growth will average 6% per annum. It is likely that at best the industry – in particular the majors - will merely maintain output.

The key message here is that gold miners have not met their production promises and investors have become sceptical. This has in recent months led to a change in rhetoric from miners. Cash is now king, not growth, and we’re reining in spending. This raises two questions. Is this just rhetoric? And, what will the resultant gold scarcity mean for future gold prices?
Expanding margins. How have the majors done in terms of EBITDA margins - which is effectively operating profit? Well, over the period from 2002 to 2011 – you can see the impact.

If you measure the compound growth in EBITDA between 2006 and 2011, the eight companies have achieved growth of only 8% against an annual increase in the gold price of 21%.

It’s obvious that we haven’t delivered the leverage.

Margins are up, but nowhere near the rise in the gold price over the same time frame.
Let’s try and explore why.

Operating costs are increasing. Paulson & Co told me last year that historically they felt cost inflation had been around 10% per annum. What I thought was scary is that they were predicting – and this is just on a cost per ton basis – that cost inflation was probably going to be 15% per annum going forward. This means you’re going to see a doubling of costs over five years.

Why is that the case? It’s skills shortages. It’s the cost of consumables. It’s energy costs. The gold price, I’m afraid, doesn’t go up by itself. Everything else moves with it. The oil price goes up. The steel price goes up. Cement goes up. Wages go up. So we’re not as levered to the gold price as we think we are. That’s one of the revelations that maybe wasn’t as well understood five to ten years ago, as it is today.

Of late a lot of the large mining companies have warned that cash costs are going to be 20% higher next year. How is that possible? It’s the combined effect of all of these issues I mentioned. Cost inflation is increasing, and it is escalating even more today because of the rapidly rising social responsibility costs that the industry is attracting.

The other issue that the industry has to confront is that our grade has declined over time. Average yields amongst the major producers have dropped by 5% per annum over the last five years. Some of this decline will have been driven by a gradual decline in the quality of ore-bodies, a trend that can be seen in long-term exploration discoveries:

Over the last 30 years, ore grades from global primary gold discoveries greater than 1Moz have declined by ~3% per annum. This trend has continued more recently, with grades falling by 4% per annum from 1998 to 2008. As these discoveries come through to production, we’re likely to see further downward pressure on average yields.
How have we done as an industry in terms of optimising our capital? Here’s another interesting comparison. Over last ten years, on a compound annual growth basis, the gold price has risen by 20% per annum.

The industry’s capital expenditure on a per ounce basis, however, has gone up by 32% per ounce per annum over the same period. Growth in capital expenditure per ounce has been driven more by greenfield development capex, which on its own has gone up by an estimated 50% per annum from 2006 to 2011.

And then on top of that M&A spend has gone up 17% per annum on a $/oz basis over the past 10 years. And of course M&A hasn’t grown the production base, as you saw earlier. What it has done is actually replace production that has been falling off. So we’re spending more to stand still.

If you look at the combined effect of all of that, it means that we’ve got to mine more tonnes of ore at a lower grade to get the same gold and, combined with rising cost inflation, it is costing us more on a per ounce basis to actually sustain and build new operations.
If you combine the effect of the increases in operating costs, the decline in grades, the increase in capital expenditure – as depicted by the Notional Cash Expenditure (NCE) you can see on this chart—we have in fact not created much leverage at all.

Compared with the explosion in the gold price over the same period the assumption most people would make is that the industry’s all-in-costs - represented by NCE - shouldn’t have escalated anywhere near the same extent. In fact we’ve had a 16% annual increase in our total costs. As I said to you earlier, in five years that means costs have doubled. We’ve lost a lot of the upside!

Just a brief word on NCE. At investor conferences the industry often extolls its cash cost performance – that we are making significant operating cash flow margins - sometimes in excess of $1,000 an ounce.

Who are we trying to kid? We don’t kid the investors because they know how much cash we really generate after everything is accounted for. The sell-side also understands this.

The only people we’re kidding are governments and communities who, not surprisingly, say okay, you’re making super profits, please pay up. And before we know it we have windfall taxes, higher royalties and so on.

We’ve got to change the lens through which we and the world view this industry, and start talking about what it really costs to produce an ounce of gold. I don’t care if we call it NCE or something else, but to talk about cash costs only is not telling the full story.

It is like scoring an own goal every time you play, and being proud of it!
What has happened to capital expenditure? If you take the average market cap of the eight large gold companies and you look at their spending over the last five years in relation to that market cap, we’ve invested 40% of our market cap. That’s more than what we did the previous five years. And if you look at communicated investment plans for the next five years, it’s going up even further.

Good work done by the World Gold Council shows that if we implement all of the projects that have been announced in the gold industry over the next ten years, the gold industry will probably have to spend its market cap again - in other words $400 billion would have to be spent to bring these projects into production. It is estimated that as much as 60% of market value may have to be spent over the next six years to progress all of the projects currently on the table.

What’s concerning is that these projects aren’t all going to be growth, because the base is declining. We know that we’re mining finite resources. A lot of that is going to be replacement. So we’re dealing with a situation where, in order for us to sustain this industry at somewhere around 70 million to 80 million ounces a year, it is going to cost a lot of money over the next ten years.

Having said that, investors are fed up with promises of jam tomorrow and they are sending the message to the industry. And we are starting to wake up to what investors want.

Most recently, and in line with the broader mining industry, gold CEOs are indicating a much greater emphasis on capital spend discipline. Gold miners are beginning to walk the talk of reining in capital spend, and focusing more on returns than on growth. We can expect announced plans to be trimmed. But this will in turn impact on future production growth in an already flat production environment.

But the jury is still out and, not surprising, investors are cynical.
Let’s look at some of the financial issues confronting the industry.

The one depicted here, in particular, is difficult: provide balance sheet leverage with debt. Historically the gold industry has turned to equity deals to finance major expansions. We’re not really leveraging a lot of the balance sheet with debt. So you might argue in some cases we haven’t leveraged enough.

Having said that, a lot of the balance sheets have been put under pressure by gold hedges that have had to be retired as well as extra funding that has been needed for overruns on projects.

But certainly if we’re going to follow a classic model of leveraged returns, it’s something that we haven’t necessarily optimised in the gold industry and should consider more in future.

The long-term debt markets are attractive, but this won’t last forever.
Dividend yields continue to underperform in a ‘yield-hungry’ environment. So what has happened to the gold sector? We’ve lagged. The mining sector overall has picked up recently, but the gold sector has not done so.

Historically we’ve felt that this was ok because gold is money. You buy gold stocks you buy money. But people aren’t looking at gold counters in the same way anymore and the so-called gold premium isn’t as attractive as it used to be. So we’re not paying dividends that are competitive in comparison with other mining sectors.

I’ve been asked by some investors why can’t we pay out a dividend yield of 5% to 10%? If we really want to get our stock up we’ve got to push dividend yields into those territories. But we simply can’t do that, because then we will be paying out all our earnings. We won’t have anything left for sustaining capital or maintaining our current production base.

But investors are hungry for a dividend yield, so they’re not particularly enthralled by this argument. Having said that, Gold Fields is ahead in the gold sector at the moment. We are paying out an average dividend yield of about 3.8%. The rest of the peer group is at an average of about 1.8%.

Why don’t we get credit for it? Because investors don’t believe we can repeat that performance. Paying out one good year of dividends is not enough. You’ve got to repeat that performance again and again to be believed in a world that is becoming incredibly cynical.
The positive rating multiplier effect is also not a good news story. The gold industry used to trade at a premium to other sectors. We’ve actually come back to the S&P 500 and diversified miners have closed the gap, though we’re still trading at a premium to base metal miners.

The gold premium is still a very important consideration, but the gap has narrowed. So we haven’t been able to get the re-rating. We’ve been punished in part because of some of the issues I’ve just talked about. Investors have reacted through the ratings.
...driven by years of over-promising and under-delivering

Guidance. Over-promising and under-delivering. If you go back over time 40% of us have not been able to achieve our goals within a tolerance level of 5%.

This is critical as more and more investors are investing, first and foremost, in management. It’s not enough to have great ore bodies. It’s a question of “can you guys execute? Can you take the latent potential that exists in your company and translate that into bottom-line delivery?”

Management credibility for the industry is a big issue and we don’t do ourselves any favours by not meeting our guidance. I’m seeing the even in the senior peer group more companies are now starting to revise their guidance, and that includes us. It’s a black eye for the industry.

The other thing with the industry is that if one of us gets it wrong, investors retreat from the sector as a whole. When one of the large companies gives bad news, the generalist fund managers who don’t analyse companies to the nth degree, often take that as a sell signal for the entire sector.

They’ve get a sectoral view on what they should do. So we shouldn’t think if somebody gets it wrong, we’re going to be unscathed. They think it’s our turn next. And often it is.
Recap: how has the industry performed?

- Grow production volume
- Expand margins
- Optimise capital
- Provide balance sheet leverage with debt
- Return free cashflow through dividends
- Enjoy positive ‘rating multiplier’ effect

So, I’m afraid to tell you, and if we’re really brutally honest with ourselves, the industry has not done terribly well on any of the six key metrics over the past decade.
So what does the future hold?

So the question is, what’s the model for the industry going to be in the future and which road are we going to take?
First of all, let’s talk about our product. If we don’t have a product that is attractive then a lot of our decisions would be easier. But our product is attractive and gold’s fundamentals remain strong. ETFs continue to increase. We’ve gone way beyond the 500 tonnes dream and there is no reason to believe that demand will wane significantly.

Furthermore, even at current investment levels, investment in gold is very low. It’s only 1% of global assets under management. Surely there is potential for this to increase.

The doomsday prophets will say that the gold price has run too far, that it is a bubble and it is all going to end in tears. But more and more people are putting their money into gold because they know that the world economy is not in great shape, and it is not going to get better in a hurry.

Investors are recognising gold’s role as a safe haven and there are no signs that this will change fundamentally any time soon.
Demand. China and India have doubled their demand of gold in five years from 25% of the total to around 50% now. These are the only two large economies in the world which have reported meaningful growth of late and which accounted for 35% of global GDP growth last year. Admittedly their growth has slowed, but growth projections for 2012 are somewhere between 8% for China and 7% for India – a lot better than any of the other large economies.

Those two countries have a strong affinity towards gold. And even though India has come off it a bit recently, it is still a strong cultural issue in that country and gold off-take should increase again in future. So I believe that demand is reasonably solid and should remain so, provided the two principal drivers, China and India, continue to grow into the future, which looks likely.
Central bank buying has been a strong feature of the market over the past five years.

Central banks are strange animals. They tend to sell when the price goes down and they buy when it goes up. So if gold keeps going up they will probably keep buying. In this way incremental demand is self-generating.

China is sitting with a massive over-exposure to US Dollars and they’re looking for ways to diversify. They don’t want to buy gold in the open market, because they don’t want to signal panic buying. They want to keep a nice balance between the US dollar and the gold price. So they’re absorbing all the production in their country but, even though China is now the world’s largest gold producer, on its own this is not enough to satisfy the state’s demand.
Production. Primary gold production has not gone up anywhere near demand growth. On a classic supply-demand fundamental ratio, with gold rising five or six times over eight or nine years, you would have thought there’d be a lot more gold coming to the market. But it’s just not that easy to find any more, as I have said earlier.

So what has been the filler? All sorts of people selling their jewellery. There are gold merchants going around trying to buy your old jewellery. Obviously they want to make money so they’re not going to pay what it’s really worth. How much of this can still keep coming to market?

Based on analysis by the World Gold Council, we’re going to need to see higher prices for more of those sales to materialise. So if it wasn’t for people selling their jewellery and merchants buying it the gold industry would already be in massive deficit.
We have talked about the fundamentals and they do support a higher gold price. Here’s what is interesting. If you look at the forecast gold prices over the last seven years, against the actual price, it’s a telling picture. The analysts, who keep telling us the gold price is going down, have been wrong seven years out of seven. That’s a remarkable track record!

And despite that, they’re still telling us that gold is going down again! The CIBC long-term consensus forecast is US$1,214 per ounce!

Now, the big eight companies’ all-in cost (on an NCE basis) today – based on the March 2012 quarter - was US$1,380 per ounce of gold produced. Based on that, and if we believe the CIBC long-term consensus forecast of US$1,214 per ounce, we don’t have an industry.

So, if all of this is true, what we should be doing is to stop all of our capital investment now, and to harvest and get as much as we can in the next two or three years, before the doomsday scenario hits us.

If you look at futures prices – this graph is based on futures curves built on Bloomberg data for contracts that expire at year-ends in 2012, 2013, 2014 and 2015 - what can you expect?

The way the analysts see it, the gold price is going down. It’s going to be up in the short term but it’s going to be down in the long term. Judging from their past 7-year track record, you draw your own conclusions.
What do investors want us to do?

We need to believe in our product. If we’re going to sustain this business into the future and if we’re going to drive long-term returns, we’ve got to believe in the gold price. Don’t bet against the gold price. Obviously we shouldn’t be using ridiculous prices, but we shouldn’t call it down too low.

Investors interested in gold stocks believe in our product and they want us to do so as well! Stay focussed on gold. That is the strong message coming back consistently over the last three years.

And stay focussed on gold as there is still a gold premium. On a fundamental, absolute value basis there is not a gold premium right now because the senior peer group are trading at about 0.85 to NAV compared to 1.5 to 2 times a few years. But against base metals there is still a good premium.

If we acquire pure base metals assets, we will dilute our relative premium. Investors do not want us to do this. They can do it themselves without paying an acquisition premium. Having a base metals component from gold assets is fine, but there’s no place in a gold miner’s portfolio for pure copper assets.

Hedging. I will guarantee you that hedging is going to come back into vogue. It will be a mistake and we shouldn’t do it. In the long run you can’t beat spot. Empirical data supports this view. You may get it right in certain peaks and troughs, but you will give it all back over time.

How much has been spent on repairing balance sheets? Possibly as much as $30 billion in retiring underwater hedges. I’m afraid to tell you, hedging is coming back. It’s a silly thing to do. Remain unhedged – investors can hedge for themselves.
Focus on cash flow. At the end of the day why are we here? We are here to generate shareholder returns. Everything we do has got to be measured against shareholder returns. If it doesn’t meet those criteria we have to ask ourselves whether it makes sense at all.

Now, you’ve almost got to take a private equity style approach to managing the business. Private equity is very, very tough on allocation of capital investments. They want short payback periods. They want to see robust returns with conservative technical parameters. And you’ve almost got to take a big company like us, or this industry, and say let’s change the way we run this business, as if this is our own money. Every dollar we spend is absolutely critical.

I’m not saying we’re not doing it, but the sector overall probably needs to do more of it. And it’s not about asset stripping. It’s about optimising how we run our mines, sweating our assets. It’s about optimising every Dollar we spend and maximising our ore flow and our grade.

Cash and cash returns. Making sure we do get our money back. That will demonstrate to investors that we have the right to spend more money.
So what does this mean for the industry?

We’ve got to get back to really looking at KPIs that measure whether we actually make money or we don’t. And it is not about ounces in the ground. It’s not about production. It’s not about reserves. It means focusing instead on metrics such as free cash flow per share.

That’s a mind shift for us, because everyone in the industry is terrified that their production is going to go down. What am I going to tell my investors? How can I tell them that my production is going to decline?

Many investors still focus heavily on production. They say, we’re going to look at your production, we’re going to look at your costs, and we’ll figure out what the gold price is. But it shouldn’t be ounces for ounces’ sake. It should be ounces that make money. Fewer ounces that make more money are surely a better option?
We as an industry need to get a much better grip on so-called growth and sustaining capital to demonstrate the true value of our investments – unfocused sustaining capital spend can destroy a company’s ability to provide investors with leverage over the gold price.

As I explained earlier, we at Gold Fields have reported for some time on a total cost basis – we call this Notional Cash Expenditure (NCE) - which captures both the operating costs and capital costs of running a mine. NCE tells it like it is. And if we can get the industry to tell it like it is, it might solve a lot of our problems linked resource nationalism. Governments are seeking to impose significantly higher taxes on us because they think we’re making super profits - the opposite is true.

We are now taking NCE a step further to seek greater transparency on the returns generated by capital spend, which historically has simply been considered essential to sustain mine operations - and to ensure that effective capital discipline is applied.

Focus on the all-in cost of producing an ounce of gold. Don’t get mixed up in the debate on what is sustaining, replacement or growth capital. It’s all going to end up in the same bucket because, at the end of the day, what has the industry done over five years? The top eight companies have not grown. All capital is sustaining capital. That is the reality of our business today.
The industry needs to look at all of the options and not just the marginal ounce that gets you over the line.

The investment case has got to stand on its own two feet, based on the hard technical information that we have in front of us.

The key point here is to be bullish on the gold price….but not to allow this to justify going after more ounces that are not economical. These additional marginal ounces will not necessarily provide investors with the leverage to the gold price they seek. The risk is that chasing marginal ounces encourages mine teams to increase production or extend lives of mines, rather than optimise cash returns.

Consider a project where the known ore body is attractive, but too small to carry the costs of the required processing plants. The project feasibility team recognise the project return and payback is marginal, but justify a decision to proceed on the basis of the unquantified “option value” of the unexplored ore body in the vicinity of known resources. This can be dangerous.

Key point: ensure that the project feasibility considers all commercial options, not just the preferred technical solution that barely clears the investment hurdle.
What investors want

1. Believe in our product
   • Manage portfolio for cash returns and investment payback
   • Translate cash returns into production guidance (and not vice versa)
   • Ensure guidance is realistic and transparent regarding likely impact of gold price movements
   • Ultimately, delivery remains paramount

2. Focus on cashflow

3. Deliver on relevant promises

This industry is suffering from a management credibility discount. I’m not sure what that discount is, but it is high because we don’t deliver on our promises.

Execution is everything. We can have great assets, we can have great ore bodies, but if we can’t execute on our promises there is a massive discount.

We need to focus on metrics that we can control and not lose sight of cash returns. We must give realistic production and cost guidance, supported by underlying information that is credible.
Earn the right to spend money.

If we want to go and spend a whole lot of money on growing this company, let’s make sure we do it off a solid platform.

How are people going to believe that the industry should go and spend another $200 billion or $300 billion, when we have not been able to manage their money as optimally as we should have on our existing assets?

It’s a fair question, I have to say. So we have to earn the right to spend money. Show that we’re actually using investors money wisely.
A gold price of ~$2,000/oz by 2015 will provide gold majors with a realistic chance to deliver leveraged returns.

This chart shows the average expected annual shareholder return for the major gold producers from 2011-2015, assuming that the gold price increases to $2,000/oz by 2015.

On the left you can see that the average returns will just exceed the growth in gold price if average valuation multiples remain as they were in 2011 – which using EV/EBITDA was about 8x EBITDA across the Top 8 gold majors.

So, if we believe in a gold price of $2,000 by 2015 and if we believe that cost inflation will continue at 10%, what sort of returns are we going to get by 2015?

On our current multiples as an industry we have a reasonable opportunity to make returns on the investment that is in line with an appreciation of the gold price. At that level – assuming we have the cost disciplines in place I talked about earlier - we have a chance for the first time in five years to demonstrate that we can offer leverage to the gold price. Matching the gold price would represent a major turnaround.

If we can achieve that an improvement in our ratings should follow. And at a 25% increase in our rating – by rating here we’re talking principally about enterprise value divided by EBITDA – we can deliver considerable high leverage vs the gold price, with average returns of ~15% vs gold price growth of ~7% p.a. This should make more investors sit up and take notice.
But, if the gold price remains similar to today’s price, we’re not going to see any leverage against the gold price, unless cost inflation can be dramatically reduced, which - given current price trends - will not happen.

If you are going to invest in gold stocks, you need to believe in a gold price of at least $2000/oz in the short term. And you have got to believe that the industry will be able to deliver the gold price in higher returns for shareholders and that management can actually do that. Deliver their growth projects and deliver on their promises.

So, managers and directors – don’t bet against your investors – they believe in gold. They expect the gold price to remain robust – but they demand that you provide them with a decent return at that higher price.

Thank you for your attention.