Q2 2014 Results
Conference call transcript
Nick Holland – CEO

Good afternoon ladies and gentlemen, or good morning depending on where you are in the world today. Thank you for joining us today to discuss Gold Fields’ results for the second quarter of 2014. On the call with me today are Paul Schmidt, our Chief Financial Officer, Willie Jacobsz, our Head of Investor Relations, and Taryn Harmse, our General Counsel.

I am pleased to report that our continued focus on improving execution and delivery at all the mines within our portfolio, as well as on better margins and generating free cash flow, has achieved appreciable success during the quarter.

As we have previously shared with you, all activities undertaken in the Group and at our operations are singularly focussed on the objective of generating a sustainable free cash flow margin of at least 15% at a $1,300 gold price. However, as we have also said previously, this has to happen without compromising the long-term sustainability of our ore bodies through a lack of investment in ore reserve development and stripping, or through high grading. Otherwise we will impact the integrity of our operations.

During the quarter, Gold Fields exceeded this 15% target for the first time by achieving a free cash flow margin of 18% compared with 13% in the March quarter. To achieve this, the Group recorded an all-in sustaining cost of $1,050 per ounce and all-in cost of $1,093 per ounce, from attributable gold production of 548,000 ounces.

Compared with the same quarter a year ago, the Group’s all-in sustaining costs improved by 26% from $1,416 per ounce to $1,050 per ounce and the all-in cost, which includes everything, improved by 30% from $1,572 per ounce to $1,093 per ounce, a fundamental change in our cost base as I’m sure you’ll agree.

Over the same period, however, attributable gold production increased by 22% from 451,000 ounces to 548,000 ounces, reflecting the October 2013 acquisition of the Yilgarn South assets in Australia. So effectively we’ve been able to bring our cost base down 30% whilst at the same time increasing our production base by 22%. That’s a nice story to put together.

Notably, if the South Deep project, which is not at commercial levels of production, is excluded from the June quarter results, then the group’s all-in costs were just over $1,000 an ounce, at $1,030, and the group’s free cash flow margin approximately 23%, which demonstrates the robustness of the international assets in our portfolio.

Despite a 1% decline in the realised gold price and a 2% decline in gold production against the March quarter, cash flow from operating activities, after taking account of capital expenditure, environmental payments, debt service etc. improved by 20% from $54 million to $65 million this quarter. That $65 million is after all expenditures. So it really is what we’ve put in the bank account at the end of the quarter.

Notwithstanding a 7% decline in the gold price, from $1,372 per ounce in the June 2013 quarter to $1,275 per ounce in the June 2014 quarter, cash flow over the same period improved by 128% from a cash outflow of $230 million in the June quarter to a cash inflow of $65 million in the June 2014 quarter. That reflects a positive swing of $295 million quarter on quarter for the same period last year versus this year. And that is despite a 7% decline in the gold price.

This brings the total cash flow from operating activities, after capital expenditure, debt service costs and non-recurring items for the year to date, to $119 million. And that places Gold Fields we believe as one of
the most cash-generative gold mining companies in its peer group.

Despite the lower production expected from South Deep for the year, the group remains on track to achieve its full-year guidance of $1,125 per ounce all-in sustaining cost and all-in costs of $1,150 per ounce on attributable gold production of 2.2 million ounces for the year.

Our strong cash generation for the year to date has enabled the group to declare an interim dividend of 20 SA cents per share. This is in line with our well-established dividend policy of paying out between 25% and 35% of normalised earnings to shareholders. And let me re-state it again: if we generate the earnings we will pay the dividend in line with the policy. That’s our commitment.

Despite the robustness of our balance sheet, we have decided to further improve its strength and maturity by reducing the absolute amount of our debt, as well as improving our net debt to EBITDA ratios and also re-scheduling our debt over longer periods.

Now, in pursuit of this objective, we reached agreement with our group of bankers during the quarter to amend and extend certain facilities under our syndicated bank credit lines agreement. Under the amended agreement the maturity date of commitments totalling $715 million has been extended on the same terms by two years from November 2015 to November 2017. And that really gives us great flexibility and a much improved debt maturity ladder.

In addition, during the June 2014 quarter, we reduced our net debt by a further $52 million to $1,635 million. This is in addition to the $49 million reduction in the March quarter. So for the year to date we have reduced our net debt – in other word the capital principle amount – by $101 million.

Based on a 12-month rolling historical average our net debt to EBITDA ratio improved from 1.53 in the March quarter to 1.47 in the June 2014 quarter. In fact if you annualise the June quarter our ratio is 1.44. So we are improving our debt to EBITDA ratio and we are well within our covenants which are 2.5.

Now let’s talk about South Deep, an important growth project for the group. At South Deep all mining related activities were severely curtailed towards the end of May for the final one month of the quarter. This followed two fatal accidents in quick succession unfortunately, after a period of 13 months fatality-free, as well as the separate and unrelated introduction of an extensive ground support remediation programme.

As a consequence South Deep’s production declined by 14% from 59,200 ounces in March to 51,100 ounces in the June quarter.

The remediation programme took all of the legacy haulages and arterial routes on the current line - that is 95 level and above, from where approximately 70% of current production is sourced - and took it out of service. The programme will continue for the entire September quarter with a commensurate impact on production for the September quarter against the June quarter.

While normal production is expected to resume at the start of the December quarter, the ground support remediation programme is delaying the opening up of a number of long-hole stopes that were planned to be mined in the December quarter, with a commensurate knock-on effect on production during that quarter.

Considering the total impact of the safety stoppages as well as the ground support remediation programme, production during the second half of the year therefore is expected to be approximately similar to that of the first half of the year. I’m thankful though that we are making very good progress on the ground support.
We are about 70% of the way through it, and we are certainly on track to complete this within the next four weeks.

A positive consequence of the ground support intervention, and in the absence of normal production pressures, is that it has afforded management the opportunity to fast-track a number of other critical interventions aimed at setting South Deep up for long-term success. The leadership structure on the mine has undergone a fit for purpose transformation aimed at the introduction and enforcement of greater levels of accountability and responsibility throughout the operation.

Management has embarked on a programme to address the surplus of old high-cost equipment and people on the mine, both of which are prerequisites for an improved safety culture and improved productivity, and are deemed critical to de-risk the mine’s build-up to full production.

After extensive discussions with the trade unions, a voluntary separation process was implemented which resulted in a rationalisation of the employee body by approximately 550 people. That represents about 14% of the workforce. Further rationalisation is expected as certain contractors are exited and existing employees redeployed to fill their roles. Post the voluntary separation process, South Deep currently has 3,400 employees as well as 1,900 contractors.

The process of rationalising the equipment is currently underway and includes the removal of surplus and redundant equipment as well as the limited introduction of more appropriate, specialised new equipment in certain areas.

In addition, management and the trade unions have reached agreement on changes to the shift roster which is expected to lead to the optimal re-deployment of employees to further improve productivity. The implementation of the amended shift roster is currently underway. The mine has utilised the hiatus in normal production activities to fast-track an extensive training programme aimed at improving the mechanised mining skills of employees.

It is expected that the ground support programme will not impact the build-up to full production of 650,000 ounces by the end of 2017. In fact, if anything this will de-bottleneck the current haulages and ramps, make the mine safer and improve logistics as well. We are still hoping that South Deep will achieve cash break-even, gold prices prevailing, by the middle of 2015 as previously advised.

We have also been looking at mining methods at South Deep. I did report on this at our presentation in the morning. Soon after the appointment of the new management team in February, and in line with the team’s overall mandate to improve the mechanised mining culture on the mine, an International Geotechnical Advisory Board consisting of industry leaders from around the world, was appointed to review South Deep’s current de-stress mining methodology.

The board’s mandate was to consider the latest developments in the industry as well as the accumulation of new knowledge and experience in the application of the de-stress methodology at South Deep over the past five years and see whether there was a different method that could be used to be more cost effective and easier in the future.

After extensive studies and investigations over the past eight months, the board has concluded that there are two alternative mining methods. The first method is the 4X4 meter de-stress method, which effectively reduces de-stress mining from a three-pass system to a one-pass system by increasing the de-stress excavation dimensions from 2.2m high and 5m wide, to 4m high and 4m wide.
This will allow for the use of conventional equipment throughout the mine as opposed to having two classes of equipment, conventional equipment and low-profile equipment, which are used in the de-stress area. So that gives us a tremendous rationalisation. In addition to removing the need for footwall stripping to increase cavity sizes before mining, this will also alleviate logistical constraints and facilitate a fully mechanised mining process.

In essence what this means is that we can use the same equipment that we use for our development drives, which will very quickly and efficiently do all of the necessary follow-on support at the same time. And we will have one suite of equipment for our operators to get used to, instead of having two suites of equipment. Even though the dimensions of the de-stress could increase to 4m x 4m, the beauty of this is that it is all on strike and it is all on reef. So it won’t result in additional dilution. In fact, if anything it may give us a little bit of extra gold.

The second method, and the most promising, is what we call the Inclined mining slot method, which is a one-pass system which completely removes the need for conventional de-stress mining as well as the need for low-profile equipment. It also decreases the mining lead time from opening up the open stopes from around three years to closer to six months. So it gives us the ability to accelerate the mining. Both of these methods, if successful, could significantly de-risk the South Deep build-up plan and future production profiles, and have a meaningful impact on costs.

I think it is also worth noting that we are also looking at the mining span. Currently we are looking at four corridors of 240m mining span. And we are looking at reducing that to eight corridors of 120m span, which not only could improve the geotechnics in the mine, but would also provide greater flexibility and the ability to accelerate production in certain areas.

Both methods will be piloted in discrete areas of the proximal part of the mine during the period from Q4 this year to Q4 next year. It is too early to assess whether either of these methods could be commercially deployed, the results of the pilot studies will determine this. But I think the one point I would make is, if the studies are successful, we could potentially roll this out in 2016.

Normalising of production at Tarkwa in Ghana has taken place and the transition from a mixed heap leach and carbon in leach operation, to a CIL only operation, has progressed well and the heap leach operations have been closed. We continue to rinse the heap leaches and we continue to get gold out of that, but there is no new stacking taking place as of the beginning of the year.

The realised yield from our CIL plant increased from 1.19 grams per tonne to 1.29 grams per ton. During the June quarter the low grade stockpile to the north-east was significantly less utilised than in the March quarter. And that resulted in an increase in the grade. Tarkwa achieved year to date production of 285,900 ounces at an all-in cost of $1,021. A great performance from Tarkwa, and we believe that there is a lot more to come.

During the quarter Damang delivered another strong performance despite a nine-day mill shutdown, as a result of which gold production decreased by 13% from 46,700 ounces to 40,500 ounces and all-in costs increased by 15% up to $1,282 per ounce. However, we believe that during the current quarter and given the fact that we shouldn’t expect further mill shutdowns, Damang should return to levels achieved in the March quarter. For the year to date Damang has achieved production of 87,000 ounces at an all-in cost of $1,192. Despite the unplanned nine-day mill shutdown, Damang has now consolidated its return to profitability from a loss-making position a year ago. We think this is going to continue well into the foreseeable future.
Now, the strategy of revisiting historically mined open pits along the 27 kilometre strike between Damang in the north and Tarkwa in the south, which were last drilled when the gold price was between $300 per ounce and $400 per ounce, is starting to bear fruit and is expected to contribute to an addition to Reserves and Resources by the time of the next declaration early next year. Success in this programme will redefine the future of Damang in the Gold Fields portfolio, and has the potential to extend the life of this mine substantially.

Turning to Australia. The Group’s Australian operations had an excellent quarter, recording all-in costs of $1,042 per ounce on gold production of 257,000 ounces. This brings total production for the year to date to 502,000 ounces at an all-in cost of $1,072 per ounce. Central to this performance are the newly acquired Yilgarn South assets which have now been fully integrated into the Australia region and are exceeding our expectations.

The star performer was the Granny Smith mine, which contributed 84,600 ounces at an all-in cost of $692 per ounce for the quarter. Year to date, the mine has produced 151,100 ounces at an all-in cost of $788 per ounce.

A key focus of the Australian portfolio is the accelerated US$52 million of near-mine exploration at all of the mines in the region, aimed at increasing the Resource and Reserve position by the end of 2014.

Good progress has been made, particularly at St Ives, with the newly discovered high-grade-Invincible deposit, and at Granny Smith where exploration results are indicating significant Resource and Reserve expansion potential at the Wallaby underground deposit. Good progress is also being made at Agnew/Lawlers with potential extensions to the Waroonga underground mine as well as the New Holland and Genesis underground ore bodies.

During the quarter, we hosted a series of site visits to our Australian mines to give the investment community some insight into the outstanding potential of these assets. The presentations are available on our website at www.goldfields.com.

Turning to disposal of non-core assets. During the quarter, good progress was made with the disposal of two further non-core assets in our International Projects portfolio, with the disposal of both the Yanfolila project in Mali as well as the Chucapaca project in Peru.

Gold Fields sold its 85% interest in the Yanfolila project in Mali to London-listed Hummingbird Resources for $20 million in the form of Hummingbird shares. The consideration represents an acquisition price of $16 per resource ounce, which was higher than both the weighted average enterprise value per resource ounce of listed West African gold companies and recent M&A precedents of West African exploration/development assets of $14 per ounce.

Through our shareholding in Hummingbird, which also holds the Dugbe asset in Liberia, we see real potential for Gold Fields to receive significant growth in the value of its shareholding, which was a key consideration in favouring this bid.

The latest sale is that of the Chucapaca project in southern Peru, which was announced a couple of days ago. Gold Fields has sold its 51% stake in CDH, which is the company owning the project, to its joint venture partner Buenaventura, a Peruvian company. The total agreed sale price is $81 million all paid on closing of the agreement. And in fact I’m pleased to announce we actually have the cheque in hand. And in addition
Gold Fields will also receive an uncapped 1.5% net smelter royalty on all future gold, silver and copper sales emanating in the area of interest that was the subject of the joint venture.

Not only does the consideration ensure that our historical costs on the project are essentially covered, the consideration also represents an acquisition price of about $26 per attributable gold resource, which compares favourably to deals done in Latin America. The royalty of 1.5% provides us with future upside potential, especially as we see a quality company of Buenaventura’s standing moving this project ahead.

The sale of our holdings in these projects is in line with our strategy of focusing on growing cash flow through quality assets. This focus has also led us to move away from greenfields exploration as a strategy for growth in favour of the acquisition of in-production ounces such as the Yilgarn South assets and near-mine exploration and development at our Australian, Ghanaian and Peruvian assets.

With that I conclude my prepared remarks. We are now ready to take some questions.

Andrew Byrne – Barclays

Hi. Good afternoon Nick. A couple of quick questions if I may. The first one is around St Ives. With Neptune and Invincible coming on where are you expecting the grades to go to for 2015?

Nick Holland – CEO

We haven’t yet done our business plan for 2015, Andrew. But Neptune looks like it is around about 4g. But we will probably mine stage one by the end of the year. There are four other stages, and we want to see the results of stage one before we carry on further. Invincible, we will start stripping in Q4 and we will probably get that into production I would think around about the middle of next year. And the open pit grades look like they are somewhere around 4g per ton. So this could contribute 25% to 30% of the total mill feed. So it will definitely get the grade up, but I couldn’t tell you at this stage what the grade is likely to be. In 2015 we expect the mill contribution to come from Athena, Hamlet, Cave Rocks and probably Invincible with a couple of peripheral open pits. So it will be the weighted average of whatever they are.

Andrew Byrne – Barclays

Sure, no worries. I think it was Neptune phase one, pausing and then coming back, if I remember from the site visit. Looking at Ghana, on Damang and Tarkwa should we expect to see volumes closer to what we saw in Q1 over the next two quarters? I know we had the rainfall there and then also the unplanned outage at Damang. Is that the way to think about those two assets?

Nick Holland – CEO

Absolutely, because the rain was particularly tough in the last quarter. I would think we should see an improvement from that perspective. We have given guidance for the year for Tarkwa in February and we should actually do quite a bit better than that. But I don’t want to give definitive numbers yet. And Damang should also do better given that we lost nine days in Q2. So I think the big thing we are looking to do on Tarkwa is finish the CIL expansion by the end of the year, which would give us 13 million tonnes of processing capacity. We probably won’t see the benefit of that until Q1 next year. The other thing is at Damang we making sure that we are maximising the grade to the plant by really focussing on dilution in the pits. And we are getting into some of the better grade stuff now - deeper into Huni, in the saddle and in Juno as well. So the grades should improve. So we are more focussed at Damang on the grade than we are
on the volume, because we are focussing on 4 million to 4.2 million tonnes per year through the plant.

Andrew Byrne – Barclays

Two last questions if I may. Looking at what you’ve done in Australia do you look at Iduapriem and think there is an opportunity to do consolidation with Tarkwa and Damang, even from a regional management perspective and look for some synergies on that side? Is that something you have looked at? Or are there some obvious reasons why that just doesn’t work?

Nick Holland – CEO

Certainly Iduapriem is contiguous to Tarkwa. The Teberebi portion of Tarkwa is contiguous to Iduapriem. It really depends on what AngloGold’s aspirations are given the fact they are pulling back Obuasi and what they want to do in the country. It would depend first of all on their strategic direction with regard to Ghana. And then, whether or not a deal could be done on terms that made sense. I think we would not be averse to the idea. We haven’t got a good idea of all of the synergies that might exist between the operations. I’m sure that there are some. If the opportunity arose I guess we would look at it.

Andrew Byrne – Barclays

Looking at your full year cost guidance, given that you have done an all-in sustaining cost of $1,058 in the first half; when we look at the second half and let’s say volumes from Tarkwa and Damang are likely to be at least in line if not somewhat better, potentially the volume coming in from Neptune in Q4, when we look at your cost guidance does it imply a second half cost of around $1,200 an ounce? Is that you just being cautious or is it something that we really need to just be wary of?

Paul Schmidt – CFO

Andrew, it is Paul here. We are just being cautious. And I think you also need to understand we said South Deep will have a tough third quarter based on the announcement we put out. We are being cautious. I don’t want to bring down my all-in cost guidance. If we beat it, great. We will see what will happen.

David Horton – Bank of Montreal

Hi Nick. Thank you for the update. Can you just give us a bit of an idea for South Deep where you’re at with these two new methodologies, the 4 x 4 and the inclined slot? What is required for you to move from it simply being on the drawing board and it being implemented, and what kind of timetable could you imagine for that?

Nick Holland – CEO

Sure, David. What we’ve done is, we’ve identified two areas to run the pilot. These are areas outside the current plan on the eastern side of the mine. And we have set aside these two areas. So we are hoping to get these pilots mobilised in Q4. We need our geotechnical review board to sign off on the design of the final pilot. And we will probably run these pilots for maybe nine months or so and then see how they go. If it works we will decide which method to adopt. Clearly if we could move to the incline slot method that would do away with the need for the conventional de-stressing that we currently adopt, it would enable us to open up the ore body much faster than what we are currently doing. The only thing we would need to do though, before we could implement any of them, is we have to make sure that we have all of the faces
along the 1km strike all in the right position. When you change this mining method you have to obviously change it across the entire mine and we need to keep our geotechnical sequence and shape in place. That will take a few months too. So realistically, if it all works I would say we are looking at the beginning of 2016 to implement one of these two methods. The conceptual work has already been done and the geotechnical review board is very confident that these methods should work. But that said, the proof is in the pudding. We’ve got to put this into action, run these pilots and see how we end up. That is the best estimate I can give you at this point in time. Obviously if it works, David, then we will have to not only implement it but we will have to remodel the entire life of mine, and that will take some time too. But I think the best estimates are that hopefully by the end of next year we might be in a position to implement either one of these methods. They are mutually exclusive of course.

David Horton – Bank of Montreal

And each of those two methods, do they use similar kinds of equipment? I guess the follow-on from that is if you select one or the other how different is the equipment and the training compared to what you do now?

Nick Holland – CEO

We wouldn’t need to use any different equipment. It would be the same equipment we are using. We would be using our conventional 282 drill rigs and we would be using our long-hole drill rigs. So no change there. The one benefit through common to both is that we could get rid of low-profile equipment. In other words we could work with one suite of equipment that we already have. In terms of skills, this is bog standard mechanised mining. Whether you are drilling an incline slot or whether you are drilling a de-stress face, it is all the same principles. It is just a change in the overall mine design. So we don’t see a major challenge in terms of equipment because we’ve got the equipment. And the skills are common. Whether we mine as we currently mine or whether we change we’ve got to get the skills upgraded. That is common to all scenarios.

David Horton – Bank of Montreal

Just guestimating from the description that you’ve provided it would seem as though the incline slot method might have a lower sustaining capital number to the 4 x 4 and to the exiting one. Is that a reasonable way to think about it because you’re not doing the de-stress slot as a separate kind of exercise?

Nick Holland – CEO

Exactly. Firstly it is one-pass mining instead of three-pass mining. We would need much less support because the slots would be a no-entry area so they would be unsupported. And the open stope, of course, is a non-entry area and you just blast that out. So we would need a lot less mesh, steel anchors, split sets, all of those kinds of things. So we will save some money there. And we will save time. I think the biggest benefit here is you can actually get mining areas opened up in six months as opposed to 24 to 36 months with the current de-stress mining grid, which requires us to have a whole grid opened up of main access drive, secondary access drive, coming through, ripping up the footwall to make sure we can get the big fleet in. So it is going to save us a lot of time. I think the biggest benefit here is the time that we will save.

David Horton – Bank of Montreal
Looking at Granny. In your slide deck you've got quite a number of slides there about the geology, where you're sitting and expectations. The quarter itself was surprisingly good grade. Is that just a spike in the grade profile or is it something that we should be thinking about as a better grade going forward? How should we be thinking about Granny in a go-forward situation?

Nick Holland – CEO

We said when we bought the asset that we thought the grade would improve as we get deeper. The other thing is we're finding that we're getting positive reconciliations on the grade compared to the resource model. And that is something we flagged when we bought the mine, so that doesn’t surprise us. The other thing we are doing is we are reducing our dilution. There has been a big focus on reduced dilution. We have probably chopped our dilution by 10% to 15% if you look at the period since we bought it. The other thing that is good, and doesn’t come through in the head grade but comes through in the yield, is we have improved our process plant recoveries by 5% from 87% to 92% simply by just changing the cyclones that we used. Putting in smaller cyclones has given us better grind. And then changing pumping systems to get more consistent flows. So that has given us a 5% increase in recoveries, which we think is sustainable. As we get into the deeper parts of the mine you will see the grade getting better, and that is borne out by the exploration results. So I think this quarter has been particularly good. I’m not saying that you should model the grades that we are showing here going forward, but certainly we believe we should be getting better grades than the historical grades achieved.

David Horton – Bank of Montreal

Okay, and last one, probably more an accounting kind of question. With the sale of the assets would you expect to record a profit or loss on the sale or is it close to break even?

Paul Schmidt – CFO

Close to break even on Yanfolila. On Yanfolila we’re going to be reversing $4 million of impairment we did last year. So $4 million positive. And on Chucapaca it is fairly much break even or a small profit we’re going to make. But we don’t account for the royalty.

Nick Holland – CEO

With the value of the royalty I think we would be in a profit, but we can’t value it at this stage.

Patrick Mann – Deutsche Bank

I have a follow-up to the previous question. Have you got a sense of the tax implications on the sale of Chucapaca? And then I think just on the safety review at South Deep. You said that it was the new management team identifying weakness in the system and that they could potentially find other things or you couldn’t guarantee that they wouldn’t. Have they finished that process of looking through the mine now? Are you more comfortable that they are up to speed with everything that is going on and what the support structures across the entire mine look like? Just an update on that please.

Nick Holland – CEO

I think we are in a much better position, Patrick, compared to where we were six months ago. But I think we probably need the rest of the year to really make sure we really understand all of the issues and areas. I
think slowly but surely the list of issues coming out of the review are getting less and less. I think when we finish the year we will identify if there is anything more that we think is going to impact us. But certainly there are much less surprises coming out. There are obviously ground support issues to be done across the mine, but these are not urgent and we think we can do a lot of those concurrently with normal activities. We had to stop these areas because they were really impacting on safety and not really the required standard we see internationally. But I’m not seeing any roadblocks for us to get back to normal production, let me put it that way, in the last quarter of the year. At this stage we believe we can get back into normal production and flow that into next year.

Nick Holland – CEO

Thanks very much everyone for joining us today. And we look forward to talking to you again following the year end results and seeing a lot of you face-to-face in the various meetings and conferences that we will be doing over the next number of months. Once again thanks for dialling in and showing your interest.

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