Fortescue

December 2021 Quarterly Production Report

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Start of Transcript

Operator: Thank you for standing by. Welcome to the Fortescue Metals Group December 2021 Quarterly Production Report analyst call. All participants are in a listen-only mode. There will be a presentation followed by a question and answer session. If you wish to ask a question you will need to press the star key followed by the number one on your telephone keypad. We ask that participants limit themselves to asking two questions per turn. To ask further questions please re-join the queue. I would now like to hand the conference over to Elizabeth Gaines, Chief Executive Officer. Please go ahead.

Elizabeth Gaines: Thank you Harmony. Good morning or afternoon everyone. Welcome to Fortescue's December 2021 Quarterly Production Report. Joining me today in Perth is Ian Wells, Chief Financial Officer. I am delighted to welcome Ben Watego who joins us as CEO for a day. Ben is a proud Yugambeh man who joined Fortescue in 2014 as a contractor at our Christmas Creek mine.

Then in 2016, Ben went on to graduate from Fortescue's Vocational Training and Education Centre program as a Mining Operator, and has progressed through various roles before stepping up to a Coordinator Mine Services role at Fortescue's Eliwana mine. Ben always embraces any task, demonstrating outstanding leadership to his team members. It is great to have you with us Ben.

Ben Watego: It's an honour to be here. Thanks for having me.

Elizabeth Gaines: So, during the quarter the momentum of Fortescue's transition to a vertically integrated green energy and resources company continued to accelerate. Of course, just yesterday we announced some exciting news with Fortescue entering into an agreement to acquire Williams Advanced Engineering (WAE) for £164 million. That will provide critical technology and expertise in high performance battery systems and electrification. I will speak a little bit more on this later.

So that brings me to our second quarter results. As you can see from today's report it was an outstanding quarter for Fortescue, with the team's strong operational performance delivering across our key metrics of safety, production and cost, with mining, processing, rail and shipping combining to deliver record second quarter shipments as well as a record for the first half.

So, I'll start with safety. The health and safety of all of our team members is our highest priority. I want to commend the entire Fortescue family for continuing to look out for their mates on our journey to zero harm.

During the quarter we achieved a Total Recordable Injury Frequency Rate (TRIFR) of 1.8 for the 12 months to 31 December 2021. That's a 14 per cent improvement on 2.1 at 31 December 2020. This is a reflection of our core value of safety and our commitment to always look out for our workmates and ourselves.

The State border restrictions have been a critical factor in controlling the COVID-19 outbreak in WA. However, it is disappointing to see the border reopening date has been delayed. We continue to review our robust COVID-19 Management Plan to ensure we can operate safely. We have introduced a policy requiring vaccinations across our entire operations, including our office facilities here in Western Australia.

With higher vaccination rates evident across WA, we believe it is important that we have a defined plan to transition towards the reopening of WA's border. We are continuing to work with all of the relevant authorities and take every precaution to keep our team members safe.

So, moving to our operational performance for the quarter. We continued the strong start to FY22 with the Fortescue team achieving record second quarter shipments of 47.5 million tonnes, contributing to record performance for a half year of 93.1 million tonnes shipped. Importantly, our C1 cost was in line with the previous quarter at US$15.31 a wet metric tonne. That reflects our strong focus on cost management to mitigate inflationary pressures that are impacting the mining sector as a whole.

Turning to the market, the market remained dynamic during the quarter. That resulted in increased price volatility. Chinese crude steel production reached 1.03 billion tonnes for calendar 2021. That's a decrease of three per cent compared to 2020's all-time record level. Output in the second half was impacted by steel production curtailments and energy supply shortages. This lower output contributed to an increase in iron ore inventory at China's ports to current levels of about 154 million tonnes.

Steel mills in China have started to restock since December, as severe production curtailments were relaxed, also in response to more supportive government policy settings. Iron ore arrivals at ports has recently slowed and heavy rainfall in Brazil over the past fortnight serves as a reminder of the risks of weather-related supply disruptions at this time of year.

We also acknowledge that it is three years today since the tragic accident at the Brumadinho Dam, that reinforced the industry's commitment to tailings management and safety more broadly. This event continues to influence the supply demand dynamics observed in the iron ore market today.

Crude steel production outside of China increased by 12.6 per cent to 804 million tonnes in the 11 months to 30 November 2021, returning to pre-COVID levels. The pandemic remains a clear risk, but we are encouraged by the prospects for growth in global steel demand this year. We continue to see strong demand for our products achieving an average revenue of US$74 a dry metric tonne for the quarter.

That's a revenue realisation of 68 per cent of the Platts 62% Index. As always, we are continuing to work closely with our customers in China and elsewhere to ensure that we are responsive to market conditions. Our marketing strategy means that we are well-placed to deliver on our customers' needs and maximise the value of our product portfolio.

So, turning to an update on Iron Bridge. I visited the site in December and was really pleased with the significant progress made by the team. That progress includes the completion of the module offload facility at Lumsden Point with five ships received and unloaded to date along with 20 vessels that have been offloaded at Berth 2 in Port Hedland.

Module fabrication is progressing well and has reached 85 per cent completion at the end of December. Civil construction on site is now over 75 per cent complete with the transition to SMP and E&I activities underway. The team has also commenced laying the concentrate pipeline, return water pipeline and the Canning Basin raw water pipeline. Earthworks have also commenced at the concentrate handling facility at Fortescue's port facility in Port Hedland, and we have also started pre-strip mining. That's all ahead of first production scheduled in December this year.

The project has made excellent progress to date with a continued focus on managing industry cost pressures, supply chain constraints and the other challenges associated with the impact of COVID-19.

As the project ramps up to peak construction workforce numbers, the availability of labour and access to specialist skills remains a key focus. Iron Bridge is an important and strategic investment for Fortescue and our Joint Venture partner, and will further enhance our range of products to meet strong demand from our customers.

So, on exploration, total exploration and studies capital expenditure for the December quarter was US$45 million. During the quarter we announced an agreement with the Government of the Republic of Gabon to study the opportunity to develop the Belinga Iron Ore project in Gabon, West Africa.

Just last week we signed a binding MoU with Sinosteel to complete a rapid project assessment of Sinosteel's Midwest Magnetite project, with that assessment to include a rail and port development at Oakajee. We are looking forward to working with Sinosteel on this important project, which will also consider the potential future development of a renewable energy and green hydrogen hub.

Iron ore exploration in the Pilbara included target and resource definition drilling in the Western Hub and Eastern Hamersley with a focus on the program at Mindy South. Exploration activity on the Australian copper-gold portfolio included the completion of airborne magnetic and electromagnetic surveys, a ground gravity survey and on-ground mapping and soil sampling over the Paterson and Rudall projects in Western Australia.

Our international activities included the commencement of a drilling program at the Rincones project in Argentina, as well as continued exploration activities on several project areas in Ecuador.

On that, I'm going to hand over to Ian for an update on the financials. Ian.

Ian Wells: Thanks Elizabeth and hi everyone. As you can see from the results, the team have delivered another excellent quarter with record volumes and continued strong cost control, and effectively managing the challenges associated with COVID-19. We continue to invest in sustaining and growing our business, supported by our strong balance sheet and disciplined capital allocation framework. Consistent performance is enabled by focusing on the things that we can control – which of course is safety, production, and costs.

So, on to the quarterly, our average revenue in Q2 was 68 per cent of the Platts 62% Index at US$74 a tonne, and our average revenue for the first half was US$96 a tonne at a realisation of 70 per cent of the Platts Index. There was clearly a rapid shift in price realisations in the half, and I would just like to provide some additional context to that result.

Our realised price was impacted by both severe reduction in China's steel production which was down 15 per cent compared with the first half of calendar year 2021, and also the same period last year. So that's down 15 per cent to 16 per cent between those two corresponding periods.

While at the same time low grade iron ore supply increased with the high grade supply constraints and the low grade increasing also in response to the higher index prices. We estimate that this low grade supply was up about 12 per cent year on year in the second half of calendar year 2021.

So put simply, demand down, supply up is going to always impact price. Our customers have been focused on value amidst that strong competition in the low grade segment and will continue to see firm demand and liquidity for our products underpinned by our team's integrated approach to product quality and also direct customer engagement.

That's also evident by the low levels of Fortescue products as a percentage share of China's total port stocks. They have been maintained or in fact slightly reduced at about 10 per cent share, even as the total low grade stocks have increased to almost 45 per cent of port inventories.

As we have previously indicated, price realisations are cyclical. Fortescue's product pricing continues to be influenced by a range of cyclical factors such as steel margins, coke price and the relative iron ore demand and supply in the various market segments. As a reminder, our quarterly average realisation over the past decade is around that 82 per cent.

So, moving now to costs, our Aussie dollar total C1 spend was up quarter on quarter, largely the result of higher import prices, particularly diesel, and also ammonium nitrate. Our higher shipments achieved contributed to a C1 cost of US$15.31 which was in line with the previous two quarters and also underscores our strong cost control across the business, particularly amidst the inflationary environment that obviously we are all aware of. So C1 costs in the first half were US$15.28, and that includes COVID related costs which we estimate to be in the range of US$0.15 to US$0.20 a tonne. Our C1 cost guidance for the full year remains at US$15.00 to US$15.50. This guidance is underpinned by an average Aussie exchange rate of $0.72. That is down from our previous $0.75.

Switching gears to the balance sheet. Closing cash on hand was US$2.9 billion. A couple of key movements during the quarter to highlight capex of US$744 million. We also paid the FY21 tax instalment of US$915 million. That has been well flagged, and is of course in addition to our monthly instalments paid for FY22 tax. We also saw a major working capital outflow. That reflects the unwind of provisions and payables which again we flagged at the September quarter, meaning that the cash for those payables was sitting in the bank at the end of September. We also had an inflow from the proceeds of drawing the additional US$400 million for our Term Loan facility, and that funding will support this year's growth capital program.

As a result of drawing the facility, gross debt increases from US$4.2 billion at 30 September to US$4.6 billion at the end of the quarter. Whilst I'm on the subject of debt, during the quarter we also established our Sustainability Financing Framework and that will enable future issuance of Green and Social debt instruments that will support our investments in eligible projects.

The framework obviously leverages heavily off Fortescue's ongoing commitment to ESG leadership and recognises also the growth in sustainable, green, and social sources of capital in the market, and further optimises our debt capital structure.

On capital expenditure in the first half that was US$1.5 billion and looking ahead, we've increased FY22 capex guidance by US$200 million to incorporate the purchase of WAE. So, capex excluding FFI of US$3.0 billion to US$3.4 billion, that was previously US$2.8 billion to US$3.2 billion, and our capex guidance includes US$1.1 billion to US$1.4 billion on growth projects: Iron Bridge and Pilbara Energy Connect.

On FFI, operating expenditure in first half was US$174 million and expenditure guidance for FFI for FY22 is unchanged at US$400 million to US$600 million, noting that that comprises both operating and capital expenditure categories.

For me in closing, strong cost management and discipline together with our robust balance sheet and liquidity has supported another outstanding first half performance and puts us in a great position going into the second half and I look forward to updating you with some more detail and our half year financial results in a couple of weeksOn that note, Elizabeth, back to you.

Elizabeth Gaines: Thanks, Ian. As Fortescue continues its transition to a vertically integrated green energy and resources company, Fortescue Future Industries will be a key enabler of delivery of our industry-leading decarbonisation targets. As we announced yesterday, our acquisition of Williams Advanced Engineering supports these targets and further underpins our leadership in green energy through the provision of critical technology and expertise in high-performance battery systems and electrification.

We've been working with WAE since March last year, and during this time it quickly became apparent that WAE's electrification technology and capabilities are industry-leading and they can't be easily replaced or replicated. So, we made the decision to acquire WAE to mitigate key supplier technology and intellectual property risk in order to significantly de-risk the execution of our decarbonisation strategy.

Together, Fortescue and WAE will develop battery electric solutions for Fortescue's rail, mobile haul fleet, and other heavy mining equipment to accelerate the rapid abatement of diesel usage across our operations. And, as the world transitions, the potential market for WAE's technology and engineering capability is very significant and that will extend beyond the decarbonisation of Fortescue. This further demonstrates our commitment to diversify into a renewable energy and resources company.

Other FFI milestones during the quarter included the continued advancement of our green fleet development and the arrival of two four-stroke locomotives at Fortescue's research and development facility in Hazelmere. We also recently announced the purchase of two new battery electric locomotives from Progress Rail Australia, with the first locomotive scheduled for delivery in 2023.

We received planning approval from the Queensland Government for the Global Green Energy Manufacturing Centre in Gladstone, Queensland. You will recall that the first stage development is an electrolyser manufacturing facility with initial capacity of two gigawatts per annum with an investment of up to US$83 million.

In closing, you can see it's been a very busy quarter for the team, and we have maintained our operational excellence and continued to invest in sustaining and growing our business.

That strong first half means that we're well placed to meet our FY22 guidance with iron ore shipments in the range of 180 million to 185 million tonnes, a C1 cost of US$15.00 to US$15.50 a tonne, and capital expenditure excluding FFI updated to a range of US$3.0 billion to US$3.4 billion. Our record operational performance, along with that focus on safety and cost management, means Fortescue is positioned strongly for the future.

As always, I'd like to thank our team members, contractors, and suppliers for their hard work and commitment this quarter as we continue to deliver on our strategic priorities.

On that, I'll hand back to Harmony to facilitate Q&A. Thank you.

Operator: Thank you. If you wish to ask a question, please press star 1 on your telephone and wait for your name to be announced. If you wish to cancel your request, please press star 2. If you are on a speakerphone, please pick up the handset to ask your question. A reminder that we ask that participants please limit themselves to asking two questions per turn. To ask further questions, please re-join the queue.

Your first question comes from James Redfern from Bank of America. Please go ahead.

James Redfern: (Bank of America) Hi Elizabeth, I hope you're well. My first question, please, is in relation to Williams Advanced Engineering, and just wondering if you could please talk a bit more about the decision to buy the company for US$223 million as opposed to just buying the technology or licensing their battery technology down the track. Then maybe any numbers you can provide around EBITDA generated by WAE, if any, just in terms of putting some valuation metrics around the transaction at all please. I've got one more. Thank you.

Elizabeth Gaines: Okay. Thanks, James. I think the decision to buy versus continuing to work with Williams Advanced Engineering was quite an easy one actually. It became apparent when we worked with them, that they are the leaders in their field and their expertise, their innovation, for us to accelerate our own decarbonisation but to also recognise the significant commercial opportunity for the heavy industry sector once that technology is proven.

We see that we could have worked with them, we could have paid them quite a lot of money and they would have made a margin on that, or we could have invested at this point in the cycle, and we think that's going to create excellent value for our shareholders. We've quoted the revenue, the unaudited revenue, and their EBITDA margins are modest as you could probably see from their accounts that they've lodged in the UK in the past, but we focus more on the opportunity ahead of us. It's not unusual for technology companies to be valued more on a revenue multiple versus EBITDA.

James Redfern: (Bank of America) Okay, thanks Elizabeth. Then the second question is in relation to the iron ore market. Iron ore price is very strong at the moment, as you know, slightly above US$130 a tonne. I just was wondering what your view is given the outlook for Chinese steel production this year and iron ore in core inventories at 3.5-year highs. I'm just wondering if you think that iron ore price at these levels are sustainable. Thank you.

Elizabeth Gaines: I never like to predict the iron ore price and we've seen the current dynamics at play really for some time now. Of course, there's been some moderation and you'll see some strengthening. There's been weather impacts, supply constraints, as well as the steel curtailments in China. We've seen some easing of those curtailments; we're seeing policy that's supportive of I guess stronger economic growth. All of that would indicate that we should see conditions stay around current levels, given we expect to see an uptick in steel production coming out of that curtailment period and post the Winter Olympics.

There is no major change on the horizon for supply. As I said, we don't like to predict the iron ore price but there's nothing to indicate any significant changes other than we should start to see some further easing of those curtailments. We're seeing strong demand for our products from our customers. Ian mentioned that our share of those port stocks has slightly moderated, so we're not seeing a build-up of our products at ports. Strong demand, keep our costs low, and generate strong margins.

Operator: Thank you. Your next question comes from Kaan Peker from Royal Bank of Canada. Please go ahead.

Kaan Peker: (Royal Bank of Canada) Happy new year, Elizabeth, Ian, and team. Just two questions from me. The first one is around FMG Trading Shanghai. I'm just wondering how much inventory currently sits with that entity, and has that changed over the year or this quarter?

Elizabeth Gaines: Look, it's stayed pretty modest and the team have done a great job. We've seen a slight build-up, as you would expect as it only started 12-18 months ago, but it's sitting at about 1.6 million tonnes of inventory.

Kaan Peker: (Royal Bank of Canada) Okay, pretty minor then. The second question is more around Sinosteel and the MoU. Just wondering if you could provide some details around that. I know it's pretty early stage, but some high-level comments around timing, funding, process, and why the attraction in the infrastructure over the mine. Is there a view on operational synergies given the large distance between Iron Bridge? Thanks.

Elizabeth Gaines: Well, it is very early stages, Kaan. When we announced the MoU on Friday, this now gives us the opportunity to work with Sinosteel, get access to the data that they've got so we can actually undertake that 12-month assessment. So, it's just too early to provide any other guidance on that. We see that there's opportunity.

We're not necessarily saying whether it's the mine or infrastructure at this point in time; we're looking at that whole opportunity and what that might look like, including the port infrastructure, but certainly the mine is a significant opportunity. We'll undertake that assessment; we'll work closely with Sinosteel. We're really pleased to be working with them and now we can access a lot of that data and we can undertake that project assessment.

Operator: Thank you. Your next question comes from David Radclyffe from Global Mining Research. Please go ahead.

David Radclyffe: (Global Mining Research) Hi Elizabeth and team. My question is back on FFI and the internal technology business. You've now acquired I guess a number of companies which plugs holes or accelerates internal R&D you've been conducting. How should we now think about the key potential technology gaps or risks across either the decarbonisation or green energy internal businesses to achieve the 2030 targets you've set out?

Elizabeth Gaines: Yes. It's a very good question, David. You're right, we're developing a lot of capability, like electrolyser manufacturing. We know that demand for electrolysers is increasing so we've got that opportunity in Queensland. All of this is adding to our goal to decarbonise by 2030. The work we're doing with Williams Advanced Engineering, we've had a lot of success to date but there's a lot more work required on I guess the research and development aspects of how we actually get a mining haul truck that gives us the same efficiency as a diesel fuelled haul truck, and that's the work ahead of us.

One of the benefits of WAE is their battery management systems and their light-weighting and fast-charging capabilities. That's the type of technology we get access to, so all of this will help to accelerate our decarbonisation. As we've said on many occasions, we're aligning our capital investment in decarbonisation with our current plans for fleet renewal, with the majority of our fleet renewal due in the middle of this decade. We've still got time to work with WAE and other partners to optimise the performance of that fleet so that we can make those capital decisions with enough lead time that we're making smart decisions about the mining fleet of the future, plus obviously contributing to our other decarbonisation objectives.

These are big projects; we're well down the path in terms of stationary energy with Pilbara Energy Connect and the installation of large-scale solar, but as we look to decarbonise by 2030 there'll be demand for additional renewable energy, so stationary power as well as these solutions for our mobile fleet, and rail operations is also another key opportunity, and that will displace around 85 million litres of diesel a year.

David Radclyffe: (Global Mining Research) Okay, because I guess we're just trying to understand what if anything is on the critical path as you see it, because the flipside of that is I imagine you also probably feel like you've ticked a number of boxes that we just don't know about.

Elizabeth Gaines: Yes, we're ticking a lot of boxes but it's all part of that journey to align our fleet renewal with that mining fleet of the future. It's bringing together all of those pieces of technology but there's more work required, more work to make sure that we have, as I said, the same efficiency, operating capabilities in a green haul truck versus a diesel haul truck is one example. The opportunities for rail we think are significant but that will take some further work and development.

Operator: Thank you. Your next question comes from Paul Young from Goldman Sachs. Please go ahead.

Paul Young: (Goldman Sachs) Hi Elizabeth, hi Ian. Just questions on Iron Bridge. Elizabeth, did you actually have enough sufficient access to labour and all the different components of the project to actually get this project commissioned by the December quarter?

The second question is around FFI. Thanks for showing a list of activities during the quarter, that's helpful. Can I ask, how many feasibility studies are actually underway on the particular overseas projects like the Papua New Guinea opportunity? Also, is there any guide to give us on when you think the first major feasibility study will be complete?

Elizabeth Gaines: Well maybe we'll start with Iron Bridge, Paul. Look, the team have made enormous progress and in my script I just talked to then about the progress that we have been making and it is significant. Whether it's the module offload facilities, module fabrications, civil construction at 75 per cent complete. So obviously we've got the labour to do all of that activity.

We are ramping up to peak workforce. We did have an anticipation that WA borders would re-open on 5 February and we're now working with the State Government on making sure we have access to the resources that we need to continue that progress. We're getting some good engagement with the Government around what qualifies as specialist workers and essential workers and we're continuing to work closely with them. But it is something we're very focussed on because we need to make sure we maintain that access to labour and we have some mobility of labour across Australia.

And FFI, the portfolio is progressing and there is a number of pre-feasibility assessments. Certainly, in Australia, with work still under way with the Tasmanian Government on the Bell Bay opportunity and Gibson Island, where we've confirmed the potential development of that and we're moving to the next stage of studies on Gibson Island.

So, there's quite a lot of activity in progress on Gibson Island in Queensland and there's the portfolio of I guess pre-feasibility studies occurring globally. You mentioned Papua New Guinea. There's a number of other projects in line with the MoUs that we've announced in the past.

Paul Young: (Goldman Sachs) Elizabeth, then a follow up, please. So, based on that, which of those projects do you think, as far as the studies are concerned, will be completed first on the study front?

Elizabeth Gaines: The studies need to take into account a range of different factors, including approvals and community engagement. So, it's hard to put a defined timeline on that but certainly, that opportunity at Gibson Island in Queensland is pretty well advanced. As well as Fortescue's decarbonisation and the work that's under way on Fortescue's decarbonisation and energy requirements.

Paul Young: (Goldman Sachs) Yes, are we talking next six months we see some project study outcomes? Next 12 months? Next two years? Any idea on timing?

Elizabeth Gaines: Look, Paul, as typical of Fortescue, we're always ambitious to get things moving and we've set ourselves stretch targets, so there is a lot of activity. Gladstone's a good example. I mean, we're getting on with the manufacturing facility at Gladstone. So, there's no shortage of activity. On the feasibility studies, we'll go through the process. We're disciplined in our approach, but it'll always be with a sense of urgency.

Operator: Thank you. Your next question comes from Saul Kavonic from Credit Suisse. Please, go ahead.

Saul Kavonic: (Credit Suisse) Hi, folks. I have a few FFI-related questions, but I'll just start with the first one. So, the Williams Advanced Engineering acquisition, that spend appears outside the FFI spend guidance. So, I want to understand if we should expect more FFI-related M&A that could consume cash outside spend guidance?

Previously you talked about 10 per cent of NPAT going to FFI. This would now be about 14 per cent if we include WAE and should we expect much greater than 10 per cent of NPAT being spent on FFI if we include M&A going forward?

Elizabeth Gaines: Well look, I think we've been very clear on our allocation to FFI of 10 per cent of NPAT and that is funding the studies that we spoke about, the technology developments. On WAE, it was Fortescue that started working with them in March last year and that's to build, test, integrate a battery system to power an electric mining haul truck for Fortescue's mining operations.

So, we see this investment as part of our overall decarbonisation of Fortescue aligned with our goal to be net zero emissions by 2030. So, it fits squarely within the Fortescue decarbonisation. The 10 per cent of NPAT for FFI, that's what we've guided to and within that, they have already made some, I guess more M&A-style transactions - which is relatively modest and are within that 10 per cent framework.

Saul Kavonic: (Credit Suisse) Thanks, so just a point of clarification, then. The US$230 million odd on the WAE acquisition, is that part of the US$400 to US$600 million FFI guidance? Or that's in addition to that?

Elizabeth Gaines: No, it's in addition. That's Fortescue acquiring Williams Advanced Engineering, which is why we've increased the guidance for Fortescue's capex, excluding FFI.

Saul Kavonic: (Credit Suisse) Thank you and just my second question, also on the acquisition was just appears more focussed on battery rather than hydrogen fuel cell tech. I just want to ask how we should think about the scope of FFI's ambitions here? I mean, previously it's been a lot more hydrogen-focussed and internal decarbonisation focussed but do you see scope to expand this well beyond hydrogen and just the internal operational decarbonisation to include things like the battery supply chain? What kind of defines the limits of FFI's ambition here?

Elizabeth Gaines: Well to bring green hydrogen and green ammonia to life, you need battery technology. So, this is not an either/or equation and this technology with Williams Advanced Engineering will optimise our green energy. So, it doesn't mean that FFI is putting a greater focus on electrification rather than green hydrogen. I think you'll find that WAE expertise in battery systems and electrification really complements FFI's green hydrogen capabilities and serves to further underpin FFI's technical leadership in decarbonisation more broadly. So, we see it as highly complementary.

Operator: Thank you. Your next question comes from Lyndon Fagan from J.P. Morgan. Please, go ahead.

Lyndon Fagan: (J.P. Morgan) Thanks very much. I was hoping you could maybe outline a bit more about the Gabon iron ore opportunity as well as the Sinosteel iron ore opportunity. I guess, more holistically, how does Fortescue plan on funding what appears to be two major iron ore projects as well as all of the FFI projects? I just can't really square it in terms of getting to the ambition of 15 million tonnes of hydrogen by 2030 on top of that, plus two iron ore projects. That was the first one, actually.

Elizabeth Gaines: Sure, well why don't I tackle that one. I think to create opportunity and growth, you've got to take these opportunities and do the studies. Do the work. We're very disciplined about capital allocation and we've demonstrated that consistently. But to not undertake this assessment, to not understand these opportunities is not the right approach. The ways of funding things can be varied. We could partner with others, as we have done with Iron Bridge and with Formosa, for example.

So, we're not constrained yet by thinking about how we're going to do it. It's more about what is the opportunity? Do the studies work? Understand that opportunity, how we can grow our iron ore business. I think it's in all our shareholder's interests for us to look at opportunities for growth. So, I think these are really positive opportunities to further develop and enhance our iron ore operations.

We've got first class iron ore operations and sales and marketing teams. This is a significant opportunity. How we fund that, once we've done that work, that's a separate discussion and clearly, we go into it understanding that that may require - we might partner with others.

There could be other opportunities but let's not be constrained yet by thinking about how we're going to fund that, let's understand the opportunity and the assessment of that opportunity where it fits in the timeframe, within the portfolio and at the same time, we're advancing on our strategy to diversify to a renewable energy and resources company.

Lyndon Fagan: (J.P. Morgan) I guess just to follow up, how do I think about dividends over the next five years? So clearly Fortescue will be in a very heavy investment phase. The payout ratio guidance of 50 per cent to 80 per cent, clearly 80 per cent is not going to be possible but I'm not even sure how 50 per cent is possible, to be honest. I'm just trying to understand, is there likely to be any renewed guidance on the dividend payout ratio in the lead up to the 2030 period? Thanks.

Elizabeth Gaines: Well, we're committed to our capital allocation framework, Lyndon, and that includes payout ratio of 50 per cent to 80 per cent. All of that would go into the mix in assessing those opportunities, where we invest and with earnings versus cashflow, there's opportunities to generate sources of funding for those opportunities that don't necessarily have to compete with dividends or payout of earnings.

So, all of that balance sheet capacity, partnering with others, I wouldn't interpret any of this as us looking to change our very disciplined capital allocation framework but also our policy of paying out 50 per cent to 80 per cent of dividends to shareholders.

Ian Wells: I'd add Elizabeth, that you have to think about the projects on their merits, Lyndon. So, you can't lock in all of this capital expenditure without the respective project return. So, what we've done, as Elizabeth said, was - have been clear on our capital allocation framework and we've got a pipeline of opportunities. You want to find projects that will fund themselves as opposed to the age-old challenge of, if we could only get the funding, this would be a great project. Which of course is the wrong way of looking at it. So, a disciplined pipeline of opportunities and a competition for capital at the end of the day. So, nothing new on that, other than the fact that there's a lot of opportunities that we've got.

Elizabeth Gaines: I wouldn't interpret that as a change to our dividend policy.

Operator: Thank you. Your next question comes from Robert Stein from CLSA. Please, go ahead.

Robert Stein: (CLSA) Hi Elizabeth. My key question today was based around the WAE acquisition and just the synergies between the battery electric systems and the hydrogen strategy. Because on face value with the move to electric locos and potentially battery electric applications in haul trucks, it appears that we're stepping away from hydrogen application in those areas of the business, which was a big selling point initially of the strategy.

So, are you able to lay out a little bit how those synergies between WAE and the hydrogen strategy play out just to give us a bit more of a feel for how this is on-strategy?

Elizabeth Gaines: Well, as I said, Robert, to bring green hydrogen and green ammonia to life, you need battery technology. So, we do see this as complementary, we're not abandoning it. There's a strong focus on green hydrogen and we think there'll be significant demand for green energy, both in our own operations for decarbonisation purposes but also as an export opportunity.

I think there's broad recognition of that ongoing and growing demand for green energy by markets like Japan and Korea so we don't see this as a change from our strategy and that's why, as we said, Fortescue's acquiring WAE to really facilitate our decarbonisation of our fleet. Even for stationary energy and for the charging of batteries and the like, you need a source of energy. That can be green hydrogen, green ammonia if we look more broadly at shipping and the source of energy.

So, it's not a change in strategy, this is complementary and really helps to accelerate and advance the developments across the FFI portfolio.

Robert Stein: (CLSA) Thanks Elizabeth, and then the second question I had was regarding Belinga and Oakajee. Given that these projects were ones that didn't quite get up last time or last boom due to the high-risk or the high capex nature of them.

I mean, last time Fortescue was growing, it was small enough that the incremental tonnes didn't really impact the business from a margin point of view_but now that we're getting to a 200 million tonne operator, adding big chunks of projects into the market, 50 million tonnes here, 100 million tonnes there, will start to eat away at your base business profitability.

I'm just wondering how you guys think about that internally, sort of keeping the existing business valuation up there when you're comparing capital allocation into new projects like a Belinga?

Elizabeth Gaines: Yes, well I think that gives us the opportunity to look at the portfolio, the demand from customers for certain products. Almost every day that we're mining, we're depleting our existing resource, so we're taking a long-term view on the future outlook of the iron ore industry. We're not necessarily saying we're developing all of these immediately. We've got a 36 month exclusivity period to study the mine and then determine how we might take that project forward. We've got a 12 month period for the Midwest.

So, this is about understanding those opportunities, where does it fit in the whole supply, demand universe and then from there, we can make decisions about how we might allocate capital, where we look at future growth. What we might develop within our broader portfolio of tenements as opposed to those that we currently have that maybe are getting further away, higher costs, higher strip ratios. So, this is about the whole portfolio approach to iron ore.

Operator: Thank you. Your next question comes from Hayden Bairstow from Macquarie. Please, go ahead.

Hayden Bairstow: (Macquarie) Morning Elizabeth and Ian and team. Just a couple from me on costs. Just interested - I mean, your AUD dollar costs are gone because you stripped out the currency shifts at 4 per cent. I mean, are we still waiting to see final details from the Government? I know you had the meeting with them yesterday but assuming they do open the border this half, is there going to be further cost pressure risk on having to have more flights and stuff like that to keep social distancing if all those measures are implemented?

Elizabeth Gaines: Good question, Hayden. I mean, we did that - was it last year or the year before? We've gone through those periods of extra flights, physical distancing. Now with the 100 per cent vaccination rates for anybody visiting a mine site, plus we do testing and screening before flying to a site. That's where we have to work with the relevant authorities and follow their guidelines but we're in a different position than we were two years ago or even 12 months ago when we didn't have the rates of vaccination that we currently have.

So, I guess times have moved on. Whether that extends to additional flights, Ian mentioned our COVID costs are running about US$0.15 to US$0.20 a tonne. That's if we have additional costs, obviously we'll have to wear those costs. I don't think that's the biggest part of our current pressure on cost, albeit we have to take that into account. Health and safety is our priority, obviously.

But the requirement for that sort of distancing with all the testing and everything else that we're doing, I'm not sure that it's as relevant as it was at the commencement of the pandemic when we didn't have those measures in place. I think more broadly, it's thought that diesel costs, ammonium nitrate, those external costs that really influencing on our cost outlook at the moment.

Hayden Bairstow: (Macquarie) Okay, great and just on the magnetite angle. I mean, I'm just interested to understand internally, has the thought process started to shift a little bit towards magnetite potentially being the more likely early green steel solution, hence you want to get some more exposure to that side of the iron ore market as opposed to your core business? Or is it purely just an opportunity to grow volume do you think? More longer term.

Elizabeth Gaines: Look, I think it's a combination of both. I mean it is an opportunity, as you said, to look at the portfolio and to determine where we invest our capital. But also, the opportunity is for green steel but we're doing some great work on our hematite science as well on the potential for green steel. So, it's not constrained just to magnetite. So, our thinking on green steel wasn't just centred around magnetite but certainly having the opportunities in the broader portfolio, we think makes some sense as we look long term.

Ian Wells: Perhaps I can add as well, in terms of the previous assessments on magnetite, it's been high capex and not necessarily getting value for the revenue side. Whereas the market, as we've seen, really for the last two or three years, the valuation differential on iron units and also then when you overlay that and it's part of the reason why the Iron Bridge project has better economics than when we first looked at it because the realised price is going to be better.

Then you've got the application of the technologies which are unlocking values within the Iron Bridge to other magnetite projects. So, understanding how that comes together and there's two key elements which change the project economics relative to perhaps - I don't know when the assessments were done but even if they were five years ago, that they're materially changed now on face value.

Operator: Thank you. Your next question comes from Lachlan Shaw from UBS. Please, go ahead.

Lachlan Shaw: (UBS) Hi Elizabeth and Ian. Just a couple of questions from me. So firstly, on Iron Bridge, notwithstanding great progress recently, is progress there ahead of schedule? I guess looking at it a different way, do you have some buffer or contingency in the timing for December production?

Elizabeth Gaines: Look, it'd be fair to say, Lachlan, that it's on schedule. I wouldn't say it's significantly ahead of schedule. It's on schedule so every day counts. Every day between now and December absolutely counts but the progress we've made, whether it's with the civils at over 75 per cent complete, the pipeline, the offload facility, that's all aligned with our expectations on progress so we are on schedule.

Lachlan Shaw: (UBS) Okay, got it. Thanks. Just a follow up then for Ian, perhaps. So, you've talked before about ultimately having the Iron Bridge capital structure 60 per cent, 70 per cent debt funded. Any indications on timing of - and nature of when you'll look to put that in place?

Ian Wells: Yes, no specifics on timing but yes, that's absolutely still on the agenda. It sort of goes to part of Lyndon's question on we've got balance sheet capacity, we drew the term loan leading into December and we've put that cash on the balance sheet, which will help us with funding our growth capex.

We were in the fortunate position last year of having such a strong market and we can fund our entire investment portfolio through free cash flow last year. So still on the agenda, Lachlan, but no specific timing at this stage.

Lachlan Shaw: (UBS) Great, got it. Makes sense. Then my second question, just a quick one, so realisations have been a bit soft recently. I'm just interested, are you seeing any indication from your customers that the market's looking to start to price carbon in terms of bigger discounts right now? Or is it still just a case the discounts today are cyclical, higher coke prices and plenty of low-grade iron ore in the market. What's your take? What are you hearing from customers?

Elizabeth Gaines: No, it's definitely the latter, Lachlan. It's nothing to do with the customers starting to price carbon or anything else. It's just it is cyclical. It's linked to steel mill profitability, supply, all the factors that we spoke about earlier.

Operator: Thank you. Your next question comes from John Tumazos from John Tumazos, Very Independent Research LLC. Please, go ahead.

John Tumazos: (Very Independent Research) Congratulations on the Sinosteel MoU. Is the Midwest Magnetite project just one project or is it an array of deposits? I believe Sinosteel has Jack Hills, which is 3.9 billion tonnes of something like 22 per cent magnetite, but there's another one called Koolanooka that's 430 million tonnes of 35 per cent magnetite and there might be 10 or 15 various smaller deposits. Some hematite, some magnetite.

So, could you just give us a flavour for whether it's a specific deposit or you have the right to choose among all of these wonderful things?

Elizabeth Gaines: Hi John and thank you for that.This does give us optionality as we do the studies to look at the broader project portfolio that Sinosteel has. Obviously, the MoU is looking at all of their magnetite and infrastructure project but as you said, there's a number of deposits there. So, it certainly gives us the opportunity to work with them and assess those projects.

If you think about the infrastructure that's required for transport to the ports, for example, it makes sense to link up those projects over a period of time, so it certainly gives us an opportunity as we work with them over the next 12 months to assess that opportunity across that broader portfolio that they have.

Operator: Thank you. Your next question comes from Glyn Lawcock from Barrenjoey. Please, go ahead.

Glyn Lawcock: (Barrenjoey) Hi Elizabeth. Two questions. Firstly, just Iron Bridge. There's some stories in the media earlier this year about you may be looking at outsourcing the fleet in contract mining. The US$3.3 billion to US$3.5 billion, does that include an allowance for the fleet spend?

Elizabeth Gaines: Hi Glyn. Yes, it does include an allowance for the pre-strip fleet so that one - which as per usual, it includes the fleet that will be required for the pre-strip activities before it transitions to operations. The reason that we're obviously considering that is we don't want to invest in diesel fuelled fleet when the opportunity is that if we look at the future of mining fleet, this is about aligning that capital investment. So, making a smart investment decision as opposed to buying more diesel-fuelled fleet when we're doing quite a lot of work around the mining fleet of the future.

Glyn Lawcock: (Barrenjoey) Any idea as to what that could save you on a capital front? Of the US$3.3 billion?

Elizabeth Gaines: Yes look, we haven't disclosed the make-up of that capital estimate but it's included in there for the pre-strip.

Glyn Lawcock: (Barrenjoey) Okay, thanks. Then just the second question. On the FFI, the capex you quoted today, US$744 million and US$1.5 billion for the half. Does that include anything for the FFI US$100 million to US$200 million capex guidance or is all FMG capex? Thanks.

Elizabeth Gaines: Ian, do you want to take that one?

Ian Wells: Yes, and that FFI capital spend is about US$70 million for the first half. So, the total capex of US$1.5 billion is inclusive, as that's group, and then in terms specifically of the FFI capex guidance of US$100 million to US$200 million, they've spent US$70 million.

Operator: Thank you. That does conclude our time for questions. I will now hand back to Elizabeth Gaines for closing remarks.

Elizabeth Gaines: Thanks, Harmony. Thanks everybody for joining us today. As you can tell, we're very pleased with that December quarter performance. A lot of activity happening across our business, and we look forward to catching up with you when we announce the half year results in a few weeks. In the meantime, stay safe, take care and we'll see you soon.

Operator: That does conclude our conference for today. Thank you for participating, you may now disconnect.

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