BHP

Financial results for the year ended 30 June 2018

Investor and analyst briefing Q&A transcript

21 August 2018

Questions and answers

OPERATOR: Your first question comes from Paul Young from Goldman Sachs. Please ask your question.

PAUL YOUNG, GOLDMAN SACHS: Andrew, I have a few questions on met coal and also conventional oil. Just looking at met coal, how confident are you that you can reverse the cost trend and actually achieve that medium term cost target? And then, also, looking at growth opportunities, have you the ability to actually accelerate projects, such as Blackwater and Wards Well? And then looking at conventional oil, some great exploration success recently. I'm just thinking, should you not look to increase your conventional exploration spend further post the sale of Onshore US? And then looking at the recent success in Trinidad and Tobago and now Samurai, which I note that your partner Murphy seems pretty excited about, what are the conceptual development plans for the discoveries at T&T and Wildling, Samurai and North Shenzi. Thank you.

ANDREW MACKENZIE: Okay. And that's a lot there. Maybe I won't answer all your questions to give time for a few others, but let me talk about met coal. Yes, we are confident that we can reverse the cost trend. Obviously, as Peter explained, some of the more difficult geotech conditions that we faced at Blackwater and Broadmeadow have led to slightly higher costs than we would have expected, but with everything we are doing with improving the reliability and the cycle time and the compliance to plan of our mobile operations, we believe that we can continue to creep our volumes at the same time as reducing our costs. And certainly if that means that some of our growth opportunities could be accelerated, we will choose to do so. It's a good discussion as to whether we should increase exploration spend. Of course, we are pleased that we are finding hydrocarbons. We think we're in the right place. But, you know, you need to analyse these things as you go along. You need to think about what it means for the geology. And there is an optimum pace. Obviously, the more successful we are, there is the case to increase our spend. And, of course, at the moment, we do have access to one of the cheapest drilling contracts, I think, to drill some of those wells in the industry as part of our counter-cyclical commitment to that. Conceptual development plans – look, we're working on them all the time. It depends on how connected they might be. We might want to do some that tries to establish that connectivity. We are going as fast as we can. But I've nothing to talk to you about right now.

OPERATOR: Your next question comes from Hayden Bairstow from Macquarie. Please ask your question.

HAYDEN BAIRSTOW, Macquarie: Just a follow up on Olympic Dam. I mean, just understanding your confidence in the ramp-up of those underground meterage targets you're setting yourself when they are, in my mind, reasonable aggressive. What's your confidence there and what's the variability on the outcome just as you go through that ramp-up in the next couple of years, given, Olympic Dam is clearly the lagging asset now, from a ROCE basis?

ANDREW MACKENZIE: Yes. Look, I accept that we have a lot to do to continue to build confidence in Olympic Dam, but this is something that we can really concentrate on now as an organisation since we've cleared almost everything else off our table other than just making the most of this tremendous portfolio we've now got. And so our attention is very much on Olympic Dam. We have seen, since we last spoke to you, a considerable improvement in our development rates at Olympic Dam in the Southern Mine Area and that, I think, has put our growth plans that we have for Olympic Dam back on track. You're right to acknowledge the criticality of that. We've also seen since our major shutdown, big improvements in smelter performance, but as we've announced in our announcement today, we're just assessing a small issue in the smelter – in the acid plant. But, yes, I think it's something that is really very important to us now to get right. It's the one piece of business that we want to get to the levels of return that you saw in Peter's slide what we're getting everywhere else now that shale has gone. And it will absolutely have the focus of the best and brightest in BHP to make that happen.

OPERATOR: Your next question comes from Menno Sanderse from Morgan Stanley.

MENNO SANDERSE, MORGAN STANLEY: Two simple questions, please. The productivity improvements of US$1 billion for FY19 seem quite ambitious even if you compare it to a very good second half in FY18. What gives you the confidence that you can deliver this type of step-up? And then, secondly, Escondida. Can you maybe give us a little bit more detail on what was proposed last week and the process from now, what takes place and when do you know if it's in the bag or not?

ANDREW MACKENZIE: It's in the bag. We've signed everything with the union. The deal is done. And it has been done on market. It's a tremendous achievement for the team. And we've secured some changes to the health agreements which means that we can provide better health support for the workforce probably at a lower cost. And we've also secured changes in work practices that will allow us to continue to drive productivity at Escondida to make sure it remains highly investable even though grades are falling. The productivity for US$1 billion – well, of course, we had a slightly higher ambition a bit earlier which we've had to, push out into FY20 as a result of the issues in coal I've already referred to and us having to deal with higher cost operations in order to produce the coal at Blackwater and Broadmeadow. But again, it's a bit similar to the comments I made to Paul, we are now firing on all cylinders in trying to improve the productivity, particularly of the mobile fleet, and the efficiency of our stripping and the signs are good.

OPERATOR: Your next question comes from Lyndon Fagan from JP Morgan.

LYNDON FAGAN, JP MORGAN: Thanks very much, Andrew. You've spoken a lot about the portfolio. Can we hone in a little bit on conventional petroleum. There's still quite a large number of assets in that division, a lot of which are small. What is your long-term vision for that portfolio; do you see it ultimately shrinking a bit from here to get it right, or do you think it is actually right at the moment?

ANDREW MACKENZIE: Well, we of course are facing a period of reasonable decline as the existing production ages, and obviously our exploration success and our success in Mexico is creating a number of possibilities for how, in the fullness of time, we can replace that production and reverse that decline, but there is a bit of trough in between that. Now, it's not absolutely essential that we fill that trough, it has to fit within the capital allocation framework. You know, we don't have particular targets for the size of particular businesses, it depends really on the options they generate and how they compete within the capital allocation framework as to which gets the most growth capital. So we like the business and we would like to keep generating options there. We have a fair set at the moment, and exploration shows one way to it and, clearly, I've said in certain circumstances we would consider some form of acquisition, but it's not critical for the strategy of the company.

LYNDON FAGAN, JP MORGAN: Okay. And just a second question. I will ask the Jansen question on this call: just wondering about the US$122 million increase in the budget there and any latest thoughts on trying to monetise a bit of that asset for shareholders, given it's still a drag on the ROCE curve?

ANDREW MACKENZIE: Okay. So that increase in budget is simply as a result of having to provide for what it will take to complete the shafts. We always said we would do that. We had assumed, in our initial budget for the shaft, that we would have made a decision at this point, which, as you know, we have deferred, and we are not in a hurry to make a decision about a project. In the meantime, we continue to work on the engineering of the project so that we can improve the returns. We're looking for a partner, which, of course, could give you early monetisation, and we're watching the market. But we're not in a hurry to make a decision.

OPERATOR: Your next question comes from Sam Webb at Credit Suisse.

SAM WEBB, CREDIT SUISSE: The first is with regards to capex outlook for the next couple of years, just under US$8 billion. How should we think about that given you've put a billion-ish into onshore petroleum. Should we normalise so that the number is effectively less than US$7 billion now? And then just to your comments around keeping within the US$10 to 15 billion net debt range – and putting the onshore proceeds to one side – can you talk around that a little bit. Should we expect at any time you expect net debt to go below that US$10 billion; will that manifest in increased returns coming back to shareholders? Thanks.

ANDREW MACKENZIE: I'm going to ask Peter to answer your two questions, basically, on the capex outlook of US$8 billion and our commitment to the net debt range. Peter.

PETER BEAVEN: So on the capex, we have guided the current financial year inclusive of onshore capex and we know that there's obviously not anything in FY20. We knew that and we're happy with that, but we've got projects that have been added – and they were great projects, so we're very happy to continue to hold that guidance at US$8 billion or less for this year and next year. I think that makes perfectly good sense. On the net debt range, it's US$10 to US$15 billion medium term. We think that that's the right number for us. We have a very strong ability to generate cash flow, obviously, in the current circumstances, but as we know also, in more difficult circumstances and, of course, we set that range in a stress-tested environment in our modelling. So we think that's the right number and so you should expect us to be at the bottom end of that range, given uncertainties in the world, but I don't think at this point in time we're expecting to see less than that range. At US$10.9 billion, we're pretty close to the bottom of it, so it's good.

OPERATOR: Your next question comes from Clarke Wilkins from Citi.

CLARKE WILKINS, CITI: Just the first question on Nickel West, how does that fit in the portfolio now? I know it's probably not the scale, but I think in a recent presentation it talked about extending the life out to 2040, so it seems to be getting there on life, but not the scale, so how does that fit within your portfolio thinking now? And also just on the cost inflation side, is there some cost inflation pressures returning? What are you seeing there and also has that had an impact on the capex side and is that basically remaining unchanged despite the US onshore assets effectively dropping out?

ANDREW MACKENZIE: When we did the South32 demerger, we retained Nickel West because we actually didn't feel South32 could really handle an early closure of Nickel West if markets had continued to deteriorate. Of course, markets have stabilised, and as you've commented, the team we put in to run that business not only reduced the closure costs, which now seem not as relevant, they've also made the asset perform much better and shown the possibility of an extension of its life. But while that's been going on, the whole world of battery materials has come to the fore and what I personally didn't appreciate at the time of South32 is that the nickel that's produced out of Nickel West is one of some of the best nickel in the world from which to make batteries, particularly for electric vehicles.

So that's obviously changing the marketability of it, but it's also giving us a window on the future area of battery materials, which we need to consider for our own strategy. So we're putting all that into the mix and, while we're doing that, we're happy to retain Nickel West for now, but it could go either way in the future and the people who run that asset are well aware of that. They don't seem the least bit distracted by it because they're doing a great job.

On cost inflation, well, we're seeing the usual things: diesel and steel, certain basic commodities, like, for example, sulphuric acid, but of course the first two and to some extent the third are things that we also make, and so we are not as affected by that on a net basis as you might think, although it will show up in the cost numbers of individual assets.

And then we're seeing sort of pockets of other inflation to do with the labour costs in parts of Australia. The shale business, which is soon to go, has seen a lot of inflation to do with fracking and drilling – but I wouldn't want to exaggerate that. There has been a bit of a margin reset as some of those suppliers have moved back into profitability and I don't think you should extrapolate that forever. So we're not completely at that phase of cost inflation, and with everything we see that's possible in productivity, we feel – and we're going to try very hard – we have a very good shot at actually matching that inflation and more so we can continue to drive our costs down.

OPERATOR: Your next question comes from Myles Allsop from UBS.

MYLES ALLSOP: On the conventional exploration, could you just remind me of the timing of when we're getting visibility on Shenzi or on Trion and the projects in Trinidad? And then, secondly, with your US$9 billion of free cash flow, what's your assumption for Samarco in there?

ANDREW MACKENZIE: Okay. I'm going to give Peter the second question, but on the first one, well, we're drilling a well in Trinidad at the moment and, after that, we have one more well to drill which is to further appraise the other gas discovery we have in Trinidad, and then the rig will go back and drill the first well in Trion, which is a part of the appraisal there, and that will give us more visibility of it. Obviously, we've got a lot of interesting information coming in around the Shenzi area – a previous questioner mentioned Samurai – and we're putting that all together at the moment. We're keen to be able to do something sooner rather than later, but as I said, in the answer to an earlier question, I don't have specific timings available for you just yet. Peter, on assumptions for Samarco and the US$9 billion.

PETER BEAVEN: Myles, I think you should expect on Samarco, the cash flows for this financial year are more or less in line of what we've been experiencing over FY18 and FY17. I think it's more or less about US$300 million or so on Renova, and then there's about US$100 million, maybe a little bit more, on other costs to support Samarco itself, working capital support, plus we have some cost inside of BHP itself. So it's in that sort of vicinity that we've included in that forecast at spot.

OPERATOR: The next question comes from Glyn Lawcock from UBS.

GLYN LAWCOCK, UBS: Good morning. Just two quick ones. On the productivity program, Andrew, just so I'm clear, are you walking away from US$2 billion number, or is the timeline just uncertain? And then the second one, just interested in your thoughts, and the Board's, when you sat down the other day to think about your dividends and capital management. You are now at the bottom end of your net debt range. By your own admission you will generate US$9 billion of free cash flow. So, by now, you're probably below the bottom of your net debt range, I would imagine, with the cash you've generated in the last seven weeks. How do you think about capital management, and buy-backs versus dividends, and why no on-market buy-backs now when you're probably at the bottom end of your range and it comes out of future cash anyway? Thanks.

ANDREW MACKENZIE: Well, there is a lot in that second question. I'm probably going to throw some of it to Peter. But on the first one, look, we're not walking away from the US$2 billion target. It's just going to take us a bit longer to deliver it because of the hit we took from the coal issues in the first half of this year. But as Peter said, once we're through that target, we intend to put all our efforts and all of our focus on using cost guidance, but we still own that target. And the deficit that we're acknowledging in what we can deliver this year is mainly on the volume side, and so we will absolutely deliver that volume, and deliver the remaining part of that target, but now in 2020 rather than in financial year 2019.

I'm going to ask Peter to handle the details of your second question, but I will just say to you that, as a company, our intention is to make decisions about a major capital distribution to do with the shale proceeds when we have the proceeds in the bank and when the board can understand that at the time rather than to pre-empt them. But Peter, you can take it over into the more detailed issues that Glyn asked.

PETER BEAVEN: As we do every six months or so with a clean sheet of paper when we think about dividends, and I will just comment on really the final dividend, which is just the same as we always think about it. Obviously 50 per cent is the minimum with cash, so that's a given. And what is left over at this point is 17 US cents. That's the additional dividend that is included in the 63 US cents we just declared. That totals about US$900 million or so, just a little less than that, US$850 million. So the first criteria for buy-backs with cash dividends is it has to be material, and secondly, it has to be value versus a cash dividend. At US$900 million or US$850 million or so, that's just not enough for us to undertake a buy-back, given the scale back. I mean, we've done big, big buy-backs in the past, and you still get 90 per cent scale back.

So for the amount of effort that we have to put in to that to get, you know, less than a billion dollars back to the shareholders, we don't think it's the sensible thing to do at this point in time. But obviously the US$10 billion, you know, that's a different kettle of fish. That obviously meets the materiality, and so we'll just assess the value of that in the way that we would normally consider investment, and we will take a look at that. But we can't make that decision until we've completed – well, nearly completed the deal. And that's 31 October. So we will make a decision before that. And what we'll have is a great opportunity which to hear from all the shareholders between now and then, and obviously that's going to be incredibly important feedback.

OPERATOR: The next question comes from James Gurry from Deutsche Bank.

JAMES GURRY, DEUTSCHE BANK: I see BP were in the press recently saying that they held discussions with you about the whole of your North American petroleum portfolio. You've definitely reiterated the strengths of it today. Can you discuss the best you can considering letting go of those assets, and perhaps talked a bit about the two assets that you're flagging a final investment decision in the next 12 months with Atlantis 3 and Ruby.

ANDREW MACKENZIE: So let me just deal with the first question, which is a very simple one. We didn't come remotely close to letting go of our conventional business. You know, we were selling our shale business. The board have made a very clear decision that conventional business as it is currently configured is core to this company, and it was not for sale. I don't have the exact times to FID on Atlantis 3 and Ruby, but I'm sure the Investor Relations teams can get back to you after this presentation and let you know.

OPERATOR: Your next question comes from Kaan Peker from CLSA.

KAAN PEKER, CLSA: Can you please provide an update on Trion given the recent government election in Mexico and also talking about cost increases in Queensland Coal? Given the cost inflation, can you please maybe talk about specific initiatives which will enable BHP to get back to that US$57 per tonne from the current guidance of US$68-72 per tonne? Thanks.

ANDREW MACKENZIE: I think I have already answered the second question in some of the previous questions, so in the interests of time, I will just talk about Trion. Look, we have not seen any consequences and indeed, the various commentary of the President Elect of Mexico are not particular cause for alarm for us in our work on Trion. We have a great relationship right now with PEMEX. We have been able to progress all the approvals to drill the well pretty much in line with what we expected. We have seen other opportunities to drill. And, as I said earlier, I think in about a few months' time, once we've completed our current appraisal program in Trinidad, the rig is going to Mexico – or the Mexican side of the Gulf of Mexico to start the appraisal of Trion.

OPERATOR: Your next question comes from Peter O'Connor from Shaw and Partners.

Peter O'CONNOR, SHAW AND PARTNERS: I wanted to follow on from the question about buybacks and, Peter, you made the comment that – I think it was about value and scale were two of the key factors you look at, and just to pick up on the value side of that. How do you take account of the value per share of BHP on an NPV basis, or however you think of the value of your business when you do a buy-back?

ANDREW MACKENZIE: If Peter has anything to add, he can do, but I think at this stage, we are very much in consultation mode. We're about to go on the road and talk to a lot of our investors. We're keen to hear from them about some of the criteria they might wish us to apply and whether we look at whether we return money through a buy-back or through a special dividend and the board really haven't started that discussion yet and won't start that discussion until we have all that shareholder feedback, until we have the money in the bank and then we will review things, so I'm reluctant to give you anything detailed there because, you know, we're still working on what's the appropriate way to do it. Have I missed anything, Peter?

Peter BEAVEN: No, that is fine, Andrew. I mean, we think hard about all of the way that we allocate capital. It's pretty consistent in how we do things, you'll be happy to know. And there's always lots of ranges that we think through, and when we get there, we will get there.

ANDREW MACKENZIE: So are there any more questions?

OPERATOR: There are no further questions at this stage.

ANDREW MACKENZIE: Okay. Well, I think given that, thank you for listening to myself and Peter. We've certainly enjoyed presenting these results. And we look forward to meeting probably all of you in the coming days. And we particularly appreciate those of you from the UK who have phoned up in the middle of the night. That's very nice of you to do so. So, thank you, again. And the briefing is now over.