Morgan Stanley virtual meeting transcript

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Introduction

ALAIN GABRIEL

Ladies and gentlemen, my name is Alain Gabriel, European metals and mining analyst and I am hosting BHP for an interactive Q&A session as part of our annual Cannonball Run.

Before we start, I would like to remind you of our important disclosures, please see the Morgan Stanley research disclosure website at www.MorganStanley.com/ResearchDisclosures. And without further ado, I would like to welcome Peter Beaven and the rest of the BHP IR team.

Today's session will last for a maximum of one hour, starting with brief introductory remarks by Peter, followed by a few discussion topics that we have put together. And then we can open up for questions from participants to be submitted via the webcast.

Peter, the floor is yours for some introductory remarks.

PETER BEAVEN

Thanks, Alain. It's been an astonishing few months. I guess we are used to cycles in this industry, but this one has been a little less usual than most. But in any event, we're very happy that the organisation has continued to operate very well through this period given the circumstances. There have been some impacts and we can talk about those in a moment. Our workforce has had instances of COVID-19, but generally has remained safe. So you know, we've been in a good place and we've continued to operate throughout.

And we have relationships with our governments and our communities and so on, and the results have also strengthened and we've had this sensation of really feeling as if we were all put together at the same time for the same thing. And you know, we have lots of discussions with lots of folks. But this has been a good period for us.

So at our interim results in February, Mike outlined his plans to really capitalise on the opportunities that lie ahead and I guess build on what we've already delivered, and just to recap, we’re looking to be even leaner and higher-performing across the entire company. We've done a good job, but we can get a lot more out of this place. We need to lower costs. We need to be more reliable. Plus we need to be more productive from the gear we already have. We have to be safe. We've had a really good run on safety, I don't think we've had a fatality for 18 months. I stand to be corrected, but I think that's about right. But that's good, we need more of that. And that becomes the standard.

And of course, what we also have to do is to create more options in future facing commodities. The world is changing and BHP needs to change, and the way it's going to have to do that is to create more options. And then actually implement some of those options, the best of those.

So to achieve that, Mike highlighted five specific levers: culture, capability, asset-centric focus, technology and of course capital allocation. And I guess we've demonstrated our focus on these through the COVID-19 crisis, and this also has in fact accelerated our work on some of these things.

Operationally and financially we've continued to perform well. Again, notwithstanding some issues and some impacts from COVID-19, it's not been completely plain sailing. But for the main, absolutely. And so the momentum behind our strong underlying operational performance continued into what you saw for the March quarter, and we've got nothing particular to say about what's happened, as you can see, in the quarter that we're in. They are not done with it and I haven't announced it, if we had to have something to say, we would have.

So for the nine-month period, we achieved record production in WAIO (Jimblebar), record production at Caval Ridge, record concentrator throughput at Escondida and record material stacked at Spence. So the big assets are performing. And of course, we did this despite the challenges of the weather in Australia, on both coasts. Queensland was actually hit harder I think than Western Australia, although there was a pretty bad cyclone that went over the top, more at Dampier than Hedland, but Queensland really hurt.

A lot of unrest in Chile, and of course the impact of COVID-19, both on our production but also on our demand side in some commodities.

So we've accelerated our multi-year efforts to make our functions more efficient and effective. This was our world-class functions initiative. We actually started this when the sun was shining. And that's a hard thing to do when, we did a zero-based budget initiative across the top of all of our global functions. And if there isn't a sort of a burning platform, it's tough for people to accept that psychologically. But we did, and more than half way through it, and we're really happy we did that. So we don't have to then implement some form of that in the COVID-19 crisis that really turns the place over - and it probably doesn't end up with a particularly good result once the dust settles.

So when you combine that with the changes already underway in technology, we would expect to reduce overheads by well over half a billion dollars by 2021, relative to last financial year. So that's going very well as well.

So as I say, operationally I think all are running well, but we are navigating major demand and price uncertainty in some markets. But of course we do continue to sell all our products and payment performance has remained incredibly strong. And so this shows the advantages of having a diversified portfolio, high-quality products, and having good relationships, strong relationships with our customers, and actually having very good customers too. I mean, they have performed very well themselves.

The way the stimulus has gone a long way to just cushioning the damage to economies and to commodity demand. It will of course help support a faster recovery, and happy to see the green shoots of the relaxation of some of the COVID-19 restrictions around the world. But other than in China, where a V-shaped recovery appears to be underway, we think the recovery elsewhere will be more protracted in other major economies.

Re-establishing the billion-plus livelihoods that have been disrupted will of course take time and consumption will be constrained. The likelihood of a V-shaped recovery measured in quarters is very unlikely. I think that's very clear at this moment other than like we said, in China. But we are seeing some recent signs of reopening in Europe and US, and even in India. And so by the end of 2021, our base case has the global economy around 4% smaller than it would otherwise have been.

In terms of commodities, we think that if China can avoid a damaging second wave, and obviously we have read about Beijing, but at the moment it looks like that's happening. So we expect that Chinese pig iron production has the potential to actually grow slightly this year. But in the rest of the world, we'll probably experience a double-digit decline.

The diverse performance of iron ore and met coal is actually quite easily explained. China is the main game on the demand side in iron ore, while met coal is much more diversified. So lockdowns in Europe, India and Japan, Korea, have had a major impact on the demand for met coal.

Copper demand ex-China is also expected to fall, but it will be less severe than steel ex-China. And with the epicentre of the COVID-19 outbreak now in South America, we're seeing the impact on the supply side. And obviously that is probably with a risk on sort of mentality for the traders. Those two things are providing a degree of price support to the copper price we see today.

Demand for all products is expected to begin to recover in line with the easing of mobility restrictions. Certainly you can see that in the US. But no question the level of demand is unlikely to fully recover, before the end of the next calendar year, 2021.

So what hasn't changed are the fundamental underlying demand drivers that underpin our view on investments, and the global appetite for the commodities we produce in the long run. It's too early to really say what the longer-term impact, frankly if any, is of COVID-19. It certainly, as I say, the main GDP drivers are population growth, urbanisation, industrialisation, increased standards of living, and climate and these remain the same.

There's no doubt we have some uncertainty, but we are very well-positioned. We have built a balance sheet that can support both offense and defense. It's performed extremely well in these last few months. And we streamlined our portfolio. It's not limited to shale, and I've lost count how many billions of dollars of assets we've sold in the last 5 years or so, 10 years even. And so our portfolio is relatively small in number but it's very high quality and very low cost.

And of course with the combinations of those two things - good balance sheet, great resource base, we can continue to invest through the cycle and to continue to grow long-term value.

Then in the current environment, of course, we're looking to see where it makes sense to defer projects for value. Our strategy is not a balance sheet but if there are opportunities to delay things, and that means that the value of that project in fact is higher, then so we should do that. And of course, there are in fact some direct impacts from COVID-19. We have not been able to get all the people we want, ordinarily, to site to complete projects. So that's those two things combined will mean we are in the process of reviewing our capital expenditure guidance for the coming year. And we'll obviously have more to say about that when we get to our Results in August.

Petroleum is a good example of where we see this in action. We've deferred making a final investment decision on Scarborough until the middle of next year, and we also have flexibility to reduce exploration spend next year by around US$200 million. That would be a third of spend over recent years. Some projects have shorter life cycles, and in fact we can increase the value of that project by shifting that production to when we anticipate stronger prices.

What we said is that group capex financial year 2021 will be lower than previous guidance of around US$8 billion, and as I said, we'll provide updated guidance in August. I think it's also worth pointing out that FY21 capex guidance will reflect some capex that will have been pushed from financial year 2020 into 2021, that's obviously primarily COVID-19-impacted spend. For example there's been some impacts on SGO (Spence Growth Option). And eventually the capex that we defer in financial year 2021 will get pushed into financial year 2022, and so on. I doubt really that we're going to be cancelling projects in a major way. This is simply deferring to the right most value accretive period.

So to sum up, we've got strong momentum in operating and financial performance. And in fact, that's continued through the pandemic. We've got a simple, diversified portfolio; large, high-quality assets; the balance sheet remains rock solid; and our capital allocation framework is specifically designed to balance returns to shareholders and continued investment at all points of the cycle.

And of course, we're in an industry which continues to operate and support local communities and economies. We're in a very privileged position. But you know, we did a lot of work to put ourselves into that position, too. And so with our strong financial position and low-cost operations, we're pretty confident we can continue to generate the very solid cash flows and returns for shareholders through this period.

With that, Alain, I'll pass back to you.

Questions and answers

Please note some questions and answers have been removed as not relevant to an update on the company or company performance.

ALAIN GABRIEL

Thank you, Peter. That's quite comprehensive. So if we may start with the COVID-19 pandemic. So from your introduction, it seems that BHP has fared quite well through the crisis. However, where do you see the biggest risks to your operations from today's perspective onwards?

PETER BEAVEN

Yeah. I think we have done well. I think that the big assets have continued to really knock out some really great numbers. And on the balance sheet, you know, it was designed exactly for this. And we simulated and stress tested. Of course we do. And so whatever happens, you know, we just run the same numbers, more or less, than we've been simulating which is now appearing on the screen. Different cause, it has to be said, from the simulation that we had in mind. But that doesn't matter because the numbers turned out to be the same. And the balance sheet did exactly what we thought they would do, and so that was really very important. But not just in terms of net debt, but also in terms of liquidity.

So you know, I think the areas that we will see the impact of COVID-19 is always a combination of what we do and what the country does. So of course in Australia, it's a well-organised place. Saw COVID-19 coming quickly, early, and really reacted I think very appropriately across both the Federal and State governments. State governments have very strong roles to play in the system here. And so the combination of those things, means that from the production side of things, have seen relatively muted impacts on our assets in Australia.

There has been some impact, for instance, hot seating out of trucks, for instance. You have to stop the truck and normally you would just put one driver in after the other, and you'd minimise the break. But in this case, you have to get it cleaned and so on, which means the truck is out of action for, you know, whatever it takes, 20 minutes, half an hour to get the truck cleaned up and so on. And that has impacts on production. The other part of it is the demand side, gas demand for example from Bass Strait and Trinidad as well. Same impact. Just haven't been there to the extent that we would have ordinarily been, and so there has been some impacts on that.

I suppose the biggest impact is really in Chile. Chile as a country did a really good, great job in the beginning. The numbers looked pretty comparable to Australia. But unfortunately, the way that those cities are set up, people are in very close proximity, and so on. And so the lockdown that they initially went through just wasn't particularly effective and so what you're seeing now is some very, very severe numbers coming out, the hospital system's under a lot of pressure. They have added a lot of beds. They've added a lot of ventilators and increased the capacity of ICU, but I'd say it's under quite a lot of pressure. And it's across Santiago, the metro, but also across Calama, Antofagasta, and Tarapacá in the north and Iquique.

And so you know, I think with that we're still in quite a lot of stress there. We've taken 30% to 35% of the people off the sites for various reasons. And so that level of absenteeism is having some impact and will continue to have some impact. We haven't provided updated guidance on that but we expect to do that in July. But even that guidance will be somewhat uncertain, depending on how the circumstances turn out there.

In petroleum, as I would say, other than on the demand side, I don't think COVID-19 has really had a major impact on us.

ALAIN GABRIEL

Okay. Thank you. Very clear. And what have you learned from this pandemic, and how do you plan to integrate this learning in your business? So in other words, how will a post-COVID-19 world look like for BHP, and what long-term megatrends do you expect to accelerate?

PETER BEAVEN

I think from BHP's perspective, the thing that really helps is having a single purpose, which is for all of the assets, for all of the functions. And in that moment of crisis having everybody finds out if they work exactly for the same thing at the same time under very constrained timetables, they can knock out extraordinary things. Now, we ordinarily do some pretty decent things but this has really been, again, just an amazing set of outcomes for us. And I'd really encourage everybody to remind folks about added productivity and so on. I have had these questions for five years now - “you must be out, you must use nothing more, there's nothing more”. There is more, and it's because if we really get the full weight of this organisation set behind fewer things, then as I say, we can knock amazing things out. So that's sort of the way of working here, is what we have to preserve and take thought.

In terms of COVID-19 and the impact on the world, there is literally rooms full of paper now written on this. We had a good discussion with our Board the other day. My sense of this personally is that there will be a couple of things that you can guarantee, I suppose. Let's start with those things, one of which is that there's going to be a massive bill to pay. And so you know, government, so the monetary authority is out of gas but the fiscal lever is getting pulled to a greater or lesser extent. But to most countries, to a great extent. And somehow that's got to be paid. Does it get paid through increase in fiscal take, does it get paid for through growth, with some inflation. You know, those are the sort of uncertainties that we'll have to face.

But for now, you know, since our relationships with our governments are very cooperative, and I think government, as far as we can tell in our production side of things, it's probably clearer in Australia than it is in Chile, for instance. But the government here appears to be focused on growing the economy, and a major fiscal reform doesn't seem to be at this moment on the agenda. But you know, things can change very quickly. And we'll still see what the stakes have to come up because the stakes are really where we pay royalties.

I think the other thing that will be, which seems pretty obvious, is that, whatever you think about how we got into COVID-19 in the first place, China is coming out of it quicker, and even more aggressively than it was when it came out. And so it's a trend, like most of these COVID-19 trends, I think they're not new trends, they'll just be accelerated trends. So I think that, for us, we sell more than half of our product into China, and so that'll be something that will have to be really nimble to see how to navigate that successfully.

Of course, for every risk there's an opportunity in that so you know, if China continues to promote its infrastructure and so-on, that creates a lot more to monitor our product. I would say it's a very complex issue. But there's no question that that trend is underway. I think the other one is really, a big one would be climate. Climate is here to stay. I think it's a much bigger deal than COVID-19. And I think it will be complex, and it'll be different. Some places, the fact that there's a big bill to pay will mean that countries will be less interested in pushing climate agendas.

I noted yesterday that I think the Chinese government just re-graded the head of environments, I forget, it's called ecology and environment, so whatever ministry, to a non-party official. And that generally means it's less important. And so for all of the signs that come out of Europe about, you know, we're going to have a green revolution as we recover out of this, and so on. Again, as always, with these sort of pronouncements, you're never sure exactly what that actually means. But for sure, I wouldn't be surprised if in some places the green agenda will be accelerated by COVID-19 but in other areas, in fact, it'll be held back. And so you know, we'll wait and see.

In any event, context as that is, I think we just keep coming back to this and basics that are going to drive the world in the future, those are big, secular changes. And we've got a lot of conviction around those things. And it is going to be a big the world in ten years' time, 20 years' time, particularly because of climate, is going to be different. And we've got to adapt with it.

ALAIN GABRIEL

Okay. Thank you, Peter. And I guess you have been talking about China, coming back in a meaningful way, Chinese demand. But you also made comments to the press about the expanding your iron ore production capacity. What is the rationale of that ambition, and are you not worried about Simandou or a race to get market share by your competitors?

PETER BEAVEN

Yeah, absolutely. We obviously had a position ourselves in West Africa, so we have first-hand knowledge for 20 years or so. In fact, we sold that. That division was relatively small and it's essentially in a world biosphere, so you can imagine, that makes our life a little bit more interesting given the standard that we hold ourselves to. At any event, that's us.

But Guinea is no question. I mean, that's very high quality product. There's billions of tonnes of it particularly in the Simandou blocks. And of course, it'll find a home in the market in the event that it gets to market. The folks who are putting together a consortium, they've got a track record of Guinea. They've been producing bauxite for quite some years, and I personally I think that thing is underway. And you know, I think it's going to have an impact, no question about that, if there is the initial phase, it always tends to be that way, you know. You put in the infrastructure and of course that's the very expensive piece. I mean, the initial economics of that, that first stage, would be way beyond us by glancing at the numbers. Way beyond us. So that would never be something that we could justify through our capital allocation framework. But if others can, and are willing to do so, well, fine. We're just going to have to live with the consequence of that.

Of course, once you do it once, you could do it twice, and three times. You could very easily do, say, billions of tonnes of the material there.

So I won't lie to you. I think it is a concerning development from a price perspective. And you know, what can you do about it? I don't think we should try to get involved in it because that would destroy value twice over, in the project as well as potentially in our own Western Australian iron ore position.

But what we've got to do is just be ready for these, if it does come and it does have an impact on margins, of course what we have to do is just keep ramming our costs down, making our quality better and so on. So speaking on South Flank which increases the quality of our product suite, quite materially, as well as continue to do what we've done so successfully over the last few years which is reduced costs. As you know, we're now the lowest cost iron ore producer, not comfortably on FMG but compared to the rest.

And as I say, we continue to do better every day on that score.

ALAIN GABRIEL

Thank you. And there's a related question that came via email on your expansion to 330 million tonnes. This is what you have mentioned previously. Do you think the market needs these volumes, and what infrastructure would you require to build or to achieve that level? And what would be the potential Capex and timelines?

PETER BEAVEN

Yeah, Alain, I wouldn't get too excited about us doing that next week. I mean, we've got a licence to 290 million tonnes, and that's all we can do at the moment. So if we ever wanted to really fully utilise what we've got in development in our system, we're going to [need to] get licenced to go beyond. And so that's what we've applied for. And you know, it's typical in resources that people [take] years and years to get licences. So you want to get well ahead of that. And you don't have to do anything about that, you just put it in your pocket if you need to.

So really that's what I would say, it's hard to think through that. We'll get to 290 million tonnes. There is additional de-bottlenecking that we will get, naturally, through the rail, what we call the RTP - it's a new signaling system. We'll be able to run a lot more trains on the same line. So we'll get that in the next couple of years and then it's the port-rail interface that needs to be de-bottlenecked. And it's a series of relatively small things that need to be put in place in order to squeeze up to probably the 330 (*correct number is 290) million tonnes.

Beyond 330 (*correct number is 290) million tonnes, you start to think about putting in another car dumper and you know, maybe you start to talk, I don't know, probably US$700, US$600 million worth. But you know, none of the amounts here are particularly material, as far as you say the question is, does the market need the tonnes.

At this point in time we just feel like getting ourselves reliably to 290 million tonnes and then we'll see what happens. But yeah, we should have that in our pocket because who knows what will happen.

ALAIN GABRIEL

Okay. Very clear, thank you. And staying good with iron ore, I guess, there has been a lot of coverage lately of the destruction of an old Aboriginal heritage site in Australia by one of your peers. Will there be any implications for your existing production of 290 million tonnes, and the South Flank project?

PETER BEAVEN

Yeah. The things, they tend to be a bit complex. The short answer is no, we don't expect any impact on our production or on South Flank. You know, the way the thing works is that, at least South Flank, you know, we have comprehensive agreements with the Banjima who are our traditional owners in that area. There's about 600 of them. And we've had agreements and we've been working with the Banjima for 30 years. We've had a comprehensive agreement with them on South Flank since 2015. This thing runs to, you know, 200, 300 pages. And it took 10 years to negotiate, so you know these are very, very, very detailed pieces of work which go through all of the implications of a development such as South Flank including a massive exercise to go and gather and understand what all the sites of cultural significance are and listing those all out, and obviously it is done in conjunction with the Banjima. It's not by any stretch, it's not a unilateral thing.

And then there's an agreement with the Banjima in that to preserve things which are particularly culturally sensitive. We obviously do whatever we can to avoid destruction of any of those things. But to the extent that some of those areas are on mineralisation, then we specifically have those listed and that is agreed with the traditional owners as to whether we can or cannot disturb those things. And then that agreement is then the basis of what we then put to the government in WA to say that these are what, they're called the Section 18 exclusions, or approvals, to disturb traditionally-owned land.

And the government has to, and the minister has to, sign off on those things. Now, we make the application but because we have this comprehensive agreement with the Banjima, they agree alongside us, and confirm in writing to the government, and so on, that they won't object to any of the applications that we have made under the Section 18. And on the basis of that then the minister provides us consent to disturb the areas that we've listed and agreed to the Banjima.

So that's the basis of our operations, that's the basis of South Flank. That isn't the end of it, and I know because I operated in manganese for five years and we had similar arrangements for a manganese mine in the Northern Territory. And so you can have these agreements and they are comprehensive. But they're actually living documents because the relationship with the traditional owner is a living thing. So the traditional owners will have a view on something but they have complex societies and of course over a long period of time because these mines are like 30, 40, 50 years, they're subject to obviously changing their minds, having different views, and so on. So what you have to do is not, like all contracts, you can't just put it on the shelf and say, okay, there it is, I got the approval for this. And on we go, sort of thing. You have to have that relationship every day with the folks and you have to take into account the fact that they will change their minds on things and they have every right to change their minds on things. And you've got to keep that day-in and day-out conversation.

So in the event that they come to you and they say, okay, well, here's something which we feel is particularly sensitive, but that we already have provided the consent through the comprehensive agreement to disturb that, then you have to simply take that into account and go back to work and essentially renegotiate this thing.

And so that's the subtlety and the complexity of this thing, and we have a very large set of folks in our organisation, that's their job. And as I say, to this point in time our relationships with Banjima have been excellent we don't see that this would change in any way.

ALAIN GABRIEL

Okay, thank you. Shifting gears to your Petroleum business, and this question is in the context of ESG investors. How does this business fit in the complex environment where investors are increasingly pushing you for a faster progression to fossil-free?

PETER BEAVEN

Yeah. I think there are some investors who push for that. I think this whether we should or shouldn't be in a commodity is -- you've heard me say this, or some of you may have heard me say this many times. But you know, it depends on whether we are able to make money out of that, that commodity, make good returns for shareholders and if we are the best owner for that particular asset. And so whether we can make money out of something is defined very simply, by saying: do we like the commodity, can you make money; is there rent available; is there growth available in the commodity; is it large?

Secondly, do we have great assets, are they well-positioned in the cost curve, can you expand them, can you build them, can you expand them in a capital-efficient way?

And then thirdly, do we have the right capability to run those things, at least as well as anybody else?

And then if you can put those three things together, it tends to be that you make money in this industry. It's not more complicated than that. And so whether we have a commodity or don't have a commodity, we do or don't have an asset, that's the lens that we look through. So in the event that we think that we continue to make money out of petroleum, for instance, because there is rent available, because we've got great assets, because we can expand those things and we have the right capability, then that passes the first and by far the biggest and most important hurdle.

There is a fourth hurdle, which is that you need to be the best owner of this asset. Now, we freely acknowledge and we test all the time. It's like okay, fine. We can say, one, two, three, good asset, good commodity, good capability. But it may well be that somebody else is a better owner of that. So we could have a set of shareholders that was more appropriate to the risk and return, and we'd value that more, more highly frankly, or another company would value that more highly. And so that's the lens. That's the basic framework, the strategic framework lens that we put against petroleum and in fact, any of our commodities.

On top of that of course, we don't live in a bubble. We also live in a world where everybody else has a view on what we should or shouldn't do, and so on. And of course, that is becoming very much a part of the daily commentary that has always surrounded BHP, but even increasingly so. And so we have to take their views, essentially activist views, into account as we make these decisions.

But as far as petroleum is concerned, we think that there is no question that there is big transitions underway for the demand side of oil in particular. Gas also but probably on the other way. We have modeled very, very aggressive penetration of EVs and so on, but there still remains a large and the majority of the demand for oil is very hard to abate. And none of those initiatives are underway at this point in time.

And in addition, there is ongoing field decline as we know, which is you know, between 3% to 5% maybe every single year. So you put those two things with the growing population and higher living standards, and of course, we all know, one-third of the Capex of this industry just got wiped out in the last three months.

And so I think it'll be a little premature to say that the oil and gas industry is in terminal decline and you can't make money out of this thing.

So I think we'll continue to be a bit thoughtful about this, more than a bit thoughtful about this. For having said all of that, no question, you know. Having as we always do, we've been in oil and gas for 40 years and for every one of those 40 years we've been having this discussion around does mining and oil and gas go together, shouldn't you sell it, and so on.

All I'd say is that's fine, that's normal for us. We'll continue to actively think our way through that, and continue to just remind people that some of the very best returns in all of the businesses we've got have come from and continue to come from our oil and gas business, and certainly the highest EBITDA margins. And we've got a number of very good growth projects that sit in front of us. So we'll see how we go but there's some thoughts on that.

ALAIN GABRIEL

Okay. Thank you. That's very clear. And staying with the ESG, you have recently switched from coal-fired power to renewables at Escondida. Where do you see the scope for similar switches within the rest of your portfolio?

PETER BEAVEN

Yeah, look. I think that model, outstanding model, which we have to do quite a lot of work on ourselves because you have to create a stable grid, so the Kelar gas-fired plant that we put in, or we caused to be built by the Koreans, I think that was an incredibly important underpin. But when you put together, I think, what we have done by building/ causing Kelar to be built, to stabilise the grid, to put our tender up because you know, we're about what, 10% of the power demand in Chile, the Government has had some excellent policies to interconnect the southern and northern grid and really bring hydro, again, as a point of green stabilisation into the northern grid. And then of course the wonderful sort of efforts and progress that the renewables industry has brought with its capital. Very, very low cost of capital, to reduce costs.

You put all those things together, what it means is that as you say, Alain, we can completely switch out of what was, just what, seven years ago it was completely coal-fired power that we sourced into Northern Chile, into completely renewable, with a stable grid, with much lower costs. So it's the magic trifecta that so many countries warble on about, and how to do it, and so on. We did it as a combination of companies, and the government in Chile.

And so I think it's an important lesson, really fascinating case study for how things can be done. So we are trying to do that here in Australia, East coast is really where we're going to. We'll probably take a couple of bites of the cherry, and because the grid is going to have to take a little bit of time to adapt and so on. But some of the elements are in place here. West coast is going to be a little bit more difficult because we have much more isolated sites, and so there's not sort of not a natural grid as it appears here in Eastern Australia.

And so those are the sorts of things that you will see appear as we really take care of our scope 1 and 2.

Scope 1 and 2, the things that we really want to get after and it will be of course to fix power, as we're discussing. The second will really be diesel and removing or mitigating as much diesel as possible - on production sites, on mining sites, but also on freight. And so switching our freight over to LNG in the first instance.

So lots to do but I think it's very important for us to talk about Scope 1 and 2. You can have all the aspirations in the world and all the highfalutin slogans and all the rest but you better have a real plan to sit behind that and the projects that are starting to come to life, and so on. And so that's certainly what we are very much focused on across the organisation.

ALAIN GABRIEL

Okay. Thank you. Very clear. And staying with ESG what is your strategy regarding your thermal coal business? Is there an exit plan and what sort of timelines should we expect?

PETER BEAVEN

Yeah. I mean, this little thermal coal thing *[(*refers to EBITDA contribution)* which always takes up so many minutes of all of these meetings. But anyway, look. We've got two very good assets. I think Cerrejón is very difficult to sell in a clean way because of the joint venture. It's not impossible but it's a complex thing for various reasons. New South Wales Energy Coal is a little bit cleaner as it is 100% owned. But there are a large amount of tax losses that associate with it which would otherwise be stranded. So we've had tremendous returns out of New South Wales Energy Coal over the last three years and we've been chomping those huge tax losses which in fact associate with some S32 companies, that have got left behind in the complexity of this [demerger], not by accident, because it was pretty complex, trying to put into S32.

And so we've been very happy with the returns in New South Wales Energy Coal over the last few years. We've been very clear that if anybody wants to make a cash offer for those things and they are for value, then you know, we're more than happy to sell it. We've received a bunch of offers. Honestly you know most of them have been pretty disappointing relative to value, and you would hope and expect that we would look after value for shareholders. So that's what we've been doing. But it's safe, you know. If we get good offers, yeah, why not.

And just one thing I'd just say on climate and maybe this is a personal view on this, but you know, this idea that if it's got carbon it should go, well, I live in I think a rather more pragmatic world that says if your objective is to remove the carbon that they produce from the world, well, then you will fail completely. If these assets are good assets, they're not going anywhere. They just change ownership. And I certainly subscribe to the fact that BHP should have those assets, you know, and owned by companies that are more responsible, more transparent, and you are genuinely delivering against the objectives of reducing us, our Scope 1, 2 and 3 emissions. And it is not just disappearing into the shadows where nobody can ever see these things ever again.

And so if we are to make significant impact on decarbonising the world, wishing these things away by not seeing them in the portfolio of a particular company is probably not the best way to do that. I find that, it's intellectually reprehensible, honestly. We've got to have a more adult, a more constructive debate than that.

ALAIN GABRIEL

That's very true. Very true. Thank you for that. I guess the next question is on the broader strategy about your thoughts on the DLC structure. There has been lots of debate and discussions historically but it would be good to have your thoughts here, especially after the announcement that we have seen a few days ago from Unilever, for example.

PETER BEAVEN

Yeah. Interesting one. I guess Unilever got it right the second time …. with the focus on getting the deal done …. You've got to be pragmatic about these things.

Now, we actively consider what the DLC is for us. You know, I've said many times, the thing doesn't actually cost us anything. And actually has got a lot of benefits because it really streams the franking credits that we produce here in Australia to the folks that can really use them. And so that creates an efficiency in the pricing and so we don't see that, that dual pricing out of LTD and PLC as an issue. We see it as just an efficiency.

But having said that, we don't have the luxury that Unilever has of choosing either collapse if we ever wanted to collapse. We don't have the luxury of choosing whether to collapse into Australia or into the UK. The Australian government, when Elliott turned up the first time and it said we should collapse the DLC. Elliott, if you recall said, we need to collapse into PLC into London, and here's the reasons why, and share price will go up by 50% (or something similar).

Look, anybody who lives in Australia will understand that that is never going to happen. In fact, the minister of finance here, the Treasurer, recorded a little video which he then put on a Twitter feed to say that if Directors are considering collapsing BHP into the UK, then we have an agreement with BHP under the foreign investment review rules (* *which means the Head Office needs to remain in Australia*), and we would hold them accountable for that. So the Board of BHP would be accountable in the event that they agreed to what Elliott was suggesting. But in any event, we were rejecting Elliott's perspective.

But just to give you a bit of a sense of again, what it's really simple reality for those of us who live here in Australia.

So I don't know how that was put in, if we would just collapse into Australia, how that would fit into it. Certainly if the lookalike narrative with Unilever is put on top of BHP, it would suggest that that might be a little bit more difficult. But there's many, many aspects to our DLC which are not common to Unilever's, and that's to say, it's not hurting us in any way. So on we go. So it's not the highest priority thing for us to deal with compared to all the other things we've been talking about.

ALAIN GABRIEL

Very good, thank you. I will take a pause here and switch, because there's some questions that have come through the email and the webcast. So just give a chance to go through these questions. So how did the current economic crisis shape your thinking about Jansen, what are the milestones of that project and any strategic options that you are contemplating at the moment? And do we still expect a decision by the first calendar quarter of 2021?

PETER BEAVEN

Yeah. I'd say that Jansen fits into that category where I talked earlier about how we're thinking about capex and so on. I think potash is clearly an oversupplied market. And so we expect great conviction that the market demand continues to be as it has been for many years, very strong. Of course that will use up all the available capacity that's around, including all the latent capacity and the brown field capacity from everybody who claims to have it, and so on.

And there will be a gap in the market but you know, this year is probably just the year that just goes by, the world does nothing, right. The year is gone.

So if that has happened then that probably means that that supply-demand gap that we were looking for probably also eases out and we don't want to ever put tonnes into markets that don't need them. Again, as per the conversation we said earlier about iron ore.

So in the event that it was better value for us to delay Jansen, we should do that. But that would be the reason. Ah, yeah, and there's also some impacts of COVID-19 on the current shafts completion. We've had to de-mobilise a lot of workers, again, for health reasons. Probably hard for people, we've had to de-mobilise. So that'll certainly have an impact on the completion of the shafts. That's just the sub-component of the overall project. But you know, we still think the fundamentals and products are really good. We still think the project is very good. It'll have, you know, a very long-term future. There's very few times that you can get a basin and dominant position as we have in potash, low cost, in a growing commodity, a large commodity. And that happens once in a generation if you're lucky, you know. That, in the way that we got position, base and dominant position in Western Australia, in parts of Chile, our corner of the Gulf of Mexico and of course in Queensland. So yeah. We'll see how it goes.

ALAIN GABRIEL

So I'm guessing the timeline for calendar Q1 is likely to be delayed, given all these circumstances, no?

PETER BEAVEN

Yeah. I'd say that's probably the likelihood for those various reasons. How long - we're not exactly sure. But we'll come back with guidance in August as we work our way through everything.

By the way you know, we haven't updated our guidance on Capex and so on. Just a quick comment on that. Look. This isn't a company in crisis. We don't have to run around in small circles and do U-turns. I would say, you know, we've been planning for these types of crises, simulating them for many years. The balance sheet's in good shape. We've absolutely knocked our project suite into the shape that it should be. These are good projects. They are projects which are designed again to be good through all the cycles and so on. We really went to town on getting our costs and our overhead and so-on done, starting two years ago when the sun was shining. So there's no need for us to turn around after three weeks of quick analysis, to say okay we're going to turn the whole place upside down. We are absolutely aware of what the issues are and the impacts and so on and we're going to take action against those things. But it's a calm place, as it should be. We continue as I say to perform very well.

ALAIN GABRIEL

Thank you. That's very clear. And another question via the webcast is how much coking coal are you selling into China today, and how much risk is there of an Australia-China tensions slipping into iron ore?

PETER BEAVEN

Yeah. You know, the biggest customer we have is India, in fact. And then for us the biggest customers there are really Japan, Korea, Western Europe. And for now, the market is struggling in those rest-of-world markets. And so really the clearing house for quite a few commodities and met coal is one of them, is really China. And so we've continued to sell our met coal and that's fine, and we've probably got about what, I think we've got some green shoots coming in, I'll say, in the Western part of India, JSW group is starting to unbank some of their steel furnaces. Western Europe probably going at about 50% utilisation. Not so much to see in Japan or Korea at the moment, but those things are coming. And at the same time we've got good, strong demand for that coal because of course we needed the highest quality met coal which China hasn't got an abundance, or a lot of, coal. But certainly the PLV that we sell is in high demand.

And in particular because there is a very high arbitrage, probably so what are we selling, US$110/t, something, of that order into China at the moment for PLV. The domestic price for that equivalent PLV is probably US$160-170/t. So there is a big arbitrage if the trade is and if the customers can get a hold of the material, obviously they want it. But there are restrictions in terms of the amount of coal that can be imported into China. It's coal whether it's thermal or met. Clearly again because of the bigger arbitrage on met, people would rather use their quotas, if they've got them, on met than on thermal. And it has been more direct political sort of impact on the sale of Australian thermal coal into Australia, into China, rather than met.

Thermal coal probably you know, six SOEs, big buyers, essentially have chosen not to buy Australian thermal coal. They still do sell some thermal coal into China but it's not those big six SOEs. But we haven't seen that same impact in met coal. The issue is really just on the quotas at the moment.

Now, they may tighten this. I think with last year was probably over 300 million tonnes with the quota effectively and that might get tightened, it's still sort of -- nobody's exactly sure what happens. It probably gets tightened to something like 270, 280 million tonnes, or something like that.

At the moment, people are trying to buy coal ahead of any further restrictions on those quotas. In fact, with all those quotas running out. And so that's also why we've seen a degree of support for the met coal price in China. For the world, you see one price because of this strong demand, relatively strong demand from China. But as I say it's essentially the only market at the moment so that's why you see a subdued price.

As you look forward in the near term there'll be two impacts at the same time. One will be the reopening of the steel industries in the rest of the world where again, as I say, we normally sell most of our material and that'll happen progressively over the next six months. Probably in the fourth quarter of this calendar year more than the third quarter. And so that'll be positive for the met coal. But at the same time, you know, as we've done in previous years, as we get more towards the end of the calendar year and those quotas start to run out you might see some. So you're not exactly sure how that balancing point works out, but you know, we'll continue to sell our coal and whether it's US$110 or US$150 per tonne.

ALAIN GABRIEL

The second part of the question is on the political tensions between Australia and China. Do you see that clipping into iron ore?

PETER BEAVEN

Not at this stage [iron ore] ….

And as I said, thermal coal to an extent. So you're never quite sure exactly what is next -- if there is another wave of restrictions. You'd think in the near term that iron ore would be one of the more unlikely ones because if it did restrict it, then obviously again you're going to get this bifurcation price where we'd have to, if you can imagine for something you'd have to continue to sell elsewhere in the world, the iron ore price would go down in Japan and Korea and so on, and really hurt competitiveness of the steel industry. And so you'd think that that would be less likely in the near term.

But in the longer term, there's other things to think about, right.

ALAIN GABRIEL

Okay. All right. The next question is, we've seen a third of the growth from US shale close year-to-date. Given your experiences with that business, how quickly can that production return and how did it change, if care and maintenance periods are extended out?

PETER BEAVEN

You can bring it back very quickly, no question about that. I mean, the rig count has come up. Obviously, there's lots of DUCs and so we'll see, what and those DUCs will be sitting there waiting to be completed. But the rigs are gone. But the rigs can come back very quickly and so there's no question about the flexibility of that. That is not going to be the big impact on the medium- and long-term oil price.

That's just a near-term thing. What will be the big impact is to what extent will the financing dry up, I think, for the high-cost marginal barrels that frankly sort of shouldn't be there. Because if that happens then that does have a big impact because as we've seen in other commodities such as steel, such as iron ore, such as coal, and so on where the Chinese forced reforms onto the low, the weaker higher-cost producers, what you can see is if you can tidy that end of the curve up then, and stabilise thereafter then of course you can create substantial change because those marginal barrels or tonnes do make a big difference to the price.

So I think that will be I'm sure that's what the Saudis and the Russians are thinking their way through. And so it's the oddity of this, is that probably like some part of the long-term future, in terms of medium-term future of the oil price probably sits in the hands of Wall Street more than anywhere else.

But one thing I would say is that we have, given that we've had all this experience in, certainly in Eagle Ford and in Permian, not in the Black Hawk but we'll be careful students of the Black Hawk just to see how the development goes, what you see is there is a flattening of the productivity curve in shale and in Permian and so there is of course a finite amount of the best of those resources. And to see that even now Eagle Ford and Black Hawk really sort of starting to decline in terms of its quality.

So what will happen in, as I say, probably by the middle of the decade. And we'll see the best of those barrels getting produced out. It will be substantial opportunities to produce oil of course, out of the shale. But it'll be more expensive. And so you get this steepening cost curve, no matter what.

So probably, possibly, you get two impacts which is the drying up of the finance for the weaker part of the industry, as well as just simply the geology, it gets weaker. And so that alongside the fact that one-third of the capex has come out of all parts of the industry, not just the shale, which can go back quicker. The rest of it, the exploration money, everything else, plus I think, an ongoing increase in demand, plus field decline. There is a case to be made, not particularly fashionable at the moment, but I think there is a clear case to be made that in fact the oil price will be considerably stronger than it is today for a period of time. Thereafter into the 20s and 30s and so on, it clearly becomes a little less certain.

ALAIN GABRIEL

Okay. Thank you. And another question is, how realistic is it to expect hydro-powered trucks to be operational at Escondida or in Western Australia over the next five years?

PETER BEAVEN

We are working with OEMs to see if we can get a full electric truck. It's going to take some time to develop and to get a battery that can cope with the power demand, the huge power demands of what we've got. And that's going to be very difficult. So I think the intermediate will be to really go to trolley assist, and essentially that's a technology that's available. You obviously have to reset how your mine works. And that takes some money. But you know, it's an opex-capex thing. I think it will happen because we must reduce Scope 1 emissions.

And what we need to do is make sure that that comes in, and I think the objective, our prime objective here is to do it but to do it for something that's close as possible to NPV neutral, if not positive. Again, then it goes back and still the power has to come from somewhere. And of course that means that it's so important to have your fixed power available, you're reliable and of course cheap. And renewable, otherwise you're going around in circles. And so that's really the time there.

The other thing is to reduce trucks all together and really put in a lot more belts. These are projects, certainly when I was in copper and we would study these things because we have a large amount of trucks, 150 ultra-class trucks in Escondida. And that would probably grow as the pits deepen and so on, and so there would just come the time when in fact you start to become very congested. And that becomes a limiting factor.

And so putting in belts and mobile crushers for 10,000 tonne-an-hour mobile crushers and so on, becomes again, these technologies are available. They're not really widely employed into that sort of scale over in Escondida and so on. But it's possible, and again, we need to go and just put those projects we need to become successful on those projects. So it's combinations of things which will replace the diesel trucks that we have running today and that has to happen, I'd say, certainly in the next decade. So substantial work for us to do. But as I say, one thing -- we need to be able to do that for as close to NPV neutral as possible if not positive.