BHP

Financial results for the half year ended 31 December 2020

Investor and analyst Q&A teleconference transcript - Session 1

16 February 2021

Introduction

MIKE HENRY (CEO, BHP):

Well, hello everyone. Thank you for joining. I'm here with David Lamont our new Chief Financial Officer. We'll make some quick comments before we go to questions.

We had a strong first half, operationally and financially, with Underlying EBITDA up by 21% period on period to US$15 billion, and Underlying EPS up by 16%, to just over 119 US cents per share. We had the second-highest margin in 20 years at 59%, and the highest return on capital employed in the past nine years at 24%. We've seen record production at Western Australia Iron Ore, with full calendar year shipments of 290 million tonnes, record concentrator throughput at Escondida, and the best production half at Olympic Dam in five years. And very, very importantly, we did all of this safely.

We progressed our growth projects on schedule and on budget, in spite of the challenges faced elsewhere across the sector, with Atlantis Phase 3 and SGO delivering first production during the half, and South Flank remaining on track to deliver first ore within the next six months. We secured a further 28% stake in the Shenzi asset through a well-timed counter-cyclical acquisition. And we've continued to advance our securing and de-risking of options in future-facing commodities.

And finally we continue our track record of ESG leadership, including on Climate Change, with the announcing of a new set of Climate Change commitments, further renewable power contracts, the world's first tender for LNG-fuelled bulk carriers, and steel industry partnerships with the China Baowu Group, and JFE.

All in all, a strong half performance-wise, and in terms of advancing our strategic agenda. All achieved, of course, against the backdrop of continuing COVID challenges and disruption in some of our markets, thanks to the way our people have stepped-up, and the support we've had from stakeholders.

So our business performance is strong, our strategy is intact and advancing, and the outlook for commodities is promising. Overall, a pretty compelling picture for BHP, and continued strong shareholder returns, and value creation.

David, I might turn it over to you for a few comments before we go to questions.

DAVID LAMONT (CFO, BHP):

Thanks Mike. It's great to be back at BHP after 15 years. I'm certainly very pleased to be joining such a strong leadership team, and what a great set of results to start off my CFO role here.

As Mike has mentioned, the first half was a very impressive result. Net profit before one-off items was up 16% to US$6 billion. And importantly, the reliable and consistent operations, combined with those higher iron ore and copper prices, delivered a stable and strong cash flow, reaching US$9.4 billion in net operating cash flow for the half. Return on capital employed was a very impressive 24%, the highest it's been in some nine years. And importantly, we were able to keep net debt at the bottom end of our target range.

Certainly from my initial impressions of BHP today, it is clear that the capital discipline and social value are fundamental to how the company thinks about every decision that we make. And that is one of the reasons that I joined the organisation.

So with that, I might pass back to Mike and we'll open it up for questions.

MIKE HENRY (CEO, BHP):

OK, thanks David. Operator, we might go to questions now please..

Questions and answers

PAUL YOUNG (GOLDMAN SACHS):

Thanks. Good morning, Mike and David. Two questions from me. One on the portfolio and one on the cost performance.

First of all, just on the oil division and honing-in on acquisitions. The question is, with all the majors tilting towards investments in renewables, do you see further bolt-on opportunities in the GOM? Or does the Biden administration's review on new leases and permits on federal land make you pause on acquisitions.

Second question, Mike, is on the cost performance. Pretty solid performance, but I do note that FX was strong. It's impacting costs industry-wide, but can I single out two assets which, on my numbers at least, negatively surprised. One being Olympic Dam where costs were nearly US$750 million – I think it's the highest in a half in over 7 years – and met coal absolute costs are up US$250 million, half on half, yet volumes came down. Just curious on how much of increase and the absolute cost, particularly at OD and met coal, might unwind in the next half, if at all. Thanks.

MIKE HENRY (CEO, BHP):

OK, thanks Paul. So David, I might ask you to comment on cost. I'll address the question on oil first.

So we've been clear in the results Paul, that we will continue to consider counter-cyclical acquisitions for the right assets that are a close-fit with the existing the portfolio. With Shenzi, of course, we knew that asset very well. The acquisition was timed well, counter-cyclical in nature. And the drilling work that we've undertaken since the acquisition has been very promising, and points to the upside of the internal view that we had of value range.

You've also referenced the Biden administration's pause on granting of new leases on federal lands. We're still assessing what the implications of that are. As is the rest of industry. But while it may, under some scenarios, impact on exploration-related activity, it of course wouldn't preclude existing assets, and I think it would also have a counter-balancing positive effect in terms of perhaps putting one further constraint on the supply side, on top of the big pull-back in capital investments that occurred across the industry over the course of the past 12 months.

We'll continue to assess the situation, but if the right opportunities were to arise we're certainly opening to considering them and we've got the ability to pursue them.

David, maybe on costs, there's a question on costs?

DAVID LAMONT (CFO, BHP):

Yes, certainly. Let me put the answer in the context and you certainly did call out, Paul, OD and also met coal. But I would start with the premise that we have certainly not changed any of our cost guidance for the year.

So, the performance at the assets is in line with our own internal expectations as such. Now, met coal for the half was slightly above. And that was largely driven by maintenance costs, so it's a timing aspect, and we certainly see that will come back in the second half. So again, I'd point you back to the guidance that we've given for the full year.

In relation to Olympic Dam, we continue to look at the asset integrity side of things, and some of the costs in the half were driven by the SCM process as well.

LYNDON FAGAN (JP MORGAN):

Thanks very much.

The first question is, just on the dividend payout, obviously great to see a high number there, and certainly beat the market expectations. Just wondering if you can provide some detail on how we should forecast that going forward given that you're still at the bottom of your gearing target, yet the payout ratio is materially higher than anyone expected.

And the second question is, again on the portfolio, given the volatility and results out of coal, just wondering if you can talk a bit more about your commitment to coal going forward and I'm talking now met coal. Obviously you've made your thermal coal commitments clear. But do you see a potential to maybe look at that further? And also petroleum given the way things are moving in terms of decarbonisation and investors wanting companies out of fossil fuels. Obviously still profitable, but any thoughts there. Thanks.

MIKE HENRY (CEO, BHP):

OK. David, do you want to comment on the dividends question? And then I'll come back to the portfolio question.

DAVID LAMONT (CFO, BHP):

Yeah, thanks Mike. Look on the dividends, you're right. It was a very healthy payout for the half. I would just stress that what we do is we look at each half in its own merits and look at obviously how the half has performed and what that actually means. I'll single that out in the context of the capital allocation framework. Which, let me start by saying I'm a believer in the CAF. From my side of things it does create really good capital discipline across the organisation, and it's something that we're certainly firmly committed to.

So as you know, under the CAF, a minimum payout would be 50%. So that's your starting position. Over and above that, what I would just give you an indication of is that if you look back over the last three years, we've paid-out US$30 billion in cash. So that gives you a view, but certainly says that if we have excess cash, over and above that 50% minimum in accordance with the CAF, we'll pay that out. Now I'm not going to predict what that is, that's largely your roles to have a look at. But we'll obviously look at how much cash we've generated in the six month period and look to return an appropriate amount back to shareholders.

MIKE HENRY (CEO, BHP):

I would just add Lyndon, what you've seen us declare this time around is, as David says, driven by the CAF, informed by performance in the half, and our positive outlook for commodities. Now we still have four and a half months to go in this half, so we'll have to see where we are at the end of the half. But we are constructive in our outlook for commodities and the business is performing really well.

Now if I come back to your question on portfolio, so met coal and petroleum. Yes, there are near-term challenges posed by what's happened with the China coal ban, but in looking at this from a medium to long-term perspective, we do need to keep in mind that there's high complementarity between the Australian metallurgical coal resource base and the Chinese steel industry, as there is between the two economies. So one has to hope or believe that in due course that will be a resetting of things, and both parties will be able to enjoy the fruits of that complementarity.

The other point I would note however, is our met coal business, unlike iron ore for example, is much more diversified by market anyway. So we start with greater market diversification, that coupled with the strong customer relationships we have, has allowed us to continue to move all of our product.

And if you look at the economic growth we expect to play out globally, we do believe there is going to be increasing demand for metallurgical coal, and in particular, the premium quality metallurgical coals. We think demand is going to remain resilient, and that the value of those coals will be increasingly recognised and rewarded as steelmakers seek to decarbonise, and we're sitting on the premier business in the world. And so we do see the outlook at that business is remaining positive.

Oil and gas, really no change in view from what we had in the middle of last year. And that was that we, of course, recognise the trends that are playing-out around us in terms of long-term oil and gas demand in a decarbonising world. However, given how essential oil is to so many of the processes that underpin life as we know it today, and it will remain the case for some time, we think there will be a measure of resilience to demand going forward. You couple that then with a combination of natural field decline and the big pullback in investment that's occurred in the sector over the past year, so we think there's a number of positives to point to in the near to medium-term fundamentals in the industry for investment, and so we still hold to the view that the industry will remain attractive as the destination for investment, more broadly for the next decade and likely beyond.

In terms of our portfolio, we're going about this in a very balanced way. Looking to invest in high-returning options. De-risking the options that we've created through our exploration success, but also looking to divest assets that are more mature.

HAYDEN BAIRSTOW (MACQUARIE):

Yeah, morning guys. Just a couple from me.

Firstly Mike, just on iron ore as you said, you touched the 290 million tonne run rate for calendar year 20. Just interested in where you see that business going from here. I know you've applied for potential port capacity increases, whether there is some scope to creep a bit higher from here, or will it require meaningful investment in train unloading capacity at the port.

And then just on Olympic Dam, an asset that continues to struggle. I mean, it's just interesting to understand, given the decarbonisation potential on mining fleets and hence the pre-strip and the lack of success on the underground, is a re-look at the open pit long-term something that would be considered, given you could theoretically cut it back for a lot less and a lot lower carbon emissions than was originally planned? Thanks.

MIKE HENRY (CEO, BHP):

OK. Thanks Hayden. So, look, in terms of iron ore, as I said previously we didn't seek the licence to be able to ship 330 million tonnes because we intend to expand to 330 million tonnes. My challenge was that the business year-in and year-out has been performing better and better and better. What I didn't want to see is that we end up in this weird situation of needing to stop production 90% of the way through the year because the team has done a fantastic job. So we wanted to de-constrain ourselves from the 290 million tonnes limit. And as we've shown over the course of the past 12 months, the business does have the ability to perform at that level.

First focus is on getting sustainably to 290 million tonnes per annum. And doing so with a real discipline around cost, which you can see coming through in the last half as well. I want to maintain that. As the team focuses on that continuous improvement and productivity uplift, it could see us go a bit beyond 290? Possibly. But nobody should read this as an intent to pursue expansions per se.

Now, on Olympic Dam, there were really two things in the question that you asked. One was around a point you made around performance, then a question around whether the open cut was coming back again.

On performance, I just want to draw everyone's attention back to what we've said previously. That is that our focus is on: securing reliable operations, getting back to circa the 200 thousand tonne per annum copper production level consistently, to improve underlying productivity in the underground, and then to look at medium-term de-bottlenecking and larger expansion options. And I think what you've seen come through in the past half performance and the trend on performance over recent periods, is that increase in reliability. Best half in five years. So we're starting to see the fruits of all of the effort that we've had underway around asset integrity. Still a couple of years to run. Then we get through SCM21. And I think the business will be set up for more consistent high productivity performance from there on out.

We then have the question of long-term expansions, which is your point on the open cut. If I think back to open cut at the time, the capital cost associated with that was going to be huge. And the cash flows, the payback very, very long. Nothing has changed in terms of those fundamentals. For that ever to be revisited, there would have to be quite a radical shift in underlying productivity assumptions around mass moving of dirt. So that isn't a focus for us at this point in time.

JAMES REDFERN (BANK OF AMERICA):

Hi Mike and David. Two questions please.

The first one is around the potential demerger or trade sale of BMC and thermal coal assets. Obviously creating share value is a key priority. Just maybe wondering if you could please touch on the pros and cons of a demerger versus trade sale process, and I've got one more question after that, please.

MIKE HENRY (CEO, BHP):

OK, so thanks James. And David you may want to comment on this as well. But let me just, before I talk to the pros and cons, where are we at in the process? As we said last year we saw it playing out over a two year period, or up to a two year period, because we're still early in the process and want to explore different avenues for divestment – trade sale, variants on that and demerger, we're still looking at the range of options.

At the end of the day it will come back to what we see as being the best value and risk outcome for shareholders. For us to get a sense of that, there will be a level of market engagement that needs to occur to be able to assess market views of demerger, and likely acquisition prices in a trade sale. And it's still a bit too early to tell. We'll be guided by what we surface through the market engagement. David, is there anything you wanted to add to that?

DAVID LAMONT (CFO, BHP):

No, I think other than just so, you know, as you said it's a two year process. And we're in the midst of that. So we're meeting the guidelines that we articulated to the market, and the process is under way.

MIKE HENRY (CEO, BHP):

Yeah. And sorry, just one other thing I should have mentioned James, is of course it's a dynamic environment that we find ourselves in, and the conditions for a demerger or, and/or the conditions for a trade sale, aren't static. So there will be a bit here of making our final choice, based upon the circumstances at the time, or as they evolve over the next year and a half.

I think you had another question?

JAMES REDFERN (BANK OF AMERICA):

Thank you. The second question is on Jansen that’s on track to be presented to the Board by middle of the year. Given BHP wants to grow its copper, nickel exposure, and potentially potash, being the future-facing commodities. Copper and nickel, very long dated, given that most of the projects are in the exploration stage. Potash can obviously come on a lot faster, and the commentary in the release, still talks about being positive on demand for potash. So should we read that there's a strong likelihood of Jansen being approved in the middle of this year? Thank you.

MIKE HENRY (CEO, BHP):

It would be helpful for us to come back and think about or talk to the way we think about commodities and projects.

First thing that we assess is what is the industry attractiveness of a given commodity, which comes back to demand and supply fundamentals, how we see those playing out over time, under a range of scenarios. The next question then is, “OK, so if we find a commodity attractive, are we able to get our hands on assets that are large, expandable, at the low end of the cost curve, so we can create and sustain good rent?”. A third question is, “do we have capabilities to operate those assets well”?

What we're trying to draw out in our results presentation or release, is that we do like the commodities. That first test is met. We think that the megatrends that we see playing out in the world bode well for long-term potash demand, under a range of different scenarios. And in a more rapidly decarbonising world, things look even better for potash.

Can we get our hands on good assets? Yes, we've got a large position in the world's premium potash basin, and we believe we have the capabilities to run those assets well.

Final question then, when it comes back to the individual project is, “does it generate attractive returns and compete well into the capital allocation framework?”. And that's the test that needs to be met. And if the answer is yes, so if we believe the project is attractive on its own two feet, and it competes well into the CAF, then we'll take that to the board for a decision. If the answer were no, then we wouldn’t carry it forward.

Final point to note here is, I don't like where we're at with this asset. The fact that we've got US$4.5 billion sunk into Jansen, and the time it's taken us to get here, is something that we’re certainly not pleased with. We will build upon the learnings that we've taken away from that in how we think about further projects in future-facing commodities.

But as CEO, I'm accountable for ensuring that we make the right decisions in respect of fresh shareholder capital. And so we will look, when it comes to our position on Jansen, the decision we take in the middle of the year, it will be based on what we think the best application of shareholder capital is, given what we can see in the project, and given the opportunities we see, be it other projects or increased returns to shareholders.

GLYN LAWCOCK (UBS):

Good morning Mike and David. Just two questions quickly.

Your commodity commentary obviously reads better than what it did six months ago. Clearly the vaccine has come through. Just wondering, in the context of how you're seeing the backdrop, have you looked at, I know you can't quantify the absolute numbers, but have you revised any of the medium to long-term commodity prices on the back of how you're seeing the world? And given your comments on electrification and decarbonisation, is lithium still a no-go? That's the first one.

And the second one is hopefully pretty quick. Just, you answered, you were talking about the 290 million tonne cap, hopefully going to 330 million tonnes. Can you help us understand how the dialogue is going with the EPA? Do you see any risks and do you have any thoughts on when the timing of that could be announced? Thanks.

MIKE HENRY (CEO, BHP):

David, do you want to maybe speak to Glyn's question on the commodity price outlook, and then I'll address iron ore 290 million tonnes?

DAVID LAMONT (CFO, BHP):

Yeah so Glyn, let me start by saying, we constantly look at our commodity price protocols. We have a process that’s in place as you would expect. Coming into the organisation, it's a very robust process that we follow. There's an annual cycle that we work our way through. So we review those on an annual basis. And they're staggered. It's not as though we do them all in one hit. We stagger those throughout the year based on the commodities.

We fundamentally see that the commodity prices are something that we look at from a strategic perspective. They’re not something you would expect us to fluctuate purely and simply on where spot prices are at. So we go back to a fundamental base, look at the supply curves, look at the demand side of things, and constantly update those. So have they changes from six months ago? Some have, yes.

MIKE HENRY (CEO, BHP):

The other thing I would say, Glyn, and this was a big change in the way that we think about commodity prices and investments over recent years, and it's the use of scenarios.

So everything that you see playing out currently in the world, if you’re of the view that things are going to decarbonise more quickly, we have a number of scenarios that deal with that. So if I think about the range of prices that we test our portfolio and individual projects against, everything that we see playing out around us is within those ranges. But as David said, each year we will finesse the ranges and where we see ourselves sitting within them.

On your second question around iron ore, it's still a work-in process with the authorities in WA. But I think there's broad recognition of the health of the underlying business, and so the conversations often come back to what are the conditions that are put in place under which the licence will be granted.

Because we've got a track record of improving dust management, improving water stewardship, improving community engagement, I think all of those are positive and would point to support for the request that we've made. But until we've got approval in-hand, of course, we can't say for certainty how it's going to come through. But as we've done in the past, we'll work constructively with whatever information is required, and the requests that the regulators have.

Sorry I just recalled Glyn, that you did ask about lithium. No, the views haven't changed on lithium, but that's not a view on demand because I think, as we've said previously, we do think that there is going to be a strong demand for lithium. We think the industry is going to grow. But our view was primarily based upon an expectation that the cost curve is going to be quite flat for lithium. And therefore, the ability to extract great rents we don't believe it’s going to be there, and so it's a no for us now, but we'll maintain a watching brief on it.

PETER O’CONNOR (SHAW AND PARTNERS):

Good video, Mike, and welcome aboard, Dave.

Mike, can I just explore the supply and demand pathways you mapped out in your presentation, and the divergence that I kind of picked up between the two. So, I loved your anecdote about copper and nickel demand, how they were doubling or quadrupling. And also the commentary about steel and its impact on coal and iron ore. It is clearly a robust view, I think you called it a constructive view going forward. Then you talked about iron ore and coal and, I think you talked about only incremental growth opportunities via productivity. Could you just join those somewhat divergent views on demand versus supply on those two commodities?

MIKE HENRY (CEO, BHP):

Sure. What we're trying to draw out there Peter is that for many people - almost because of the focus on how positive things look for copper and nickel – there's this latent view that somehow things must be bad for all other commodities. What we're trying to say is that's not the case.

We also said, when we spoke about the 1.5 degrees scenario last September, in a more rapidly decarbonising world we actually see that creates more demand for a number of commodities including the steel making raw materials. So the way to read this is, copper, nickel, and potash will have faster rates of growth than for other commodities. In addition to that of course you've got the issue of grade decline which can compound the investment attractiveness there. In the case of steel and coal, for the right products we think demand is going to be resilient. The question is for how long. So, for example, in China, we're still predicting the steel demand is going to plateau and then move into decline. And over time, there will be some pressure in the iron ore market. But the pressure will be alleviated a little bit if the world gets onto a stronger trajectory of decarbonisation.

Now, in the case of metallurgical coking coal, there's specific positive dynamics, I think, for the right quality coking coal in a decarbonising world as steel makers seek, in the interim, to reduce their carbon footprint by increasing blast furnace productivity. So for the core of the BMA coal we think demand will be particularly resilient and the value increasingly recognised and rewarded. Now, why are we not talking about big expansions in iron ore and coking coal. Because, whilst demand will be resilient, they're not going to have the sort of market or demand growth that we'll see with copper and nickel. And so our predominant focus has to be on creating more value through productivity. But, if we're wrong and somehow demands takes off in iron ore and met coal, we do have the latent ability because of the big resources that we have to grow those businesses more proactively, but that's not our starting view.

PETER O'CONNOR (SHAW AND PARTNERS):

So Mike, steel you mentioned doubling over the next 30 years since the last 30 years. You're saying there's not room for iron ore expansion beyond your 330 Mtpa you're asking for at the port or 290 Mtpa cap .

MIKE HENRY (CEO, BHP):

So to be clear, what we've said is that the area under the curve over the next 30 years will be higher than it was over the past 30 years. But that's not to say that the demand for steel making raw materials will double over that same timeframe – the rates of growth for the individual commodities will remain quite different.

RAHUL ANAND (MORGAN STANLEY):

Hi Mike, welcome David. Look, some of my questions have already been asked. But if I can ask two. First one on the dividend and second on the DLC.

Look, first one on the dividend, is basically around, is mainly an extension to Lyndon's question I guess. Would you consider a free cash flow based dividend perhaps, going forward? I mean, it would seem as though it would better suit the needs of the business going forward from a changing capex requirement and perhaps proceeds from divestments that you've talked about. That's the first one.

The second one was around how your views have progressed in terms of the costs and benefits of the DLC structure of the group post the divestment of the coal assets. Thanks.

MIKE HENRY (CEO, BHP):

OK. So, I might answer the question on then DLC first and I'll turn to David for comments on the dividend.

So the DLC, you've called out one of the costs associated with collapse of the DLC is reduced. As we said previously, the DLC remains under regular review. It has for quite a number of years. I think we all start from the perspective of, all other things being equal, we like simple. But at the end of the day the business case needs to stack up when looking at value, costs and risks. We'll continue to review that. The situation is dynamic.

However, my current priorities one, two and three are: managing through the continuing risk of COVID; driving forward the performance agenda; securing and creating options in future facing commodities; and continuing to strengthen ESG leadership. And I think you can see the benefit of that focus, and the priority that we're putting on those things, shining through the results we've just released and I dare to say the shareholders will be pleased by the record interim dividend.

David, Rahul's question on the dividends. Maybe if you can take that one.

DAVID LAMONT (CFO, BHP):

Yeah, certainly. So, let me just make one observation that I'm sure some of you haven't missed. Your question was around the dividend in relation to the free cash flow. I would just point out that the free cash flow after we paid our dividends to our minority partners that we have was some US$4.4 billion. So, if you contrast that with the dividend that was paid out at US$5.1 billion, we ended up with a payout of 116% of the actual free cash that ended up in BHP hands.

In relation to the question “would we change the metric”? Short answer, no. You know, we believe that the appropriate way to look at the dividend is in accordance with the CAF as we have outlined. Come back to the net debt range of the US$12 to US$17 billion as the framework that we use alongside the CAF. Understand the nature of the question, but we think it's better to look at things on a half on half basis in relation to the principles established under the CAF.

KAAN PEKER (RBC CAPITAL MARKETS):

Hi Mike and David, thanks for taking my question. Just the first one is on the Biden administration policy. I know Mike, you mentioned that exploration activity and not existing operations will be impacted. But just wanted to ask about possible decline rates at existing assets. Also does this uncertainty impact plans for the possible sale, or the divestment of Bass Strait stake.

The second question is on Escondida. Maybe an update on absenteeism. Is it still running at circa 30%. And is the asset opening up sufficient mining areas to continue to produce around that 1 million tonne mark. Thanks.

MIKE HENRY (CEO, BHP):

OK, thanks for the question. I'll answer the Escondida one first and come back to the Biden administration and petroleum more broadly.

Yes, absenteeism rates are continuing around the 30% level at Escondida. You may have noted that the prevalence of COVID in Chile has remained at quite high levels. However, we are seeing a real acceleration there now in terms of the vaccine rollout. The situation there remains uncertain. And you'll see that we've maintained guidance for the full year albeit pulled up the bottom end of it. The other thing I would note is outside of COVID, there has been some weather challenges in Chile. So quite uncharacteristically for the Chilean Coast. There's been extended periods of choppy seas is the way I would put it. But because they're unusually choppy for Chile, that has impacted some producer’s ability to ship out or bring input in for a period of time. But guidance holds, brought up the bottom end of the range. But, you know, all these things together, COVID uncertainty, what we've seen in January and February, points to why we've maintained guidance rather than lifted it. Probably the other point to know is just in terms of medium term guidance for Escondida, it remains strong and certainly no changes there, with a lift towards the back end.

Now, if I come back to petroleum and the Biden administration situation. Firstly, still trying to understand what the full implications of the pause are. As to decline rates, I think it depends a little bit on who you're dealing with in the industry. But anywhere between 3% and 6% before you get to things like infill wells and so on is generally what you see it across the industry. And if you are not seeing replacements because, if the moratorium is extended, then of course that will bode well for the supply demand balance in the US. So if you are an existing producer with some big assets like we have, there could be positives there.

On the question around Bass Strait, does this impact the Bass Strait divestment at all, the answer is no. Our view is still that it's an asset that obviously it's been part of the BHP portfolio for a very long time. Solid part of the asset, created a lot of value for us. But it's a more mature asset and we'll continue to progress the divestment process.

ROBERT STEIN (CLSA):

Hi Mike and David. Solid result. Just two questions on the portfolio. We’ve talked a little bit about iron ore expansion plans. Just changing tack a little bit, what type of signal would you need to see to start to recommit to some of the de-bottlenecking projects in WAIO. If you saw that signal, how shovel-ready would those projects be?

MIKE HENRY (CEO, BHP):

Robert, I'm trying to think of what the few are that we would look at. So, obviously, you've got probably the third year running of China running at over a billion tonnes of steel production. Our view remains that through the middle of this decade you'll see that plateau and start to come off. If something happened by way of the Chinese economy which causes us to have the view that you are going to see these high rates for longer or even higher, that would obviously improve demand side fundamentals.

Then the other question is on the supply side. So what are we looking at right now? Our base case expectation is that you'll see the Brazilians come back stronger. So you'll see more supply out of Brazil and in the medium term you will see supply coming out of West Africa. If, again, something were to happen which caused us to take the view that there was more of a cap on supply coming out of Brazil, or West Africa wasn't going to proceed, that would point to stronger supply-demand dynamics, which we could then look to expand into. If we were going to pursue any expansion, first would be de-bottlenecking, minor debottlenecking. That could probably get you to over 300, 310-ish million tonnes. You could get there fairly readily. If we then wanted to, so let's assume that permission was granted for us to be able to ship 330 million tonnes per annum, there would be more work required then to look at what would be required to go from 310 to 330 Mtpa, because we don't have shovel-ready projects to be put at. There would be some more meaningful work that would need to take place on further de-bottlenecking and some mine expansions as well.

PAUL MCTAGGART (CITI):

Good morning. So, on the earlier discussion, Mike, we touched on a topic around Jansen, insofar as how you might think about future big projects. And obviously, there's a whole bunch of them around the planet at the moment where there's sunk capital before you get to a point where you make a decision as to whether you want to go ahead or not, and just gets to be so large. And obviously, Jansen's a great example for that, but Resolution Copper is probably another one.

What can you do differently? Because, once you've sunk the capital, obviously it makes sense to go ahead with the project if it's economic from that point on, but in totality it may well be that it doesn't work. So, how do we get around that?

MIKE HENRY (CEO, BHP):

If this were simple Paul we wouldn't see what we've seen. So, I do want to acknowledge that, you know, teams will be facing a different set of circumstances at any given point in time. There is of course some value in spending a bit of capital upfront to de-risk a project or get better insights on a project before you take the big capital decision. I think we all have to recognise that, because the last place you want to be in, is taking FID only to find out post facto that there's something big and unrecognised that causes real issues.

However, in the case of Jansen, if you look at what we have there, in addition to just the usual stuff around some of the early project investments, we have shafts that are built for much higher levels of production. And again, with the benefit of hindsight we've spent capital too early, because we've effectively been investing in the business now for ten years. And we've invested capital in the business that was meant for a larger production level and we've since pulled that back.

So, what would we do differently going forward? Well, a few things. So one, the capital allocation framework has been put in place post that, which drives a real discipline in terms of assessing where the next dollar should be spent. And rather than just looking at the headline level, picking apart projects and saying what's really necessary to spend now, versus what later and that could have had implications for how much we would spend in Jansen. I also think that, not that it was the intent at the time to super-size things for successive of phases of Jansen, but as we made decisions to scale back production levels at Jansen, those decisions were taken after some of those early capital decisions. So going forward, we wouldn't do that. We would invest for the project that we have and if we were going to look to expand through further phases we would look to defer as much of that capital into further phases as we could, to improve the investment economics in the first phase and then to make separate decisions on a go-forward basis. But David you're pretty fresh to this. Any other points you'd make in terms of both questions.

DAVID LAMONT (CFO, BHP):

No, I think other than to just reiterate what you said Mike, which is important. Throughout the cycle we need to look how do we de-risk the project as well. And that actually comes with better knowledge. And unfortunately, sometimes you have to spend some money to build up that better knowledge as part of the process. But, I would just also say though, coming in cold, I think the organisation is very upfront at looking at the lessons learnt. So I don't think anyone has got their heads in the sand and just believing what was done in the past is the necessarily the way forward. And that's refreshing as we look at further opportunities.

PAUL MCTAGGART (CITI):

OK. Thanks guys.

LYNDON FAGAN (JP MORGAN):

Oh look, thanks for taking a follow-up. Really just wanted to touch on Samarco. So, I guess it's back online which is great, but we've got negative net assets of $2.2 billion and I'm just wondering if you can talk a bit about some of the future plans there. What capital expenditure plans are likely? What's the sort of, production scenario to expand from the initial run rate? And what's left, I guess, to negotiate with bond holders, etc.? Just wondering if you can provide a bit of a broader overview? Thanks.

MIKE HENRY (CEO, BHP):

OK Thanks Lyndon. I'll provide the initial view and David, you might want to add some colour. So let me start by saying Lyndon, we remain committed to ensuring that all the programs that we've laid out under the agreement there are met. That remediation is completed, re-settlements are completed, compensation is provided. That's the first focus.

Now, it is good to see Samarco restarted again because that of course brings jobs and economic activity to the local communities. Right now we should expect around 8 million tonnes of production when it gets fully ramped up. I think it's probably one to two million tonnes that we added to guidance for this year given that we're only producing for circa half a year. As to a second and third concentrator, if I understood the question correctly Lyndon, those are still kind of down the road, so you shouldn't expect that we're going to trigger those any time soon. And then, bond holders, we will be supporting Samarco in Samarco's negotiations with the bond holders. The debt of course is non-recourse to BHP and will remain so.

Final comment, first up I was talking about compensation claims and so on, we've seen more progress in the past five or six months, than we have for quite a while previously. So things are really starting to accelerate there.

David, any further colour to add to this one?

DAVID LAMONT (CFO, BHP):

No, other than to say, clearly we're supporting Samarco in the negotiations with the debt holders. That will be an ongoing exercise. I don't expect that that will be a quick solution as part of that process. We need to continue to obviously assist, but it is non-recourse and Samarco are needing to actually address that. It is pleasing though, that the asset is back up and running, and that clearly means there is at least cash coming in from Samarco that can help in relation to all of its obligations.

PETER O'CONNOR (SHAW AND PARTNERS):

Dave, two questions. One small one but met coal, and met coal payments for cargos. The boats that may or may have not been stranded off China. When do you receive payment for those and have you received payment for all of those? That's the first question and I have a follow-up.

DAVID LAMONT (CFO, BHP):

Short answer to that Peter, is yes. They were FOB sales so we have actually received payments for those cargos that are sitting off the China Coast.

PETER O'CONNOR (SHAW AND PARTNERS):

Great. And second question, return on capital employed, it's extraordinarily impressive. The charts you put in really mapped that out. Can you break that down, because you kept returning to the 2016 low point or the previous highs in the 2010-14 period, the split between price and operational efficiencies that's come with that ROCE. I.e. if you used a constant price deck, how would the ROC look?

DAVID LAMONT (CFO, BHP):

Let us to come back to you on that Peter. I don't know that off the top of my head to be honest, but I'm looking at Mike here.

MIKE HENRY (CEO, BHP):

Look I don't know the exact answer either David, but a big part of it, Peter, will be price, of course. Because back then, you know, you had all commodities at high levels. This time around we've kind of had record netbacks for iron ore and record copper prices, but oil, gas and coal have been much lower. But at the end of the day those things are also uncontrollable. On the controllables, performance is definitely improved over that period of time. We're so much more productive now. And we're much more disciplined in what we're doing with our capital. So, for the things that we pull the levers directly on, the business is really performing well and that would have contributed. But let us come back to you, with an estimate to the best we can, perhaps David, on what proportion there's been of each.

PETER O'CONNOR (SHAW AND PARTNERS):

Can I ask a follow-up?

MIKE HENRY (CEO, BHP):

Sure.

PETER O'CONNOR (SHAW AND PARTNERS):

Olympic dam and Queensland met coal have quite large asset bases or capital bases and given where they sit on that diagram Dave put up, which is on the lower right hand corner, very small positives or slightly negative. Given the outlook you've mapped out today for both those assets, is there the capability that you can return an adequate return on capital given those extraordinarily high capital bases and the outlook for even productivity and growth, etc.?

DAVID LAMONT (CFO, BHP):

So, short answer is yes, Peter. As we alluded to earlier with Olympic dam, we do see that we've got to get to that 200,000 tonnes. At that level, and consistent performance at that level, certainly turns that asset into not being a drag, I would say. It's never going to be the same sort of return given the asset base that exists, as we clearly get out of iron ore. But that doesn't mean that it would not deliver an adequate return for the organisation. And that's certainly the focus. Then we need to look at, how else do we actually maximise that resource base that exist. Because it clearly is a world class deposit. Understanding that equally as part of that what we're wanting to do is make it as robust as we can through the cycle. And the cycle is clearly going to play out through that.

In relation to met coal, I'll come back to Mike's earlier comments, which is, we do see in a decarbonised world that people are going to gravitate to the higher met coal assets of which we're in a good position on. We certainly think, to look at it another way, in its current performance where prices are at, is not a true reflection of what we think that asset can do throughout a cycle.

GLYN LAWCOCK (UBS):

Hi Mike. Just a quick follow-up on Jansen and a point of clarification. So, when you go to Board mid-year and you're under the, I think you now call it the CAF, nice acronym, will you be considering the sunk capital or when you look at this now and you have put it up against all the other options you have internally, will it just be based on the future capital, because obviously there's a very big difference looking at it.

MIKE HENRY (CEO, BHP):

Great, great call out again, Glyn. The answer, I'm afraid, is slightly nuanced in the sense that the Board has absolutely insisted that we bring forward numbers that also take into account sunk capital. So we will, as I said earlier, I think the decision we have to make today is what is the best application of fresh shareholder dollars. That doesn't mean that we shouldn't have transparency around the capital that has been sunk today. The management will ensure we have transparency and the Board will also have that transparency. Part of the reason for that, it is that you want to drive the right culture. Where you do have some capital that needs to be staring management in the face, day in and day out, so we can see coming back to the point David made earlier around learning lessons, we can reflect on the lessons of the past, but in addition to that, I think where sunk capital and fresh capital do need to be taken together is in assessing overall industry attractiveness. Because I think that, whenever we make investment, coming back to my earlier comments about how we think about commodities and projects, in addition to the project decision that we have at hand we have to be asking ourselves, is this industry attractive. And one of the indicators of that industry attractiveness will be full cycle economics or all-inclusive economics on projects which require the inclusion of sunk capital as well. Now we do think that the industry is attractive, I've made that clear, but we want to maintain the discipline of ensuring that we have visibility over the full range of financials.

Operator, we might call it a day then on questions if that's OK. So thank you everybody for joining. And we'll look forward to talking with a number of you again. Thank you.