Rio Tinto

Half Year Results
Q&A

Wednesday, 26 July 2023

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Liam Fitzpatrick (Deutsche Bank): First question on Simandou. It seems like you're finally getting close. So could you outline what the key outstanding issues are before you and the partners can move forward? And then as a follow-up, just on the Capex, it's obviously a very big project with lots of layers of partners, so can you shed some light on how you're going to account for it and guide on it from a capital point of view? Thank you.

Peter Cunningham: So, what we're showing is just our share of the capex for the project. That's how we'll put through guidance going forward. I mean, clearly we're still in the midst of negotiations and moving the project forward, so we're not showing what the whole piece looks like. We've just got to respect the fact that we're still in that period of working that through with government and with various partners. But what we've shown is what we think is our spend, just so you have a sense over the next few years of what Simandou means in terms of our total capital. So that's how we've pushed through it. But effectively it's the Rio Tinto share of the capital that we will be showing and that 500.

So, effectively in the second half of the year we expect to reach that point at which we will start capitalising, that we have confidence to go forward as the negotiations move forward. That's where the 500 is there. But, you know, it may move around. Negotiations, it will take as long as it takes to get right.

Jakob Stausholm: And where are we on negotiations? We have a big team in Conakry right now. I spoke to Bold this morning, he's down there. My sense is that we've actually solved basically all the big issues, but it's a big set of agreements that has to work for the government of Guinea and for the partners for 30 years out. And we have to get that right and it's been a big challenge for everyone. We have four partners and one government and such negotiations are complex. The fundamentals we have agreed on and you can see some of the analysts looking at satellite there is a lot of progress happening and we are progressing in parallel with the negotiations but we have to take time to build the trust and build the shared understanding of what we are trying to achieve. Obviously we need to agree final things around cost and schedule and as soon as we agree that we will disclose that to you but right now we need to agree some fundamental agreements with the government and we are getting very close to that. Overall I'm quite optimistic about it but I've learned that its very difficult to lay out a precise schedule. You probably shouldn't be too concerned about it as quite a lot is happening in parallel although, having said that we feel that we don't like to spend too much money before there is clarity and we can finally sanction the project with our Board.

Tyler Broda (RBC): On the Matalco JV, how much profitability do you expect to bring in to the company and do you see any synergies over time with the rest of your aluminium business. Can you explain your recycling strategy?

Jakob Stausholm: It's very difficult for me to answer the first question, because we have announced the deal but we haven't closed the deal, subject to obviously competition authority clearance and it's a joint venture with a private company, who's not used to a lot of disclosures and therefore it's very limited what we can say.

But I think conceptually what you should think about is that we have the Western world's largest aluminium business and they have capacity of 900,000 tonnes of aluminium. If you think about what we are trying to achieve in terms of our purpose, in terms of reducing our carbon footprint and reducing our impact on nature, we want to support recyclability. We can't really support recyclability in iron ore because we're not in steel making. But Rio is different than most mining companies because we have quite a lot of manufacturing. And where we have manufacturing, we should try to see is there a business opportunity also for recyclability. Where we have the biggest opportunity is obviously in aluminium, but we also have copper smelters, processing plants in titanium, etc.

So there are other business opportunities but the starting point is already today there is a big secondary market in North America and here is an opportunity to provide a better value proposition to our customers by combining forces.

I also like the joint venture structure, it plays to each other's strengths. The Giampaolo group knows a lot about the collection of scrap, etc., which we have no competences in but we're going to market the product. So we can each provide value into the joint venture.

I can't say anything about the profitability at this stage, unfortunately.

Paul Young (Goldman Sachs): Can I ask about the other half of the $2 billion or so investments you announced in aluminium during the half, and that's the AP60 smelter. I'm just looking at capital intensity of the smelter, which is about $7,000 a tonne or so. That's a lot better than Kitimat, which was about $10,000 a tonne or so. That was probably the high-watermark of capital intensity in the Western world. I'm just curious around the $1.1 billion investment. Does this incorporate benefits of using Chinese EPC in furnace, which I know you've been talking about for the last two, three years and does this represent a possible larger push into growing green aluminium in Canada? Thanks.

Jakob Stausholm: Yeah, you're absolutely right. The challenge that we have in the Western world is that we barely have built any aluminium smelters for two decades actually, and last time we built one, we had a cost overrun. So we are very, very focused on not repeating that mistake, and therefore we are looking towards where most aluminium smelters have been built in China and getting help from them. It's going to be primarily the local workforce in the Saguenay to execute the project, but we are absolutely looking into getting help from the Chinese contractors who are building all the aluminium smelters. And we have a fairly good feel for the capital intensity and that we can deliver against that. And you combine that with attractive renewable firm power in Canada and support from the Government, and then suddenly the smelter actually makes economic sense for us.

You're absolutely right, you're pointing towards a difficult past. We just have to get this right with the capital intensity on the aluminium smelters. We all know that. That is our top priority. And so far, I certainly have a good feeling about the project.

Paul Young: Thanks for that Jakob. I guess the next question is, if it's successful the follow up is, what's the larger strategy here? Is it rolling into another smelter, using ELYSIS? What's the broader strategy if this is successful?

Jakob Stausholm: Good question. I mean, ultimately, we cannot do things that doesn't add value to the shareholders. But the reality is there is a lot of demand growth for aluminium.

Since the turn of the century, aluminium has constantly been growing in the world by 5%. That means that the market for aluminium is today three times bigger than it was in the year 2000. And particularly in the Western world there has been a declining amount of aluminium smelters and production capacity, so I do think that there is opportunities. But you need to crack a few things: firm, competitively priced renewable power, combined with control over your capital intensity. And if you can get that equation up and running, then I can see us further expanding. And we would love to further expand, particularly in Canada where there is excess energy available.

Rahul Anand (Morgan Stanley): I just wanted to touch upon the $800 million write-down. My understanding was that the Safeguard Mechanism mainly related to scope one emissions and not scope two. And, you know, just wanted to understand, what are the main reasons for this write-down and how can we compare that to the rest of the industry, really? Because I'm aware that as we progress to 2030, the targets will be heavily based on industry emissions rather than your own. Thanks.

Peter Cunningham: No, thanks very much for the question. So, I mean, for the alumina refineries the emissions are scope one. So they're half of our scope one emissions within Australia, putting it in context. That was the trigger, but when we look at the write-down then, I mean I think what we've seen is the industry structure around alumina really get pretty tough and so, you know, when we do the evaluation, there's the trigger and then what does the business really look like. It's a tough business, that business has had some challenges and we do need to put capital into those refineries around decarbonisation and other environmental matters.

That's what's really driven when we take it in the round, the valuation. I mean, the important point is that they just do remain critical in terms of our overall systems, as I say, for getting the bauxite through to the smelters. So they're a critical part of the system but we have had to take those write-downs given that evaluation and that outlook.

Anand Rahul: You've also highlighted the decarbonisation efforts potentially being stalled. If I stick to the original aluminium business, obviously PacAl, you know, you're looking to switch to renewables and be able to reduce your emissions there. Any updates there at all in terms of progress?

Jakob Stausholm: Yeah, look, you're absolutely right. The problem is that at least for the shorter-term period, the scope one is fairly given on a smelter because it's the carbon anode in the catalytic process. Now, we think we have, well, we know we have a solution but it's not a solution that can be implemented, you know, tomorrow, of ELYSIS. So that's a given one and that's regarding the safeguard mechanism, but the problem is completely different.

The problem is that 70% of Rio Tinto scope one and two emissions stems from aluminium and 50% of the total emissions is actually from PacAl, and is mainly scope two emissions, because we buy electricity from the grid and the grid comes from coal-fired power. And that needs to change. If we should meet our objectives of 2030 of having half our emissions, we have to solve the PacAl. But that is also in the nation's interest, because the government of Australia have got ambitious targets to reduce the overall CO_2 emissions of the country.

So I think we are very aligned, we just need to find a solution. And this is really large scale. It's kind of like people told me here what we are looking at in terms of solar and wind is like

12 times bigger than any other renewable energy park in Australia. So it's not something you just solve from one day to another. But I'm just very committed to give it everything, because this is one of the biggest Australian – one of the biggest industrial assets in Australia and it is actually a business that can underwrite a lot of renewable energy. But if we can't get firm renewable energy at a competitive price, it's going to be impossible for us to manufacture and export aluminium out of Australia.

So that's kind of a very different topic than the Safeguard Mechanism. Over time, with ELYSIS we'll solve the safeguard mechanism of cost.

Peter Cunningham: Yes.

Jakob Stausholm: The problem we have short term is of course to add cost to a business where we're actually not really making money. And that's why Peter comes to me and says I need to impair the asset.

Anand Rahul: Appreciate the complexity. Thanks for the colour, I'll pass it on.

Richard Hatch (Berenberg): Thanks very much for your time. Just a couple of questions on the assets. First one on Kennecott. You've talked about how you're looking to improve Kennecott. If I look at the costs in the first half, you're sort of annualising at about $1.4 billion. Previously you've annualised at about $1 billion to $1.1 billion. So clearly there's an uplift in costs there. Can you perhaps talk us through that? And then with the underground, what does that cost base go to and where's the opportunity in terms of margin expansion?

Jakob Stausholm: Peter, you can expand on it, but I just have to say, they just didn't have a good performance this year, because the real big issue – and I was there, I've been there several times – was we'd just got the Safe Production System running – working at the concentrator. And then we had the breakdown of the conveyor belt to the concentrator. And this is the problem with Kennecott. It's an amazing asset if each part works, because it's one big flow here. And right now, of course, we have an extended shutdown of the smelter. It's the biggest rebuild in a decade. So it's just not been a good run but I'm absolutely convinced that we are doing the right things for the long term. This is a time where I have a good feeling that it will perform well in the future. But this year I just have to lie down and say we haven't had good performance from Kennecott.

Peter Cunningham: Richard, I think you're still carrying elevated costs. You know, from diesel inputs – it's a heavy diesel site – and also it's tight on labour. So you've got that sort of piece embedded in it. But most of the increase is actually to do with the fact that on the one hand we've had the smelter rebuilt, so that's additional opex costs, and we had some disruptions on the mine as well through the conveyor failure we had.

A lot of that is temporary but there's a tranche there that is sort of to do with that labour cost. I mean the key point on sort of diesel and other factors in our business is that we didn't really see benefits in the first half of the year. But we will start to see those come through in the second. And I think, I just want to emphasise that, that while you've seen Brent come down 25% in the first half of this year vs first half of last year, you're probably not going to see that translate into real cost reduction until the second half. And there's going to be some regional factors as well that moderate that.

So I would expect some underlying reduction. There's some cost pressures and there's temporary factors that will come out as we restabilise the operations.

Richard Hatch: Thanks, appreciate the colour. And second follow-up with a follow-up on IOC. Another one that's been a bit of a challenge operationally. We've talked about it before, how you're trying your best to try and improve it. Can you get to that 90 million tonne target? And again, costs seem to have blown out there first half. Appreciate there's a wildfire impact but, you know, what's going on with that asset and how are you turning it round?

Peter Cunningham: I mean, on IOC it is mostly a volume issue. Because we lost – due to the forest fires, we effectively were stacked out. We lost a complete month of production in June. So actually it was performing – through the mine and concentrator we've seen better performance. We've actually the Safe Production System go through the concentrator already. We've really seen an improvement in performance. But it's really been the fact that we lost volume in June that drives sort of fixed cost inefficiencies across the operation.

So I actually think we are seeing some underlying improvement. I mean, unfortunately it's kind of two steps forward, sometimes one back with IOC, but we are making progress, I think, in terms of getting a more stable operation and moving that forward.

Unfortunately, forest fires, that's something we couldn't do anything about.

Jakob Stausholm: You can't control that. But you're pointing towards something important and that is, in many of our assets – not Oyu Tolgoi, but in many of our assets and IOC in particular, we have too many equipment failures. It's easy to say maintenance, but we just need to find a way where we have less equipment failures. Because it just destroys of what we are trying to do with Safe Production System is all the right things, but if you turn up to work early in the morning and you've got these equipment failures, that's going to be your priority number one, two, three and four. That means that you can't do the improvements you want to do.

And that is in a nutshell, I really feel for them. I think it's a great team we have at IOC. We will overcome it but it's hard to go through.

Alain Gabriel (Morgan Stanley): Thanks. One question from my side is, if you go to slide 10 and – which is the EBITDA bridge – and you flip it to H1 versus H2, what are the key components that we need to think about? Clearly Richard touched on a couple of points, but can you give some numbers or put some ranges behind the buckets that we need to think about in terms of profit bridges, H1 versus H2, non-repeatable costs?

Peter Cunningham: On costs what we're seeing those market factors have lagged in the first half. They will come through much more in the second half. So you'll start to see the diesel come through, you'll start to see raw materials and aluminium. We sort of had about $100 million benefit in the first half but that is starting to flow through from the petcoke, pitch and caustic coming through the aluminium cost base. That will accelerate. Maybe $150, $200 million, we can already see of benefits in the second half of the year on that alone.

So there's those factors that are there. There's some factors coming through that in the first half, where we just had contracts that are indexed to inflation, and they came through the second half, they'll be with us in the second – first half they'll come – be with us in the second half. And then there's tightness in the labour markets. They're the three buckets that I would say.

So we're seeing certainly downward influences from those market factors. We are seeing some lagged inflation factors come through and some ongoing labour market factors that drive costs up. Those are the three buckets.

Alain Gabriel: And including the impact of the fire and the impact of the other one-off items that we've seen?

Peter Cunningham: Well, we'll certainly see. I mean, IOC is getting back up to full operation in July, so we would hope that the one-off factors don't return. So you've certainly got IOC running at full production, you've certainly got Kitimat now at 90% production capacity and gaining that last 10% through the year. That's a big positive. Because Kitimat so far hasn't given us too much extra earnings, because we've had the costs of sort of ramping up against the additional volume. But as we get in the second half, we start to see those benefits come through. So I think some of the aluminium business has got some real tailwinds as we go into the second half around raw materials and around volume, that will be positive.

Kennecott will – you know, we've extended the smelter shut in September, but again, starting that up is absolutely critical. That's a key part of second half, getting that right. And we would hope to be back up, ramping up towards full capacity in the smelter in the last quarter.

So certainly, some tailwinds as we go in the second half, Alain.

Jakob Stausholm: The good news is – it's terrible with the wildfires we have around the world, but we've actually had an awful lot of rain in Canada here in July and this is super important for two reasons. First of all, it stops the wildfire; and secondly, it fills up our dams as well.

Lyndon Fagan (JP Morgan): Thanks very much. My first question is just back to the Simandou capex on slide 16, if I look at the chart, there's about $5.5 billion of spend between 2023 and 2025. Can I confirm that that's Rio's 45% share? And if it is, it's implying $12 billion over that time, so just keen to explore that a bit.

Peter Cunningham: That is right. It's our share, yes. But remembering our share of the mine and the whole infrastructure.

Lyndon Fagan: So is that 45%? Just to confirm?

Peter Cunningham: That is our share. So of the mine, we are effectively 53% owner through our arrangements of the mine. And then of the infrastructure, that would be shared with the one and two consortium, 50/50. And our share is 53% of 50, if you like.

Lyndon Fagan: And so, I guess the other way of asking it, what's the 100% number, if that's $5.5 billion?

Peter Cunningham: We don't – because, I think, as we said, we're in the midst of negotiations around this, we're not going to give the complete picture. But we wanted to be as transparent as we could be as to what this was of our capital. So I think we've shown that's our share, Rio Tinto's share, of the capital for the next, you know, two and a half years. And we'll give that fuller picture when we've got those full negotiations clear. I just think that's – we've gone as far as we could, I think, to be as transparent as we possibly can be with you at this moment in time.

Lyndon Fagan: Thanks, okay. I'll ask my follow-up. Just on the aluminium investment, the $1.1 billion for AP60, can I ask the question why now? We've got the aluminium industry at a cyclical low. Clearly there's no requirement for additional capacity in the aluminium industry at the moment. Why not defer that spend further and even if it involves taking capacity off-line, why not explore the notion of value over volume in aluminium? We spoke about it for years and years in iron ore but I guess it's sort of perhaps needed more in aluminium these days.

Jakob Stausholm: Yeah, look, the reality is of course it's supply and demand. And the price doesn't matter the next few years when you're constructing an aluminium smelter. What matters is when it's up and running. So it's difficult to say what the market conditions are by then, so you have to think about what is your long-term belief in this market. And there is a couple of very good reasons why now.

First of all, it is about future-proofing the Western world's largest hub of aluminium smelters, which is in the Saguenay. And we have to start closing down our Arvida smelter. It was built in 1926 and we will have to finalise it before it has its 100 year anniversary. So it's actually in a way a replacement volume.

Secondly, the Government was very interested, of course, in protecting the employment in the Saguenay. And that's why they have come in and provided subsidies for this investment. And we have been able to secure very competitively priced firm power.

So you take those things and you grab the opportunity when it fits other stakeholders. I think it makes imminent sense to do right now. Thank you.

Hayden Bairstow (Macquarie): Back on the aluminium and minerals businesses, and obviously this is a guess, I mean the cash generation's pretty low, the ROCE's obviously not great either and obviously commodity prices are depressed. But as you go through the whole decarbonisation strategy here, do we need to just think about these business just really not going to be big cash-flow generators for four, five, six years, however long it takes you to go through this decarbonisation process? And outside of copper in Peru, we'll just be heavily reliant on iron ore?

Jakob Stausholm: I don't think so. I – we have a very cash-generative aluminium business in Canada. Yes, we are challenged on the Pacific Aluminium business in terms of profitability. The profit was around zero for the first half of this year, but it just highlights the point of how important it is to find competitively priced energy. And then we have the double challenge of also making sure that it's renewable energy so we can reduce our CO2. But, well, it's just a good challenge for us.

Peter Cunningham: Yeah, and just to add to that, I think in the first half, the cash flows weren't as strong. And there are several reasons for that. I mean, one, bauxite was highly challenged because we had really, really tough in the north of Australia, which really disrupted our operations. So we did not push the volume through that we usually would. We would expect that now, we're on a good run into the second half the year.

The alumina segment was very challenged as we've sort of talked about in the first half. We are seeing the key caustic price come down again, which I think positions us better.

And thirdly, I think in the second half of the year, we will have Kitimat really ramping up. That gives us a tailwind as well as those raw materials.

So I think the first half don't see that, Hayden, as probably representative of really the cash-generating capacity of that business. It was an unusually low period.

Hayden Bairstow: Okay. And then just on the lithium Rincon stuff. The capex, is it really specific to Rincon or does it make you think a bit differently about lucrative investments in terms of there's assets out there where the capital has been sunk and it hasn't been exposed to all this inflation? Does that sort of change the way you think about operating assets versus the longer-term growth assets like you've got in the portfolio now?

Peter Cunningham: Hayden, I think the answer there is probably no. In that, you know, that – when you're talking about Rincon 3000, that starter plant, we took the decision very deliberately to commit to it very early so we could get the learnings and when we did the studies for a much larger operation, we could incorporate all of that into the learning. So, it was taken, you know, very early after the acquisition that we did that.

The increases in the capital are not so much inflation, they are scope and definition as we've gone through that now. Really locked down what that starter plant looks like.

So it's not great that the capital's gone up like that but I think I'd much rather it went up on that initial plant than when we have to commit to, you know, something much bigger, as those studies progress. So I think we are really seriously learning about how that – both the technology works and also operating in that location. So I think we're certainly in much better place for doing it, but yeah, the capital is up.

Robert Stein (CLSA): Hi team. Thanks for the opportunity and good morning. The PacAl business, obviously big energy consumer and, you know, with electricity prices and potentially energy scarcity on the east coast of Australia, does that factor into your decision making around the future of the asset in terms of the broader societal need, given that is running at a lower margin? Is that energy better used in the Australian brief?

And secondly, how does Rio Tinto stand to benefit from any type of energy off-take that then gets released back onto the grid in that situation?

Jakob Stausholm: It's a very big question and it's a question I cannot answer. It's a societal question you're asking there and you should probably ask the Australian Government about that. But I would say to you your question is also a little bit about the chicken or the egg, because yes, on one hand you could say it could be used elsewhere, but another way of looking at it is saying it's only those assets, because they are the biggest electricity users in Australia that can actually underwrite renewable energy. If those assets were not there, there would probably not be the market for making large-scale renewable energy. And right now, particularly Queensland, of course, is going through a major transition. An economy that depends very much on two industrial sectors of coal and aluminium, and underwriting renewable energy there could be very beneficial in that transition. But a very good question, a societal question you probably should ask elsewhere. Thank you.

Patrick Mann (Bank of America): Just on the – I appreciate it's early days, but the studies into green iron ore, low carbon iron, in Australia. Would you consider investing downstream to produce some kind of green iron for customers, or do you think more – I think some of your peers or competitors have thought more along joint ventures or collaboration with steelmakers there? And how are you envisioning it working? Thanks.

Jakob Stausholm: Look, we are open. I mean, we're trying to – we as a miner, as I said earlier, we're both miners and in processing. We're not steelmakers. We're not really interested in going too much into steelmaking.

But yes, I could easily see us being part of a joint venture that secures the supply of iron ore in terms of the reduction to green iron. So that's certainly something we could participate in. But we definitely need someone who's really, really good manufacturers, because if we're trying on our own, I think we have some history around that and other companies as well, and that's not really what we're aiming for.

Myles Allsop (UBS): Maybe we haven't talked about the markets. Obviously, the Politburo announcement got everyone a bit excited this week. I mean, are you, you know, as you look at and talk to your guys marketing iron ore, are you raising your expectations for demand for steel and iron ore in the second half? And medium term, do you think $110 is a sustainable, $115 is a sustainable iron ore price? Thank you.

Peter Cunningham: That, Myles, I think when you look at it, you know, steel demand in China's been pretty flat year on year so far. But we're still seeing extremely soft property market. I think it all depends how that flows through. You're seeing, management of the economy through the government pretty carefully, and I think we'll just have to see exactly how they pull various levers on stimulus into the second half to meet their objectives in terms of growth. I think, you know, we'll just have to see how that plays out.

Jakob Stausholm: I think we still remain cautiously optimistic on the Chinese economy. They have demonstrated again and again, if there is a setback, they're able to stimulate the economy and manage the economy in an effective manner. But time will tell.

Danielle Chigumira (Credit Suisse): A question on the emissions flight path. So you spoke about not being able to achieve the 2025 initial target. Of the buckets which you identified, which is the biggest culprit? So, permission of renewables, diesel replacement, and process heat abatement. Which is the biggest culprit, and does it have any implications on meeting the larger 2030 target for emissions reduction?

Jakob Stausholm: Well, it's a bit more complicated than that. Our focus is really about getting everything done in order to achieve 2030. We thought we could get to minus 15 but I will say to you, when we announced those targets, we said we might be using credits but it's the last resort. So we can still achieve 2025. We're just coming to the conclusion we can't achieve it without credits, because certain things take longer.

And I tell you there's another reason, which is terrible but good. That is, this company is suddenly growing faster than we had expected. And when you grow fast and you have an absolute number on CO_2, it starts getting difficult for you.

So there's numerous factors but the reality is just I think we have some wonderful breakthroughs in technologies such as for example the green smelting that we have the site in California running, but, in aggregate, it's just difficult to move these things forward. The Western world is not moving very fast forward on renewable energy. That's just a fact.

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