21 August 2019

Half Year Results 2019 – Teleconference Transcript

Speakers
- Tom O'Leary - Managing Director and CEO
- Adele Stratton - Chief Financial Officer
- Christian Barbier - Head of Marketing

Start of Transcript

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Iluka Resources Limited 2019 half year results call. At this time, all participants are in a listen-only mode. After the speakers' presentations, there will be a question-and-answer session. To ask a question during this session, you will need to press star-1 on your telephone. Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Managing Director, Mr Tom O'Leary. Thank you. Please go ahead.

Tom O'Leary: Thank you. Good morning. I am Tom O'Leary, Iluka's Managing Director. With me this morning are Adele Stratton, CFO; Christian Barbier, Head of Marketing; and Melissa Roberts, General Manager Investor Relations and Commercial.

Let me start by saying the first half of 2019 has been a busy period of delivery for the Company. We've commissioned the Cataby mine, which is now performing at nameplate capacity. We've completed the planned major maintenance outage at the SR2 kiln to enable it to deliver synthetic rutile production for the next four years, underpinned by the take-or-pay contracts which support Cataby's development. We've just completed our mine move to the Ambrosia deposit from Jacinth, which has now begun delivery of heavy mineral concentrate from the new pit. The move has been completed not only ahead of schedule but also under budget by around 20%.

In Sierra Leone, we've decommissioned the dredge, completed the doubling of capacity at our Gangama mining front, and we're currently commissioning the Lanti expansion. These are vital projects to maintain current operating levels and to continue to deliver our high value products of zircon, rutile and synthetic rutile. We also continue to progress the next phase of projects in our pipeline and I'll provide some more detail on these shortly. As you can imagine, it's been a pretty busy six months.

On our financial results, Adele will take you through some detail in a moment, but I'm pleased with our performance. Our net profit after tax is up 9% to $137 million and our operating margin has increased to 43%. You'll also have seen that we've declared a fully franked dividend of $0.05 per share, even though we had a free cash outflow of $65 million in the first half. Our dividend framework is to return 40% of free cash flow not required for investing or balance sheet activity and we've determined the interim dividend, taking into account a range of factors including the payment during the first half of the $127 million final tax instalment for last year.

Our Mining Area C royalty contributed $41 million to earnings in the half, which was reflective of higher iron ore prices. As I've mentioned in the past, we're about optimising returns to shareholders from all our assets and this is also true of the Mining Area C royalty. As commencement of mining activity draws closer, I note that the South Flank development will enhance Iluka's capacity to pay dividends in coming years.

Moving to mineral sands markets, as you'll be aware, in the zircon market the seasonal slow start to the year lasted longer than expected, contributed to by uncertainty in global markets during the second quarter, and that affected consumer sentiment and ultimately purchases. This led to greater demand for concentrate and standard grade zircon products and as noted in the quarterly, there has been more standard zircon available in the market. Iluka's production flexibility has allowed us to respond to this shift and we're offering standard zircon volumes to our customers as part of
our product suite. We've focused on meeting customer requirements and supporting customer relationships while ensuring we deliver sustainable value from a diminishing resource. I believe we're well placed to adapt to changing conditions in the zircon market and we continue to believe that market fundamentals over coming years remain solid.

In titanium feedstock markets we continue to experience strong conditions with sales continuing to be constrained by production. This has been driven by the improved outlook in the pigment sector with high utilisation rates across most major producers. Price increases of 6% to 8% are expected for rutile and synthetic rutile in the second half. With respect to our operations, while first half Group production is marginally down on the first half last year, this is a consequence of the operational changes that were expected to occur in 2019 and I'm pleased with the delivery of significant projects, as outlined earlier.

At our main zircon mine, Jacinth-Ambrosia, operations continue to full capacity and as noted, we're now mining in Ambrosia. In Western Australia we commissioned our new Cataby mine which is now producing ilmenite feedstock for our kilns. In preparation for receiving that Cataby ilmenite, the synthetic rutile kiln underwent a planned major maintenance outage in the half, its most significant since commencing operations in 1997, and was returned to full capacity. Pleasingly, we're now producing synthetic rutile from Cataby material as well as high quality rutile and zircon.

At our main rutile mine, Sierra Rutile, the expansion project at Gangama has been commissioned, reached design capacity and is performing well. The Lanti dredge was decommissioned uneventfully in the period ahead of expansion at the Lanti dry operation which is nearing completion. While existing operations at Lanti have continued to perform below our expectations, we're implementing a number of improvement measures and continue to focus on achieving operational stability from this asset.

At this point, I'll hand over to Adele.

Adele Stratton: Thanks, Tom and good morning, everyone. As Tom has already mentioned our net profit after tax increase 9% from last year to $137 million, with product prices being a key driver. Zircon prices have increased 19% from the first half last year with Iluka having maintained the reference price of US$1580 per tonne for 12 months through to 30 September. Today, we announced that we will continue to hold the reference price flat for a further six months through to 31 March 2020. We believe that it is important to provide stability and certainty to our customers.

Rutile prices have increased 22% from the first half of 2018 and we expect further price appreciation of between 6% to 8% in the second half of this year. On the other hand, sales volumes are lower across all products. Sales of rutile have been constrained by production with the prior year benefiting from the inventory drawdown of the remnant Murray Basin material that is now fully depleted. Synthetic rutile sales are lower following the 45-day planned major maintenance outage earlier this year ahead of the next four-year kiln campaign, and as Tom has noted, zircon sales are lower than we had originally anticipated on the back of global uncertainties particularly impacting China.

The average Australian dollar exchange rate weakened to $0.70 from $0.77 in 2018, which had a favourable impact on revenue of $52 million with the majority of our sales contracted denominated in US dollars. Unit cost of goods sold has increased to $861 per tonne. Synthetic rutile unit costs are up, reflecting increased ilmenite feed costs since the completion of mining at Tutunup South in early 2018. At Sierra Rutile the translation of the US dollar-denominated cost base into Australian dollars has been exacerbated by the weakening Australian dollar, with the actual US dollar cash unit cost being $39 per tonne lower this year than it was in the prior year. Mining Area C continued its positive contribution to the Group's results with an EBITDA of $41 million on the back of higher iron ore prices.

Turning to the operations performance. Jacinth-Ambrosia continued to operate at capacity, generating an EBIT margin in excess of 75% whilst Cataby provided an EBIT margin of 43%. Cash costs of production increased in Australia, reflecting the commencement of mining and concentrating at the new mine in Cataby. Sierra Rutile on the other hand had a disappointing performance, generating a loss before interest and tax of $6 million in the period. The first half performance has been impacted by the transition of operations with the dredge being decommissioned and both dry mines only commissioning the expansions late in the half, and this has impacted the ability to absorb the high fixed-cost base. The focus in the second half will be on delivering consistent performance from the Lanti and Gangama mine as well as the ramp-up at the Lanti expansion.
Cash generated by operations in the half was $180 million, and I note there’s been a build of inventory of $43 million relating to both ore and HMC at Cataby as well as some finished zircon product. The free cash outflow of $65 million was impacted by the tax balancing payment relating to last year of $127 million, with total tax payments in the year of $144 million. We’ve also invested $145 million of capital into projects, including $49 million on the Cataby development, $30 million for the planned major maintenance outage of the kiln, $16 million on the Ambrosia mine moves and $42 million at Sierra Rutile.

We’ve successfully completed the refinancing of our debt facilities post the half year, extending the tenor out to five years and also achieving a reduction in the margins on the facilities. We have reset the financing capacity to $519 million to lower costs on undrawn [money]. We continue to focus on maintaining a strong balance sheet and July has been another positive month with net debt reducing to $109 million from $142 million in June.

With that, I'll hand back to Tom.

Tom O’Leary: Thanks, Adele. As you can see from our project pipeline on slide 21, we continue to progress a number of options for maintaining and for growing production. We’ve provided some additional detail on some of these projects in the slide pack.

First on the Eneabba Mineral Sands Recovery Project in Western Australia, we can now confirm we’ve contracted offtake for 50,000 tonnes of production per annum of the monazite concentrate for two years and the project is moving forward. Construction will commence in the fourth quarter this year and first sales are expected in the first half of 2020. This is a low-risk, low-capital project that delivers strong returns as well as reducing an ongoing rehabilitation obligation.

The Wimmera project in Victoria is a large long-life project with zircon and rare earth product streams. Pilot plant test work has been successful and the PFS is progressing on schedule. At Balranald, the Board has now approved the final field trials for this new technique. Pending the results of the trial, we are aiming to develop this substantial rutile and zircon resource in the next few years.

Finally, to our outlook for the remainder of the year, we’ve updated some of our guidance parameters. We foreshadowed in the June quarterly we expected zircon sales to be second half weighted. Current indications are that sales will be at the lower end of expectations with second half sales volumes now expected to be similar to the first half. We continue to support our loyal customers through our rebate system and through a flexible product offering which will include more standard zircon product. As a result, we expect a lower average realised price in the second half. Iluka expects to carry forward some inventory of higher-value premium zircon and as a consequence of the greater availability of concentrates in the first half. Iluka also expects producer-held inventories generally will rise over the second half.

On slide 26 you'll see that we've updated guidance on capital expenditure, depreciation and unit cost of goods sold. One of the drivers of the reduction in capital expenditure guidance is the delay to the start of the stage one early works for our Sembehun project which we announced at the June quarterly, as we revisit and broaden the value optimisation studies with a focus on determining a development option that's both fit for purpose for Sierra Rutile and optimises the risk-return relationship. While we're committed to directing our efforts to achieving acceptable stability and performance from our assets in Sierra Leone, we're pleased that a number of key projects have been successfully executed which support production of our key products for the medium term.

Looking beyond 2019, Iluka is well-positioned as we're able to turn our focus to our portfolio of mineral sands and rare earth projects that will continue to progress. The context remains positive as grade decline and mine closures drive global reductions in supply over coming years. As we move forward in a period of some uncertainty, we'll continue to make investment decisions and pursue market strategies which we believe will deliver sustainable value.

On that note, I'm happy to take any questions.

Operator: Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. If you wish to ask a question, please press star-1 on your telephone and wait for your name to be announced. If you wish to cancel your request, please press the pound or hash key. There will be a short silence while questions are being collated. Thank you for your patience.
Our first question comes from the line of Jack Gabb from Bank of America. Please go ahead.

Jack Gabb: (Bank of America, Analyst) Thank you and morning, Tom and team. Just two questions from me. Firstly, just on the zircon market, you previously said a move to more standard zircon would cut pricing by $50 to $100 a tonne. Does that still hold based on your updated guidance today? And the second quarter is just on Sembehun, I guess quite a lot of - or a lack of detail in the presentation. Can you give us a sense on the timing of this project now and whether you've cut CapEx guidance for this year but should we assume lower CapEx for next year going forward as well? Thank you.

Tom O'Leary: Yes. Thanks, Jack. I'll hand over to Christian in a moment for any comments he might have on the zircon market more generally, but I might just say a few words about that market. We've noted at the quarterly that the pricing for zircon typically sells at a discount of the order that you indicated and that we are starting to move into that market but the conditions in the market are difficult and we've indicated that we expect to see a lower weighted average price over the second half. This is really a consequence of the engagement we've had with customers over the last period where they're reflecting back to us the conditions they see in the market and what we've provided to you is our best assessment of the second half of the year, that sales are going to be evenly weighted with a lower weighted average realised price.

I think we need to look a bit beyond the next six months though and take a broader and longer view of the market. The market is a complex one at the moment with trade tensions across the board and with Brexit, and Iran, Turkey, India faltering; the list goes on. At the same time, concentrates have been mobilised and we talked in the quarterly about the consequences for that. You will have noted that we've decided to hold the reference price flat for a further six months now and that takes one level of uncertainty out of the market for our customers and allows them to go on and make their decisions with some clarity. We'll again observe over the next six months what happens both in terms of demand from various regions, what happens in terms of supply from concentrate processors in China as well as Indonesia. We'll also look carefully at our customers behaviour.

Overall, and I'm looking at the longer period, I think the market fundamentals remain solid. As I think about that, I look back over the last few years, and you'll remember, Jack, that just a couple of years ago the market was very concerned about Iluka production falling this year as a consequence of JA grade decline, and with bringing Cataby on and accelerating the Ambrosia mine move, we've managed to smooth production ahead of time and under budget. It illustrates for me the ease with which Iluka has been able to allay that fear of grade decline this year. We've also demonstrated in the last couple of years the ability to introduce ZIC into the market as a swing producer at minimal cost. So, the fact that global demand is relatively flat at the moment and we are seeing ourselves and others carrying forward inventory means that that supply deficit we've talked about is being pushed further out. You might have noticed that Tronox reported a build of inventory in the first half and sales cut by reference to last year. So, to my mind the fundamentals remain very sound for Iluka over the - and for zircon sales over the longer period, and by comparison to others, we don't need to bring significant fresh mining and infrastructure to bring on additional tonnes, and so I have to say that new entry into the market appears pretty unlikely, in my opinion.

We also mentioned that we - as I said, we're going to bring some - take some inventory forward and I think that's a really appropriate response to the modest surplus in product that we've seen in the market. We don't plan to build massive inventory. I'm not going to be drawn on how much inventory we're prepared to build but we'll keep a careful eye on the situation over the coming period. I think it's important to give that broader context about the market and really ensure that we remain focused on the longer term as well as what might transpire in the next six months.

I don't know Christian, if you want to add anything to that on zircon pricing.

Christian Barbier: Yes, maybe. Jack, this is Christian Barbier. Just to come back on your question regarding standard zircon, standard zircon prices have suffered in China over the last few months and weeks due to very soft demand, and also due to a higher import ratio of concentrates versus finished sands. But as you know, Iluka is weighted towards the premium segment so it hasn't affected us directly very much so far, as you can see in our reported prices. However, in the downstream markets, millers are under tremendous pressures from their customers, the ceramic tile producers, and are sacrificing margins in order to compete which in China has reduced in size, so a lot of millers are shifting towards
standard zircon for part of their production. Hence, the decision that we have made to support our customers and help them compete in that market. This is why we have a product mix change in the second half of the year.

**Tom O'Leary:** Jack, just to your second question on Sembehun, no, we don't have a lot of detail about it in the presentation. As we mentioned at the quarterly, we're pausing to broaden and revisit the optimisation studies and just the general approach to Sembehun. Again, as we outline in the quarterly, in that revisiting of optimisation of value there, we are open to changes to mining method, to the target volume, to the timing of commencement, so that it's quite a broad review and so we're going to be thinking very widely, thinking laterally about alternatives there, and Matt Blackwell and his team are very much engaged in that process. It's also worth noting that we also need to see a period of operational stability from our mines in Sierra Leone before we embark on further investment there.

**Jack Gabb:** (Bank of America, Analyst) Thanks. Can I just follow up on that, because I think when I asked on your quarterly, I said is there going to be a gap between when Sembehun is commissioned and obviously when Lanti and Gangama end, and at that point there was no clear-cut gap that was going to be created, but if we need stability to be achieved it sounds like that maybe there will be a gap. Is that right?

**Tom O'Leary:** Well, it's a bit of an open-ended question, I think, Jack. I expect we will achieve operational stability in the near term, so we're not expecting a gap at this point.

**Jack Gabb:** (Bank of America, Analyst) Okay. Thanks, Tom and I'll hand it over.

**Tom O'Leary:** Thanks, Jack.

**Operator:** Thank you for the questions. Our next question comes from the line of Paul Young from Goldman Sachs. Please go ahead.

**Paul Young:** (Goldman Sachs, Analyst) Morning, Tom, Christian, Adele. Tom, first question is on the zircon market. Did I hear correctly that you said that you expect sales in the second half to be in line with the first half and therefore that implies sales of 260,000 tonnes for the full year?

**Tom O'Leary:** Yes, that's right. We said broadly in line with the first half and the first half was 133,000.

**Paul Young:** Okay. So, you sold 380,000 tonnes of zircon in 2018. It's a 1.2 million tonne market. That's a fair drop in a sizeable market. The question for me, and you actually reference Tronox and their commentary on sales, they actually said that they expect their sales to increase in the second half. The question I have is that - two things - is that are you having to pull back your sales in the second half because your major competitors aren't pulling back? Second, are you seeing any - back to Christian's comments about the downstream being weak - are you seeing any substitution at all or is this cyclical, not structural, these lower sales?

**Tom O'Leary:** Paul, I can't talk about the reasons we're pulling back on sales and taking inventory forward by reference to competitors. I can only really comment on what we're doing. I think - I've mentioned on inventory that we are planning to - we are expecting to build some inventory in the second half. The question I have is that - two things - is that are you having to pull back your sales in the second half because your major competitors aren't pulling back? Second, are you seeing any - back to Christian's comments about the downstream being weak - are you seeing any substitution at all or is this cyclical, not structural, these lower sales?

**Paul Young:** (Goldman Sachs, Analyst) Thanks for confirming that second half sales number; that's fine. Moving on to the monazite, Tom. There's been a lot of talk for maybe six months now on this project. I see you've signed an offtake for 50,000 tonnes per annum. Is this just the start? Do you expect that maybe you can - it will all come down to end demand and plant capacity with your major customer in China, but could we expect further offtake, an increase in offtake beyond that level? Also, I know you stated here that pricing is commercial-in-confidence, but can you help us out with a percentage margin or a dollar-per-tonne margin that you think that you might be able to achieve to help everyone out there?
Tom O'Leary: Paul, I really can't help much there, to be honest, but because the terms of the contract are confidential, as we've indicated, we haven't indicated that it's a customer in China as you implied there. But just broadly, you'll have no doubt seen reference prices for monazite that are available from industry commentators or around the place. If you were to deduct from that a processing cost as well as a margin for our customer processor, you will come to a figure, and for a received price for monazite, and then with the information on the slide you can work out how much monazite is in the product sold and the - and you'll come to a price.

In terms of the amount, this could be the beginning, and there may be more, but this is very much a sufficient contracted volume to get on with that project.

Paul Young: (Goldman Sachs, Analyst) Okay, all right. That's very helpful. Thank you, I'll pass it on.

Operator: Thank you for the questions. Our next question comes from the line of Rahul Anand from Morgan Stanley. Please go ahead.

Rahul Anand: (Morgan Stanley, Analyst) Hi, everyone. Thanks for the opportunity. Just a couple from me. Firstly, if we can quickly talk about the production costs. I noticed the cost of goods sold have been bumped up, but I also wanted to touch on the production costs and just try to investigate whether those have gone up alongside as well or is it just basically that inventory that you flagged that's leading to COGS. That's the first one.

The second one is around dividend, Tom. How should we think about it going forward considering we had negative free cash flow this period and we've still seen a dividend come through? What are your thoughts around going forward the level of gearing and potentially dividend payouts?

The final one is around the zircon and rutile markets. Rutile, you spoke about inventories now having normalised. What levels were they and where are they now? Then in terms of zircon as well, how are you viewing inventories in the downstream at this point in time? Thanks.

Tom O'Leary: I'll hand over to Adele, I think, Rahul.

Adele Stratton: Yes, Rahul. In terms of cost of goods sold, so Rahul, let's start with the question around cash costs of production, so those have increased because obviously we've commenced mining at Cataby. The cash costs of production reflect your operating activities. Given we weren't operating at Tutunup South last year then there were no related mining costs in association with that. As we mentioned in terms of the Cataby development, it is underpinned by those commercial contracts because the ilmenite costs are a bit higher than what they were at Tutunup South due to the tyranny of distance from the klin.

Coming back to cost of goods sold, there's a combination of factors that impact that. One is mix, so depending on how much - as I spoke about, the margins between the different operations are quite different and therefore, depending on if you've got more product coming out of Jacinth-Ambrosia, for example, that will reduce your unit cost of goods sold from a Group perspective. So, sales mix does play a part in terms of that total cost of goods sold number for the Group.

Also, as I mentioned, in terms of Sierra Rutile, that's a US dollar base but with the Aussie dollar where it is, just sheer translation into Australian dollars will inflate those costs just on a translation perspective. I think there's a combination of factors that have driven the increased unit cost of goods sold, being as I said, mix, translation of SRL and some higher ilmenite feed costs going into the SR2 production would be the key underlying factor, but when you look through to the operational levels they're still making very good margins. I don't know if that helps.

Rahul Anand: (Morgan Stanley, Analyst) Basically, I understand COGS is impacted by the mix and that's why I wanted to sway away from that and go into pure production costs and see if there's any other movements there that we need to be aware of going forward.

Adele Stratton: No. It's all in line with expectations in terms of cash cost of production and the unit costs from the operations. As we've mentioned, SRL, obviously there are higher depreciation charges at the SRL which were flagged in the guidance outlook. That will have a flow-on impact through to unit cost of goods sold because it looks at both cash and non-cash, but otherwise no, no material changes.
Rahul Anand: (Morgan Stanley, Analyst) Okay, brilliant.

Tom O'Leary: Rahul, on the dividend, how to think about it, for the moment our dividend policy is unchanged and I think you well know it. With negative cash flow we've looked through that a little bit and taken cognisance of the very significant tax payment that was due and was paid in the first half and we've explained that in the past as well. It's a nuance of the tax system, the timing of that payment. So, we've looked through that a bit and looked at broadly free cash flows that are expected. So, that's that.

In terms of how to think about dividends over coming years, until we say otherwise then our policy remains as it is. I've just noted there that with the looming onset of the Mining Area C cash flows from South Flank it will enhance our capacity to pay dividends. In terms of our balance sheet framework, on slide 10 we've talked a little bit about that and that's unchanged as well.

Rahul Anand: (Morgan Stanley, Analyst) So basically just investment grade rating in terms of credit going forward?

Tom O'Leary: Sorry, Rahul, can you just repeat that?

Rahul Anand: (Morgan Stanley, Analyst) Yes. I was saying, so the policy remains just investment grade balance sheet going forward and you're happy to take on a sensible amount of debt within that framework?

Tom O'Leary: Yes. I think that's right.

Rahul Anand: (Morgan Stanley, Analyst) Yes. Okay. Then finally, around zircon and rutile, please, the inventory levels that I was talking about.

Adele Stratton: In terms of inventory, we've mentioned, Rahul, in the half, so inventory has increased but a lot of the driver in the half is to the build of ore and HMC at the Cataby operation. There's a small build obviously, when you look at sales versus production of inventory, as we've noted that sales are a bit lower and hence it will drive inventory on the balance sheet. I think we're at $40 million from December where we called it; normalised levels is in that range.

Rahul Anand: (Morgan Stanley, Analyst) Okay, apologies. I was actually talking about the broader markets, just in the markets at the moment. It was mentioned that rutile inventories have now normalised and - sorry, pigment inventories have now normalised. I'm aware they were elevated as well; just wanted to see what are the levels they're at, at the moment. Then the same thing for zircon. What are you seeing in terms of the Chinese levels of inventories in the downstream at the moment?

Tom O'Leary: Okay. Got you, Rahul. I'll pass it over to Christian.

Christian Barbier: Yes, Rahul, this is Christian Barbier. You're aware that in the pigment industry one of the main players has been implementing a so-called value stabilisation programme to adjust the level of inventory. It seems to have played out very well over the last six months. What we see is that there is through their reduction of sales volume the pigment market is now stable. Sulphate pigment prices have been stabilized and we've seen in some geographic areas chloride pigment prices increasing. So, to answer your question, yes, it seems that pigment prices - the pigment inventories downstream have stabilised.

Regarding zircon, with the softening economic conditions and the uncertainty of the global economy, we have noted that customers across the value chain have been very cautious in the first half of the year. We believe that downstream inventories now are fairly reduced. We don't see any build-up of inventory downstream. People are very cautious and have been drawing down on their stocks. Even in China, there is no significant inventory. You may see some inventories in concentrate processing plants but that's the nature of their business. They buy bulk - bigger quantities and release them progressively as they process them.

Rahul Anand: (Morgan Stanley, Analyst) Okay, understood. That's very helpful. I'll pass it on. Thank you, everyone.

Tom O'Leary: Thanks, Rahul.
Operator: Thank you for the questions. Our next question comes from the line of Paul McTaggart from Citigroup. Please go ahead.

Paul McTaggart: (Citigroup, Analyst) Hello. I just wanted to circle back to zircon. Is the problem - so if you look at property starts, they're up strongly [unclear], but if you look at completions they're down 10% year-to-date. Is it - the weakness that we see in the market, is it simply a reflection of those weaker completions and do you have a sense of why that is, why we've got property starts up quite strongly in China but the fact completions are down?

The second part is really around the reference price. The way we model, obviously we have a reference price and then we've got to have some kind of realised price against that, but my question is if you're not realising the reference price or less and less material is being sold at that reference price, what is the value of the reference price?

Tom O'Leary: Okay. I'll hand over to Christian in a moment, but on the first question on property starts, certainly when property completions rise there's inevitably a pull on products that we sell. Why property completions are lower than starts is a pretty complex one and a difficult one to evaluate. Christian can elaborate on that.

In terms of the reference price, if you look at the slides we've shown over the last few years, Paul, you can see that the weighted average realised price for zircon premium and standard has varied above - well, not above but it has - the discount from the reference price has varied over the years and the gap between weighted average realised and the reference price has narrowed over the most recent period. The reason for that is around rebates and discounts and what we're flagging is that that weighted average realised price is probably going to open up a little.

What's the value of the reference price? It's really a commercial mechanism that we utilise with our customers to pitch pricing and it's been very successful in building in our customers' minds a level of fairness around what they pay for their zircon by reference to what they take and the level of loyalty they show in terms of wallet share and delivering on their annual target commitments. At present, we continue to think it's a useful mechanism but at the moment we are foreshadowing a little bit of an opening up of that gap. Christian, any further comments on the housing market?

Christian Barbier: Yes, maybe. Paul, this is Christian Barbier. You had something on the housing starts. Well, first on this - much has been written and will always be written in China about the real estate market. Historically, the Chinese governments have used that to stimulate the economic growth, but also to avoid overheating and speculation and lately they have increased the scrutiny on bank loans to ensure that loans feed genuine demand instead of feeding speculation. Now, we've noted indeed for a few quarters the housing starts indicator being higher than the completion indicator. This probably means that further down the track when completions catch up there will be an upside for the consumption of titanium dioxide and zircon products. They are used in the later phases of construction closer to completion.

Now, on the reference price, I would also like to add that it's been over two years that we've decided to switch to six-monthly pricing in order to increase stability in the markets. We're maintaining our reference price for another six-monthly period because there is, as we've noticed, the economic conditions are not conducive to increasing the reference price. We also note that decreasing the price will not stimulate any demand. Overall, our customers have been very supportive of our policy to maintain stability and to give visibility in the long term, and this is why we continue to implement our strategy this way.

Paul McTaggart: (Citigroup, Analyst) Okay. I guess the risk is, Christian, that if starts are up and completions are down, it means there's an inventory build, so the risk would be that before completions actually start up again, you need to run down inventory. So, if you were a bear you could look at that and say this could be an extended period of weaker pricing.

Christian Barbier: Yes, Paul. This is a good question. I think this is what has been happening over the last - probably over the last year. It's not happening just now. We've noticed also, probably over the last couple of years, that there is an inventory of finished apartments in China and that stock needs to be resolved. Little by little, the Chinese Government has chosen to have a soft-landing policy and this is what we believe is unfolding.

Paul McTaggart: (Citigroup, Analyst) Okay. Thank you.
Operator: Thank you for the questions. Our next question comes from the line of Hayden Bairstow from Macquarie. Please go ahead.

Hayden Bairstow: (Macquarie, Analyst) Thanks, Tom. Just a couple from me, just on production, I guess. You're obviously giving good guidance on the volume numbers for the year but is there much you can do in pulling back production? You're obviously not guiding to how much inventory you're going to build but is there things at JA or some flex that you can pull volume back on the production side to help on the costs side? And just where do we sit now with the potential SR1 restart; is that on the backburner, because the rutile market certainly looks a little bit better than zircon, for sure.

Tom O'Leary: On production, Hayden - clearly, there are things we can do. We always structure our affairs so that we can wind back production, but I don't think - I wouldn't expect that winding back production is going to have a positive impact on our cost position, positive as in lower. We typically operate at high rates of production to ensure lowest cost. As the next period unfolds, we'll certainly be alive to those possibilities, as you would expect. In terms of SR1, yes, SR1 obviously is for synthetic rutile, it's not for zircon, so as you point out, I think the conditions are pretty strong in that area and we continue to evaluate options around feedstock, our own or others. That's certainly something we continue to look at pretty carefully.

Hayden Bairstow: (Macquarie, Analyst) Okay, great. Thanks for that.

Operator: Thank you for the questions. Once again, if you would like to ask questions, you may press star-1 and wait for your name to be announced.

Our next question comes from the line of Peter O'Connor from [AW]. Please go ahead.

Peter O'Connor: (AW, Analyst) Good morning, Tom, Adele and Christian. Tom, just a thought and an observation on the dividends comments you've made and relating that back to the Mining Area C commentary. I note you've been very deliberate and very careful with your wording about dividends and Mining Area C twice in this presentation. I've also noted there's been more PowerPoint slides dedicated to Mining Area C than I think I've ever seen and the word count on Mining Area C is more than I've ever seen. Part of my job and part of our job is to look between the lines and join the dots. You're telling me something about Mining Area C and dividends, which you spelled out as Iluka's ability to pay dividends in coming years will be enhanced. Is part of that enhancement a change to the way that flows? Would you consider different mechanisms for dividend payments as Mining Area C grows going forward and are there any other messages that I need to read between the lines or join the dots later?

Tom O'Leary: Well, they're very interesting observations. Thank you for those. I guess one is that many have said from time to time that the Mining Area C asset is not fully recognised in Iluka's portfolio and so on. So, over the last while we've sought to ensure that our shareholders and market participants do understand the value and so at the conference earlier in the year we put up a slide that's very similar to the one in the presentations. I've also noted there's been more PowerPoint slides dedicated to Mining Area C than I think I've ever seen and the word count on Mining Area C is more than I've ever seen. Part of my job and part of our job is to look between the lines and join the dots. You're telling me something about Mining Area C and dividends, which you spelled out as Iluka's ability to pay dividends in coming years will be enhanced. Is part of that enhancement a change to the way that flows? Would you consider different mechanisms for dividend payments as Mining Area C grows going forward and are there any other messages that I need to read between the lines or join the dots later?

In terms of the second question around different mechanisms, we have been very deliberate around our words and the Board continues to consider ways in which the value of that royalty is optimised, with a view to always ensuring that we maximise returns to our shareholders from all of our assets.

Peter O'Connor: (AW, Analyst) Okay. Thanks, John.

Tom O'Leary: A pleasure.

Operator: Thank you for the questions. Our next question comes from the line of Glyn Lawcock from UBS. Please go ahead.

Glyn Lawcock: (UBS, Analyst) Good morning, Tom.
Tom O'Leary: Morning, Glyn.

Glyn Lawcock: (UBS, Analyst) Apologies, a little bit late to the call. I just wanted to try and understand the zircon pricing a little bit better. Is it just the mix that's changing at your MSP or is it also there is price on the underlying individual products like premium, standard and ZIC? I'm trying to understand where the pressure is. Is it just the mix pressure or is there also pressure on the individual product pricing? Thanks.

Tom O'Leary: Sorry, Glyn, I did touch on this a little bit earlier. I pointed to the fact that over recent years we've put out a slide - I'm sure you recall it - where we've got the reference price and a line showing the realised, the weighted average realised price net of rebates and discounts and so on. What we've pointed to is that as a consequence of where we're at with the market, with the level of rebates and product mix, we expect that the weighted average realised price is going to be lower in the second half. You'll recall in the first half it was in the order of US$1522, so we're expecting it to be lower in the second half for all of those reasons.

Glyn Lawcock: (UBS, Analyst) I understand that. I guess I'm - I think Christian said earlier, I think it was just two questions ago, about dropping the reference price won't stimulate demand, not conducive to increasing demand. I was trying to say - so you actually are having to put this downward pressure on the standard zircon price is what I guess I'm trying to make sure I'm clear on. Sorry.

Tom O'Leary: I think it's a good observation to pick up that the view, our view that dropping the reference price would not stimulate demand. We observed at the quarterly that there is a modest surplus of standard zircon as a consequence of concentrates coming into China and as a consequence of a bit of a downshift in demand. So, there is a modest surplus of standard zircon in the market and the way to deal with that, we've talked about withdrawing some product from the market and taking some inventory forward, and that's what we're doing.

Glyn Lawcock: (UBS, Analyst) Sorry, just a final question on a similar vein. Is it only China where you're seeing the demand weakness or is it more broader as well?

Tom O'Leary: Oh no, it's broader.

Glyn Lawcock: (UBS, Analyst) Okay. Thanks.

Operator: Thank you for the questions. Our last question comes from the line of Matthew Hodge from Morningstar. Please go ahead.

Matthew Hodge: (Morningstar, Analyst) Hi. Thanks for taking my question. Not to harp on about the zircon market softness, but I'm just curious about how you see the split between supply and demand. Has there been unforeseen supply that has come to the market that you weren't expecting or is it just a cyclical weakness in demand? Looking forward, I share your view on the longer-term outlook, so what are the key events that you're looking towards for you to get confident that the market is turning and things are improving?

Tom O'Leary: I think if you go back over, we did talk a bit at the quarterly about further concentrates being mobilised into the market. It's difficult to tell in year exactly how much is around but it's evident that there is more around. In terms of demand, again, that additional concentrate and standard product has come at a time when demand has flowed both in China and elsewhere. In terms of what we need to see, I think we'll be observing pretty closely both of those things, frankly: how much concentrate comes into the market, and what happens in terms of global demand drivers across the world, when we see some uptick in activity levels - and over time inevitably those sources of product will diminish.

Matthew Hodge: (Morningstar, Analyst) Okay. Thanks.

Tom O'Leary: No trouble.

Operator: Thank you for the questions. We have no more questions from the phone line. I would like to hand the call back to the management for closing.
Tom O'Leary: Sure. Thank you. In summary, there is some uncertainty ahead, which we've acknowledged in relation to the global environment, but we do believe that we are positioning ourselves in the best possible way to navigate through that and we have confidence in the longer-term fundamentals for the industry. Thank you very much.

Operator: Ladies and gentlemen, that does conclude the conference for today. Thank you for your participation. You may now disconnect the lines.

End of Transcript