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JSC NAC Kazatomprom H1 2019 Results Investors Call Conference Call Transcript

Moderator

Welcome to the Kazatomprom 2019 half-year results conference call. All participants are in listen-only mode and this call is being recorded. The call will begin with a presentation, which will be followed by an opportunity to ask questions. To join the question queue, please press star 2 on your telephone keypad.

I would now like to turn the conference over to Cory Kos, Head of Investor Relations, please go ahead, Mr Kos.

Cory Kos (Head of Investor Relations)

Thank you operator and good day everyone, thank you for joining us. Welcome to Kazatomprom's conference call to discuss our 2019 half year operating and financial results. The press release, full version of the operating and financial review along with our viewed 2019 half your financial statements are available on Kaatomprom's website.

Participating in today's call and available to answer your questions, we have Galymzhan Pirmatov, Chairman and Chief Executive Officer, Meirzhan Yussupov Chief Financial Officer and Riaz Rizvi, Chief Strategy and Marketing Officer.

If you joined us through Kazatomprom's website, please note that there will be slides displayed during the remarks, these slides are also available for download in English and in Russian as PDFs called the First Half 2019 Conference Call Slides on our website.

This call is open to all shareholders and stakeholders with the question and answer portion being an opportunity for the investment community to ask their questions. Note that the interactive question and answer portion of this call is on the

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English line only. Those on the Russian speaking line are listen only with simultaneous translation of the English Q&A.

Please note that this conference call may include forward-looking statements. These statements include all matters that are not historical facts. By their nature forward looking statements involve risk and uncertainty, and they are not guarantees of future performance. The company does not make any representation, warranty or prediction that the results anticipated by such forward looking statements will be achieved.

I will now turn it over to Galymzhan.

**Galymzhan
Pirmatov (Chief
Executive
Officer)**

Thank you Cory and hello everyone. Thank you for joining us today to discuss Kazatomprom 2019 half year operating and financial results. This conference call is our second as a publicly traded company and we expect to continue with bi-annual calls going forward.

Before talking specifically about the company's results, I would like to first discuss the Uranium market context that we are currently operating in. Uncertainty dominated the first half of 2019 with the Section 232 investigation in the United States continuing to weigh heavily on market activity. As a result, recovery remains slow with lower contract volume in the spot market and the weekly spot price averaging between USD26 and USD27 per pound, which was an improvement over the USD22 per pound we saw in the first half of 2018, but still far from being a sustainable price.

In the long-term market, contracted volumes increased to nearly 40 million pounds through the first half of '19 compared to about 14 million pounds at this time in 2018. Although volume increased, there was a general lack of long term contracting,

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resulting in the continued stagnation of the long-term price at USD32 per pound.

In July, subsequent to the end of the second quarter the White House announced the US president's decision to take no trade action in the uranium market under Section 232. Additionally, the President established the United States Nuclear Fuel Working Group to look beyond primary domestic supply, and undertake a full analysis of the national security considerations of the entire US Nuclear Fuel supply chain. The Working Group has a mandate to report its findings and make recommendations to the president within 90 days.

While some uncertainty remains as to the potential recommendations of that Working Group, the overarching decision not to intervene in the US market was viewed as the best possible outcome by majority of industry players. Kazatomprom certainly welcomed this decision and reiterated its long-held belief that intervention in any form is undesirable. As expected, both buyers and sellers are now slowly reassessing the market post 232, though this has not yet translated into any notable increase in contracting.

Kazatomprom continued to work with utilities despite the uncertainty, committing only to contracts that align with our value strategy. Representing over 20 percent of primary supply into the global Uranium market, we have been following a disciplined approach as a responsible pure play market participant. While current spot and term prices reflect a market, which is not yet in significant deficit, we remain committed to our strategy of value over volume. This was reflected in our announcement last week to extend the 20 percent production reductions into 2021. We are not yet seeing market signals to tell us it is time to return to full licensed production level. The

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timing of our decision is driven by the near, medium- and long-term production planning and budgeting cycles which are well underway, as are the negotiations with our JV partners.

The extension to 2021 follows our announced production cut in 2017 and again from 2018 to 2020. Taken altogether this decision took roughly 35 million pounds of uranium out of the market from 2017 through 2019, most of which was in '18 and '19, with another 28 million pounds expected to come off the supply curve in 2020 through 2021.

In terms of total primary supply, the quantity of pounds we have removed and expect to remove from the supply stack is now nearly equivalent to having stopped production in Kazakhstan for a year. While our production and financial metrics drive the business itself, it's impossible to maximize value without continually monitoring our operations and activities from a sustainable development perspective. We continue to focus on health, safety and environment as our top priority for Kazatomprom. There were no significant incidents during the first six months of 2019 with two minor registered accidents.

Turning to Kazatomprom's highlights through the first half of the year, despite the uncertainty, our results remain strong and in line with our expectations. We continue to focus our attention on preserving financial capacity in constantly changing market environment. In June, Kazatomprom paid out the first dividend to its shareholders, marking an important post IPO milestone by delivering on our commitment to pay out a minimum of USD200 million to shareholders for 2018. And we're confirming our commitment to keep this minimum dividend pay-out level in 2020.

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Looking at the first half of the year in more detail, my introduction was in line with our plan, being roughly at the same level as in the first half of 2018, and with 2019 production still expected to be 20 percent lower than our subsoil use license volume. It's worth mentioning that we've added asset level production on a 100 percent basis to our disclosure, with the extra bit of information expected to help the investment community better understand our operation and it demonstrates our commitment to clear and transparent reporting.

For the first half of the year attributable cash cost and all-in sustaining cash cost in US dollar equivalent decreased by 19 percent and 18 percent respectively compared to the same period last year. The decreases were primarily due to the weakening of the Tenge, the change in the Group structure and cost optimization effort to further position the Group's unit production cost as the lowest in the industry.

Sales volumes have not changed significantly compared to the same period of 2018, though we enjoyed positive effect on our revenue due to a higher average sales prices resulting from a corresponding increase in spot price in 2019. As was highlighted during the previous conference call in March, changes in the group's structure significantly affected Kazatomprom's financial results. In 2018, we saw a change in accounting treatment for JV Inkai, JV Akbastau and Karatau. And now, with the continuation of that restructuring into 2019, the changes in accounting for Baiken-U and Khorasan-U took effect. So it must be noted that although performance in the first half of 2019 was strong year-over-year, those accounting treatment changes had a further positive impact on our financial metrics.

Consolidated revenue for the first half of 2019 was up 22 percent over the same period of 2018 to nearly KZT177 billion, mainly

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due to the increase in average sales price related to both spot price improvement and to depreciation of the Tenge against the US dollar. The Uranium segment continued to make up the majority of our revenue at about 82 percent. Operating profit for the first half of 2019 was up nearly 70 percent over last year to about KZT27 billion, again primarily due to a combination of spot price and foreign exchange rate, but also related to the changes in the Group structure.

Adjusting for one-time effects of certain transactions in both years, adjusted net profit was about KZT32 billion, increasing 2.5 times from the first half of 2018, due to previously explained factors that affected the operating profit.

Adjusted EBITDA increased 88 percent to KZT73 billion, adjusted attributable EBITDA up 28 percent to KZT73 billion, and operating cash flow reached KZT73 billion, a significant rise from a negative cash flow of KZT45 billion reported in the first half of 2018, all driven by increased operating profit, but also greatly influenced by the changes in the Group structure.

Capital expenditures at the mining unit decreased 15 percent compared to six months of 2018, mainly due to changes in the timing of spending for projects related to future expansion at some of the mining assets and constant cost optimization efforts. Looking ahead, the most important point to reiterate is our commitment to maintain a production level 20 percent below our subsoil use license levels for 2019 and 2020. And the decision to extend that reduction through 2021.

Guidance for C1, and all-in sustaining cash cost on attributable basis remains unchanged. Although through the first half of the year, the Kazakhstan Tenge has been weaker against the US dollar compared to the 2019 budget assumption. As a result,

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both C1 and all-in sustaining cash costs have trended to the bottom of the expected ranges of USD11 and USD15 respectively.

In terms of capital spending, the guidance for 2019 has been decreased by about 5 percent to a range of ZT80 billion to KZT90 billion, related to changes in the timing of spending at some of the mining assets. Guidance for other metrics have remained unchanged. As we move into the second half of the year, with the possibility of disruptive trade actions in the nuclear fuel cycle being less of a threat, the market has been generally more positive with an increase in productive customer discussions.

However, both suppliers and customers remain cautious and today, supply and demand remain roughly balanced. We are confident in the prospects for our industry, and as the uranium market strengthens, we believe that Kazatomprom, with our low-cost assets, the ability to quickly flex production up or down and the commitment to value driven strategy remains uniquely positioned to realize significant benefits and deliver strong returns as the market recovers.

So with that, we're happy to take your questions.

Q&A Session

Moderator

We will now begin the question and answer session. To maximise participation, we ask that you limit yourself to two questions at a time. If you have additional questions, you are welcome to re-join the queue.

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To join the question queue, you may press star 2 on your telephone keypad. If you are using a speakerphone, please pick up your handset before pressing any keys.

Once again, investors on the call who wish to ask a question please press star 2 at this time.

We will pause for a moment as callers join the queue and to allow for simultaneous Russian translation.

Our first question comes from Alexander Pearce. Alexander please be aware that your question is being translated into Russian so bear this in mind with your pace. Please go ahead with your question.

**Alexander
Pearce**

Great. Thank you all. So the first question I have is actually, just based on the new guidance you've given us in terms of 2021 production. Is there any way you can give us an indication of what CapEx levels would be relative to this year? If I know you're kind of still in discussions with other partners, but just to get a better indication on CapEx levels over the next couple of years.

And then the second question I have is, can you give us any kind of better granularity on sales timing over the next couple of quarters just to meet your sales guidance for 2019? Obviously. Q1 was fairly low with the seasonality, for example, will there be more sales in the final quarter relative to the third quarter? And is this something which will happen every year? Thank you.

**Galymzhan
Pirmatov**

Thank you Alexander. Thank you for joining us so early. You're in Canada?

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Alexander Pearce

No London based, this is midday for me.

Galymzhan Pirmatov

Good. About CapEx, assuming all our partners agreed to our decision to cut 2021 production 20 percent compared to license volume, we expect the CapEx should be about the same as this year. That's a pretty good guidance. In terms of sales, I'd ask Riaz to give you an answer on that question.

Riaz Rizvi (Chief Strategy and Marketing Officer)

Sure. I think you'll see sales first half of 2019 and first half of 2018 are pretty much on top of each other. There's very little difference. And you're right the second half of the year, typically is stronger. For one thing there are more physical shipments taking place in the second half of the year. And part of that is at the beginning of the year there is a process of obtaining export licenses and also weather conditions which slow down the volumes that get shipped out physically in the first quarter. In terms of that seasonality going forward, you should expect some seasonality going forward. Second half of the year is usually stronger, and certainly I wouldn't use the first half of the year as any kind of guidance for how we should be performing over the entire year. We feel very comfortable about meeting the guidance that we've provided for 2019.

Alexander Pearce

So just to follow up so Q3 and Q4 would you expect them to be kind of roughly balanced in terms of the remaining sales or, would Q3 or Q4 be one or the other?

Riaz Rizvi

You know, that very much depends because there are certain customers who take a very large single shipment. We've seen historically that shipments have slipped from Q3 into Q4 for example or Q2 into Q3, as we saw this year. So I can't really answer that with any degree of accuracy, but there is no structural reason why Q3 or Q4 would be higher or lower than the other.

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Alexander Pearce Okay. Thank you very much.

Moderator Thank you very much. There will be a brief pause while we allow for the Russian translation to catch up with us. We thank you very much for your patience.

Thank you. Our next question comes from Ildar Davletshin. Please go ahead with your question.

Ildar Davletshin Good afternoon. Thank you very much for the opportunity to ask the question, and congratulations with quite strong results. I have two questions.

So one, on this market overall for uranium, I think for those who follow the markets, it's quite obvious that the price, the spot price, is way too low and not really sustainable yet the recovery's still not happening. So would appreciate if you could maybe share a bit more - some thoughts on the market. And you did refer to uncertainty, but now with some news on petition 232 the positive outcome happening, it looks like there is less uncertainty.

So are there any particular events or projects on the demand side, on the supply side perhaps, that could move the market into a more balanced position in the next, I don't know, 18 - 24 months? That's my first question.

And then if I may ask the second straight after - so on cost optimization, you did mention that part of your cost reduction is due to these efforts. Could you maybe spend a bit more time explaining what sort of cost optimization efforts you've

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undertaken, and if you see scope for future cost reduction in the future? Thank you.

Galymzhan Pirmatov

Thank you Ildar, for the first question I'll ask Riaz to respond and I'll take the second one.

Riaz Rizvi

Yes. I think looking at the market overall, we are certainly seeing a recovery. If you compare average uranium prices at the end of 2016 or through 2017 compared to 2018 and 2019, we're definitely seeing a positive trend overall. Having said that, we've consistently stated that the spot price is very much a function of what's happening in the short-term markets - and it's not just for uranium but pretty much across all commodities, short-term supply and demand can dictate that prices can, in the short-term, remain below what we would term a long-term sustainable price.

Some people refer to this as market failure because what it can create is a fair bit of volatility in the market. Prices are low because there's a little bit too much supply in the short term. Once that supply demand balance flips, then suddenly prices run up very dramatically and we've seen that pretty much across all the commodity spectrum.

I wouldn't say that the market's in structural deficit yet. But certainly, the steps that Kazatomprom have taken and that others have taken have had some impact on bringing the market back into balance. We saw prices at around USD29 at the back end of last year. And when Galymzhan mentioned uncertainty, certainly we saw a lot less activity in the market, a lot less

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interest by utilities in particular in the first half of the year and that really relates, I would say, to spot activity.

So to summarize, I think we are looking at certain projects very closely. We're looking at the situation in Japan with the recovery there. We're looking at the changes in policy in France and we're also seeing the actions that some of the producers have taken, such as Cameco with its reduction, but also who's still planning to ramp up. And obviously all of those can have an impact on the market over the next couple of years.

So I would say, a couple of difficult years ahead. But the really important thing to underline is that even though supply and demand are balanced, when you look at the marginal cost of production at which they are balancing, it's way above the current spot price. And that analysis, pretty much all the large uranium commentators agree on, which means that yes, as you said, it's not sustainable in the long term. And we would need to see a much higher price to incentivize any new production to come online. And when you think of the lead times in uranium, many would argue that that's something that needs to happen very, very soon in order to meet potential real supply demand imbalances in the middle of the next decade. Thanks for your question.

**Galymzhan
Pirmatov**

And Ildar, on your second question, we continuously focus on our operations from the point of optimizing on a cost side, because that's what we have control over, while maybe markets and prices are not exactly easy to influence.

So specifically certain things that brought results are around streamlining our operations. One example is the optimization of use of electricity at our operations, which is both from optimizing the type of equipment, type of pumps we use and making sure

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that we're not really wasting the idle equipment or use of electricity. So that's been one of the part.

The other one we're constantly focused on use of reagents. Using reagents is one of the biggest cost items in our operations and one example is we basically, based on our R&D work and results of those considerations, we're switching from using more expensive reagents to cheaper reagents, while not really jeopardizing our operations and extraction and efficiency of our operations.

So those are the ones that we constantly focus on a procurement, streamlining our operations, but use of equipment, trying to make sure that we use equipment that's best from use of energy and output. And also, we constantly look at reagents, where we can switch from more expensive reagents to a cheaper one, readily available that can deliver the same results as before. So those will be examples that that comes to mind.

Ildar Davletshin Thank you very much.

Moderator Thank you very much Ildar from Wood and Company for your question. We are just waiting for the Russian translation to complete in the other call.

Again if you would like to ask a question please press star two on your telephone keypad now.

Again if you would like to ask a question please press star two on your telephone keypad now.

We currently have no further questions. I will hand back over to the team at Kazatomprom to finish today's call.

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**Galymzhan
Pirmatov**

Thank you operator. The team here, we're committed to continuing to deliver on our commitments and continue to create value for all our stakeholders. Thank you for joining us today and have a great day.