

CHIEF EXECUTIVE'S REVIEW



CON FAUCCONNIER – CHIEF EXECUTIVE

It's not often that a four-year-old company performs its swansong while its share price is still flying, but then Kumba Resources is not your average four-year-old company. As the financial year drew to a close, Kumba was one of the five best-performing companies in South Africa on share price appreciation of 132% for the year, having already taken the accolade as *best mining company to work for* – for the third year running.

OVERVIEW

Kumba has proved its ability to deliver shareholder value in widely varying market conditions. Operational excellence has become a hallmark of our group and was again demonstrated during the review period, with several divisions exceeding records set in the previous year and others setting new benchmarks for performance.

Across the group, our ongoing focus on the business improvement programme initiated two years ago paid off in better efficiencies, processes and productivity. Kumba's people rose to this challenge with characteristic spirit, enthusiasm and innovation – another hallmark of our group.

The strong market demand that fuelled increased commodity prices across all business segments, together with the realisation of the revenue-enhancement and cost-saving benefits of our business improvement programme, more than offset a persistently stronger currency.

Against this background, and proving that our business can counter currency fluctuations, Kumba's financial performance was excellent, with revenue increasing by 37% to R11 962 million and net profit from operations by 171% to R4 887 million on the previous year. Our financial results are set out in the financial review on p23.

TRANSFORMATION

However, the biggest headlines of the year for Kumba were devoted to the decision to split the company into a focused iron ore company – Kumba Iron Ore – and a

diversified commodity mining company – still called Newco at the time of writing. The genesis of this lies in our 2001 prelisting statement where we said, *"Kumba Resources views black economic empowerment as a fundamental prerequisite for the long-term development and stability of the South African economy. Therefore, a distinguishing feature of its strategy is to commit the company to meaningful and sustainable black economic empowerment initiatives in all facets of its business. Progressive empowerment policies, the setting of aggressive employment equity targets and black economic empowerment are integral components of the company's value system and code of conduct."*

Between 2001 and 2005, Kumba has grown from the fledgling R8,5 billion Iscor mining offshoot to a strong, independently-managed and diversified group valued at R30 billion and active in eight countries on three continents.

For the past 18 months, many parties have worked to construct an empowerment transaction that best serves Kumba's strategy, includes stakeholders at all levels, contributes to national growth and transformation and meets legislative requirements. Subject to shareholder approval in mid-2006, we will have created the country's flagship empowerment mining company and its largest black-owned, controlled and managed business, detailed on p16. We will also have materially exceeded the mining charter's empowerment ownership requirements. More importantly, for us, the transaction

embodies the spirit – the very essence – of sustainable transformation.

It was this spirit that characterised much of the negotiations surrounding our empowerment transaction – a transaction described by one of the merchant bankers involved as the most complex in his 22 years of experience. Yes, we were fulfilling a legal requirement to qualify for new-order mining rights and, yes, we had to address governance issues in our shareholding structure. But we were also realising a dream that was older than Kumba – the dream of creating a truly South African, large-scale empowerment mining company, the dream of the synergies that could be derived and the benefit to the country of such a deal. At that stage, in the closing years of the 20th century, much of our idea seemed "pie in the sky" but the seeds were planted back then and the fruits are becoming reality today – a reality crafted by the willing co-operation of teams from Anglo American plc, the IDC, government and our empowerment partners.

As we move into 2006, many formalities are being completed and approvals granted, but an active working relationship is being built with the key participants in the transaction, particularly Siphon Nkosi and his team from Eyesizwe Mining, and we will keep shareholders updated on our progress in finalising South Africa's flagship empowerment mining company.

HIGHLIGHTS

Apart from our empowerment transaction, the review period contained many other notable highlights, some internal and others external but all important to our business:

- Kumba has submitted its applications for the conversion of old-order to new-order mining rights. With the appropriate ownership structure soon to be in place, applications should be ratified once our empowerment transaction is finalised.
- Good progress by state transport utility, Transnet, in expanding its product range and improving service levels. We welcome the appointment of our former Iscor colleague, Louis van Niekerk, to the Transnet executive which is fast becoming a formidable team focused on turning this critical component of the economy into a productive national asset under the capable leadership of Maria Ramos.
- The appointment of Lindiwe Hendricks as Minister of Minerals and Energy, who has rapidly demonstrated her confidence in the contribution the mining industry can make to the economy.
- The consolidation of our heavy minerals interests by completing our acquisition of the Ticor Limited minority shareholdings, which I deal with further on p14.
- The Phase V expansion of the Richards Bay Coal Terminal received its long-awaited approval during the year. Kumba Coal is a shareholder in this expansion with a 2Mtpa export entitlement. In addition, expansion at Richards Bay also enables Kumba and Eyesizwe Coal to proceed with their joint venture Inyanda coal mine, a new 1Mtpa export thermal coal mine near Witbank.
- ISO 14001 and OHSAS 18001 certifications – our aim was to have all operations certified by the end of 2005. This goal has been achieved. By world standards, this was a commendable achievement in less than two years. At operational level, it is even more noteworthy – achieving

and maintaining world-class standards to support our goal of being a global mining group.

- Safety – While intensely disappointed that we did not achieve our goal of zero fatalities or meet our target for the lost-time injury frequency rate (see p74), several individual operations achieved excellent results as highlighted by the chairman.
- Training and development – Kumba spent almost 6% of total payroll on training and development during the year, well above the stipulated level of 1%. To quantify that, Kumba trained almost 28% of all engineering learners in the mining industry which, in turn, trains almost half the engineering learners in the country. Given that in the past 30 years, South Africa's annual intake of apprentices has plummeted from 30 000 to 3 000, this is an issue we must address urgently and with sufficient resources to prevent it becoming a national crisis. Kumba willingly played its part in developing a national pool of skills, and will continue to do so in its new form as Kumba Iron Ore and Newco.
- Sustainable development – While the independent assessment of our commitment to sustainable development in a multi-stakeholder model that placed us among the top five in the country is gratifying (p11), we acknowledge that this is a journey – one that unfolds wherever we operate and that the balance between financial performance and a demonstrable commitment to the societies and environments we touch is pivotal to our future.

SUSTAINABLE DEVELOPMENT

Sustainable development is our lifeblood – the interaction with stakeholders and their input underpins our ability to run our operations efficiently, safely and productively. Kumba therefore reports on the triple bottom line to stakeholders, integrating financial and non-financial issues. Sustainable development is far more than a business imperative, it is an integral part of our foundation values and the way we do business. It is evident in all

our practices and in our passion to improve the quality of life in the communities that enable us to trade.

Kumba's integrated sustainable development annual report is based on the internationally-recognised Global Reporting Initiative (GRI) guidelines. Additional GRI recommendations for the mining sector were published early in 2005 and incorporated into our sustainable development reporting as we incrementally progress towards being "in accordance with" GRI guidelines.

This report is aligned with the 2002 GRI Guidelines and represents a balanced and reasonable presentation of our organisation's economic, environment and social performance. Our report is independently assured, reflecting considerable progress since we began this reporting journey in 2003. The scope of the independent review of our sustainable development reporting has again been broadened (p104), and we have included earlier assurance report findings and stakeholder feedback in our processes.

During the review period, Kumba continued to make progress in many areas of reporting on sustainable development, specifically in training and development, job creation, HIV/Aids awareness projects and environmental management.

Our commitment to meeting and exceeding our targets – legislated or self-imposed – is firm. The establishment of a dedicated sustainable development division at corporate level, headed by an experienced senior manager who is accountable for setting and achieving stated objectives, is testimony to that commitment. The lessons learned and good practices developed will guide us as we unbundle the group into its new format, ensuring that we continue to report measurable results and meaningful information to stakeholders for an informed understanding of our impact on the economy, society and environment in which we operate. As our international

Empowerment targets exceeded and sizeable expansion under way

operations develop, our economic, social and environmental reporting will be consistent across three continents, whether legislated or not, and aligned to GRI guidelines.

As an integral part of our business strategy, Kumba has an approved group-wide strategic sustainable development framework. The responsibility for reporting to the board on sustainable development issues rests with me and is an integral part of the report I prepare for each board meeting. This monitors our progress towards targets in eight focus areas:

- Financial
- Governance, ownership and control
- Resource utilisation
- Workplace
- Environment
- Community and external stakeholders
- Suppliers
- Customers.

At each operation, sustainable development issues are integrated into the business plan against which performance is measured, and will be an intrinsic part of the due diligence investigations now under way to finalise our empowerment transaction.

STRATEGY

As South Africa's mining industry continues to transform itself to meet the challenges of best practices in a global marketplace, Kumba's clearly-defined strategy is now unfolding. We have previously stated that to grow and prosper, we will:

- Build a balanced portfolio of globally-competitive commodity businesses
- Attract and retain a highly-skilled and motivated workforce
- Promote innovation and employ appropriate technology
- Nurture a culture of continuous improvement and operational excellence
- Reward our shareholders with superior returns and capital growth
- Integrate sustainability into all operations.

Through our empowerment transaction and other corporate activity, we will

continue to capitalise on the growth of the iron ore market, and significantly expand our coal and heavy minerals interests.

In its unbundled form, Kumba enters a new era as a forerunner in the national strategy for empowerment and the premier mining house in South Africa. In Kumba Iron Ore, shareholders have the opportunity to participate in the JSE's first pure iron ore stock and its solid growth potential. In Newco, shareholders have exposure to a diversified, balanced portfolio of growth commodities, exciting technology and a growth pipeline whose potential is beginning to unfold. In both companies, shareholders can expect a continuation of our strategic imperative of superior returns and capital growth, underpinned by the focus on sustainable development that considers the rights of all stakeholders.

INTERNATIONAL

Hope Downs

On 1 July 2005, and after exhausting all legal avenues to preserve its rights, Kumba received a A\$231,4 million (R1,2 billion) pre-tax settlement from Hancock Prospecting for its interest in the Australian Hope Downs project. While we were disappointed that we would no longer be a partner in this excellent project, shareholders' interests were very well served with a more than fourfold return on the initial investment. We wish Hancock Prospecting and its new partner, Rio Tinto, every success in this promising venture.

Ticor Limited

During the year, Kumba made excellent progress in its longer-term strategy to enhance its position in the heavy minerals market by buying out the minorities in the Australian listed group, Ticor Limited. To contextualise this, Kumba first invested in Ticor in 1995 with an initial interest of 35% to begin to understand the market and to gain access to some heavy minerals technology that was relevant to the resources we owned in KwaZulu-Natal. Over the years, we have been supportive of Ticor Limited and played a material role in refocusing the company as a vertically-integrated titanium dioxide feedstock and pigment producer. In turn, Ticor Limited has been an important partner in establishing the Ticor SA venture in Empangeni.

Our objectives in buying out Ticor minorities were to simplify Kumba's group structure and create a significantly larger heavy minerals business with greater geographic and product diversification. Regulatory approval for the scheme of arrangement was received on 1 November 2005 for Kumba to buy out minority shareholders for A\$226 million (R1 174 million) to take its holding from 51,54% to 100%. This has consolidated and streamlined our heavy minerals holdings and given us direct ownership in a sector we believe is a key component of Kumba's asset portfolio.

We believe this transaction provided an attractive and opportune exit strategy for Ticor Limited's minority shareholders, who



A twilight view of the South concentrator at Ticor Limited in Western Australia. Kumba's heavy minerals expansion through the Ticor transaction offers the company greater exposure to the pigment and synthetic rutile markets.

were constrained by a lack of liquidity in the shares, and we thank the Ticor board for the constructive manner in which it fulfilled its fiduciary duties since the start of negotiations. We can now look forward to a closer working relationship with the people of Ticor – a continuation of our ten-year association that will provide important continuity as a wholly-owned subsidiary. We also look forward to developing a deeper working relationship with our partners in the Tiwest joint venture, Tronox Inc (the recently-listed chemical division of Kerr McGee Corporation).

For Kumba's shareholders, our heavy minerals expansion through the Ticor transaction offers more exposure to the pigment and synthetic rutile markets and better scale and balance in our overall product mix. Our heavy minerals portfolio is now arguably one of the few global portfolios to span zircon, low-manganese pig iron, rutile, titanium dioxide slag, synthetic rutile and pigment. If the option is exercised on the acquisition of the zircon-rich asset base of Namakwa Sands, this will balance our portfolio even more, entrenching Kumba as one of the three largest heavy minerals producers in the world.

APPRECIATION

Personally, in my capacity as Kumba's chief executive and as the outgoing president of the Chamber of Mines, I thank the former Minister of Minerals and Energy, Phumzile Mlambo-Ngcuka, who played such a constructive role in our industry's ongoing transformation. We wish her well in her important new post as our country's deputy president, firmly believing she is the right person for the time.

My two years as president of the Chamber of Mines during a time of rapid and far-reaching change were made easier by an extremely capable chief executive, Zoli Diliza, and his committed team. I also thank the Kumba board for affording me the incredible opportunity to play a part, albeit small, in the history of the South African mining industry. Under the leadership of my successor as president of

the Chamber of Mines, Lazarus Zim, I am confident that our industry will continue to contribute to the development of our country and South Africa's role in the global marketplace.

In 2005, we bade farewell to our chairman, Dawn Marole, and executive director, Richard Wadley, while this year non-executive director Tom de Beer will retire. They have added considerable value in their respective roles, for which we thank them most sincerely.

In its short history, Kumba has proved that it is an exceptional company, largely because it has exceptional people at every level. From our chairman and board members, to our management teams and all our people, you have crafted the ethos and culture that epitomise our group and have underpinned its success and I thank every one of you. I believe this same spirit, tenacity, experience and enthusiasm will characterise our unbundled group in future.

OUTLOOK

Kumba and its empowerment partners are on track to complete the proposed unbundling towards mid-2006 which will result in two exciting, listed and empowered mining companies. We are confident that Kumba Iron Ore and Newco will benefit from the competent and experienced management and staff who will then be in place and that both companies will be as successful as focused, independent entities as they have been under the Kumba banner.

Kumba is fortunate to have one of the most attractive growth pipelines in the resources sector: expansion projects worth over R4 billion are under way and there are projects worth a similar amount under detailed consideration. In the iron ore portfolio, there is the 10Mtpa Sishen expansion project and the Sishen South project which has the potential of ramping up to 9Mtpa. In the coal portfolio, initiatives include the char project, Grootegeluk and Leeuwpans expansions, and the new Inyanda mine. Our expansion

in the Waterberg coalfield marks the further development of the country's largest remaining coal reserves in a region with much potential for Kumba and its customers such as Eskom. Agreement was reached after the year end to investigate the development of a coal deposit in the Mmamabula central coal resource in Botswana. In heavy minerals, we are finalising approval for a new mine, Fairbreeze in KwaZulu-Natal, and are in the final stages of evaluating a world-class resource, Toliara Sands in Madagascar. We have acquired the minority interests in Ticor Limited, with the opportunity of, in conjunction with our joint venture partner, expanding its synthetic rutile and pigment production with minimal capital outlay. In base metals, agreement has been reached with our partners to more than double the capacity of the Chifeng zinc smelter in China.

The outlook for Kumba's commodities is somewhat mixed, with supply/demand factors implying another year of price increases in iron ore, zinc and zircon. Conversely, the continued shortage of zinc concentrate will maintain pressure on treatment charges, which affects Zincor's results. With the supply surplus in the titanium dioxide feedstock market persisting, no price increases are expected. Greater balance in the coal market should see coal prices declining somewhat from their record levels.

Kumba has broken much ground in its short time as a listed company. It has achieved ambitious targets and earned its place as a reputable business, a rewarding investment and a caring citizen – a past journey we view with pride and a future journey we embrace with excitement.



Dr Con Fauconnier
Chief executive
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