

# Layers of possibilities



**Group results for the  
first half of 2015**

*14 August 2015*

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# H1 2015 Highlights

## Key events

### Sierra Gorda: Commercial production begins

### KGHM Group: Mineral Resources & Reserves report:

- 22.7 mn tonnes Cu P&P reserves
- 44.4 mn tonnes CU M&I resources

### Dividend: 1st instalment paid (PLN 400 mn)

### Group Financing: optimisation completed

**Victoria** – work under way on surface infrastructure, incl. transformer station

**Deep Głogów** - GG-1 shaft sinking reaches 563 m

## Molybdenum plant starts production



## Production highlights

- **Copper** 331 thousand tonnes
- **Metallic silver** 613 tonnes
- **TPM** 78.4 thousand ounces

## KGHM Group financial results

- **Sales revenue :** PLN 10.1 billion
- **EBITDA:** PLN 2.7 billion
- **Net profit :** PLN 1.2 billion

# Sierra Gorda

## Daily processing at over 80% of designed capacity

### Sierra Gorda

Cu Mo Au

- |  |  |
|--|--|
| ▪ <b>Średnia produkcja roczna</b><br>(Faza I & II) | >220 kt Cu<br>25 mn lbs Mo*<br>64 koz Au |
| ▪ <b>Ownership</b>                                 | 55% KGHM<br>45% Sumitomo                 |
| ▪ <b>Mine profile</b>                              | Open-pit                                 |



**Coarse ore stockpile facility**

### Key events update

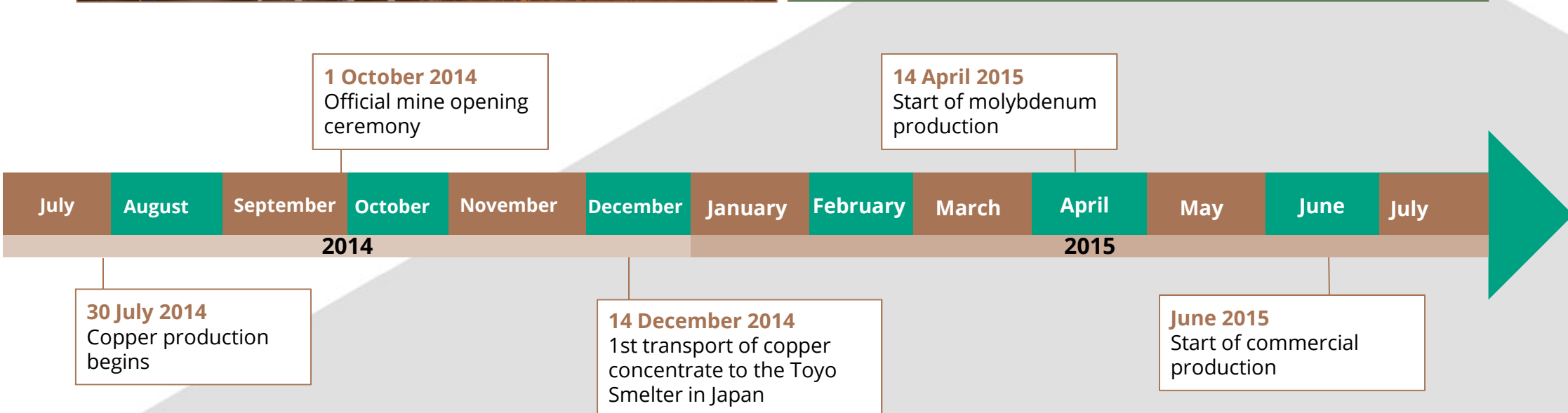
- Average daily ore processing in July at over 80% of designed phase I capacity.
- Production of copper in concentrate by the Sierra Gorda mine in the first half of 2015 around 38 thousand tonnes.
- In mid-April the first molybdenum concentrate was produced.
- During the work to increase processing capacity, in the course of one day over 120 thousand tonnes of ore were processed. Work is under way to stabilise the results achieved.
- In the last weeks of July work commenced on designing phase II of the mine's development.
- Sierra Gorda has transitioned from the ramp-up phase to the operational phase.

# Start of commercial operations by Sierra Gorda



## In June 2015 the Sierra Gorda mine in Chile commenced commercial production

- For over 60 days the copper plant maintained production at 65% of its designed capacity. The molybdenum plant has produced molybdenum concentrate with at least 40% molybdenum content.
- The plant was handed over to the operating personnel.



# Warehouse opened at the Port of Antofagasta

*Port (bird's eye view)*



*Concentrate being unloaded in the warehouse*



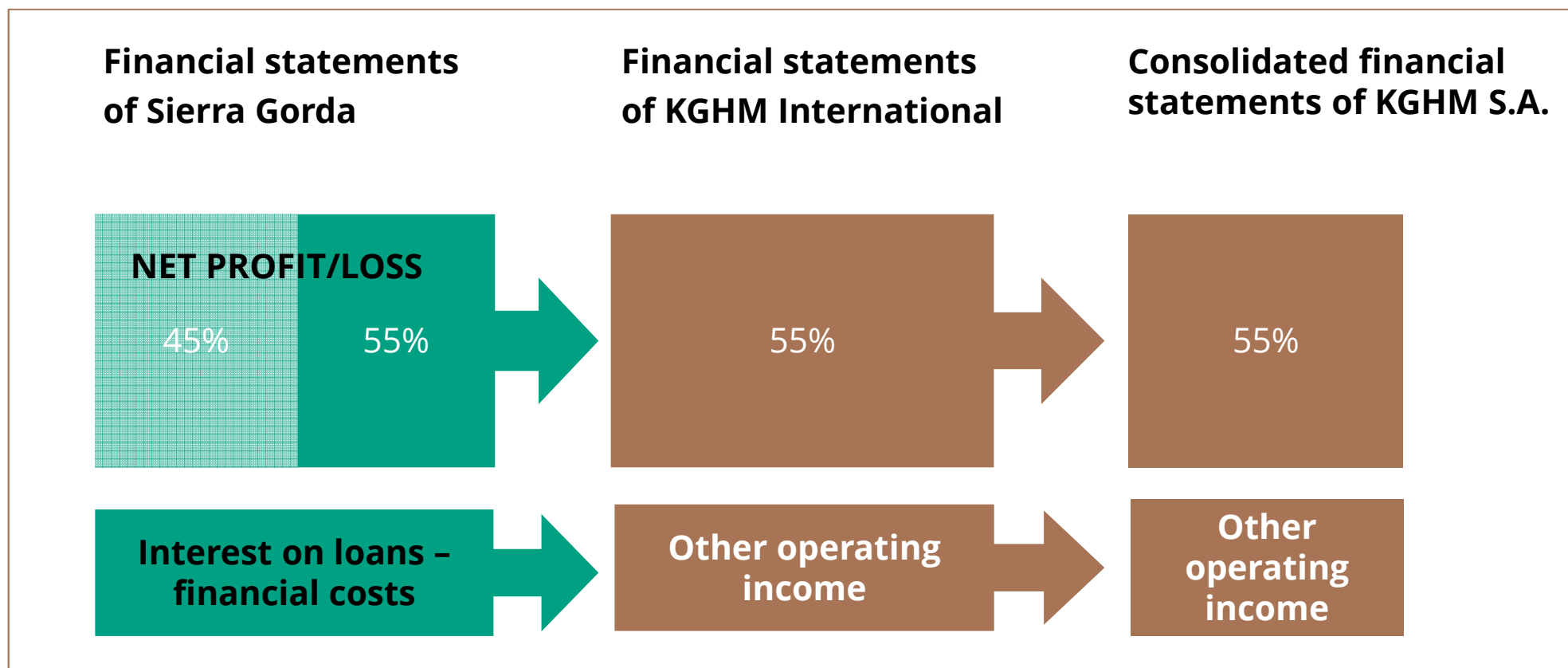
*Concentrate being loaded onto the ship NEW LEADER*

- In March 2015 terms were negotiated with the Port for port services
- On 18 June 2015 Sierra Gorda received official permission to use the dedicated port warehouse at the Port of Antofagasta
- On 22 June 2015 the transport of concentrate from the mine to the port warehouse commenced

- In the first half of 2015, 131 thousand tonnes of dry-weight concentrate were loaded into public warehouses in Antofagasta and Arika. **Utilisation of the new port infrastructure reduces monthly logistical servicing costs by USD 1 million.**

## Sierra Gorda in the financial statements of the KGHM Group










- Sierra Gorda is accounted for using the equity method in the financial statements of KGHM. From the start of commercial production Sierra Gorda will prepare profit or loss statements (from July 2015).



- Interest on owner loans granted (financing of mine construction) decreases the net profit of Sierra Gorda (financial costs) and increases the consolidated profit of KGHM (Other operating income)

## Sierra Gorda in the management reports of KGHM

- Starting from the **third quarter of 2015** KGHM will disclose the following information in its reports:

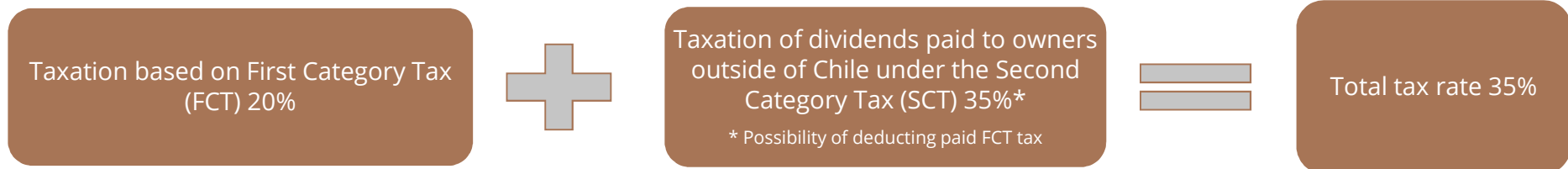
	Execution	Target
Production and sales volumes		
CAPEX		
C1 cash cost		
Basic items in profit or loss		
EBITDA		
Macroeconomic environment		

- The scope of information which will be published by the company regarding our targets will include basic operating parameters, and will be in line with information on the Group's production assets



# Taxation in Sierra Gorda – taxation model following the tax reforms in Chile

Currently



From 1 January 2017

2 taxation models available:



- Target CIT rate of 25% from 2018
- Additional taxation of companies with owners outside of Chile between 35% and 25% (effectively 10%), **paid on an accrual basis** on taxable income earned for a given year (no taxation when profit is paid)



- Target CIT rate of 27% from 2018
- Additional taxation of companies with owners outside of Chile between 35% and 65% of the CIT rate of 27% (effectively 17.45%), **paid when profit is distributed**
- Condition: the foreign shareholder must meet the condition of tax residency in a country with which Chile has an agreement to avoid double taxation

Following economic analysis, **from the point of view of the Group and investors, model no. 2 is preferred.** KGHM is in the process of creating an organisational structure which will allow this option to be chosen. The final decision must be made by the end of 2016.

**During the mine's first stage of operations, Sierra Gorda has the right to accelerated tax amortisation,** i.e. the possibility of shortening the period of amortisation up to one-third of the life of a given asset, and therefore a reduction in the taxable.

# Victoria and Ajax – resource projects at the development phase

## Victoria

Ni Cu Pt Pd Au

## Ajax

Cu Au

▪ <b>Average annual production</b>	~16 kt Ni ~15 kt Cu ~150 koz TPM	~50 kt Cu ~100 koz Au
▪ <b>Ownership</b>	100% KGHM	80% KGHM 20% Abacus
▪ <b>Mine profile</b>	Underground	Open-pit

### Key events update

- Preliminary work continued on gaining access to the deposit, aimed at the preparation of, among others, shaft infrastructure.
- Work continued on developing the project's Integrated Development Study, by a team of Polish and Canadian engineers.
- The team is preparing for work directly related to shaft sinking. In addition, work continues aimed at preparing surface infrastructure.
- The *Basic Engineering Report* is on schedule for completion in the fourth quarter of 2015. Over 50% of the work has been completed.
- The Canadian regulator has approved the AIR document, which had to be accepted prior to submitting an application for environmental permits.
- A further agreement was signed with another First Nation (the *Lower Nicola Indian Band*). KGHM to date has signed a total of 4 agreements with various First Nations, which will be taken into consideration during the process of evaluating the application for environmental permits.



**Foundations of the 230 kV transformer station**



**Cores obtained during drilling**

# Strategic projects in the core business

## Deep Głogów



▪ <b>Resources</b>	290 Mt @ 2.4% Cu, 79 g/t Ag
▪ <b>Ownership</b>	100% KGHM
▪ <b>Mine profile</b>	Underground

## Pyrometallurgy Modernisation Program

Flash furnace construction at the Głogów smelter/refinery

### Expected effects

▪ <b>Higher production</b>	- Silver - Lead - Rhenium
▪ <b>Costs</b>	- Lower unit copper production cost
▪ <b>Environmental protection</b>	- Lower dust and gas emissions by 50%

## Key events update

- Continued sinking of the GG-1 ventilation (inlet) shaft using tubing construction.
- At the end of H1 2015 the shaft had reached a depth of 563 meters (target shaft depth – 1340m).
- Since the start of the project 64 921.4 meters of tunnel have been excavated. In the first half of 2015, 7 574,4 meters of tunnel together with necessary technical infrastructure have been built.
- The first stage of work on the Surface-based Cooling Station was completed comprising 15 MW in June 2015 (target capacity – 25 MW). Completion of construction is planned in H1 2016.

- Construction and assembly work continues on the main elements of the modernised flash furnace production line at the Głogów I smelter/refinery, including :
  - Flash Furnace,
  - Electrical Furnace,
  - Recovery Boiler, and
  - elements of the Charge Preparation Section.
- All technical permits were received. About 98% of the design work on the modernised flash furnace has been completed.
- 98% of contracts signed for construction-assembly work.
- The current state of permitting allows the work to be completed on time.\*
- Start-up of the flash furnace installation is planned for the fourth quarter of 2016.



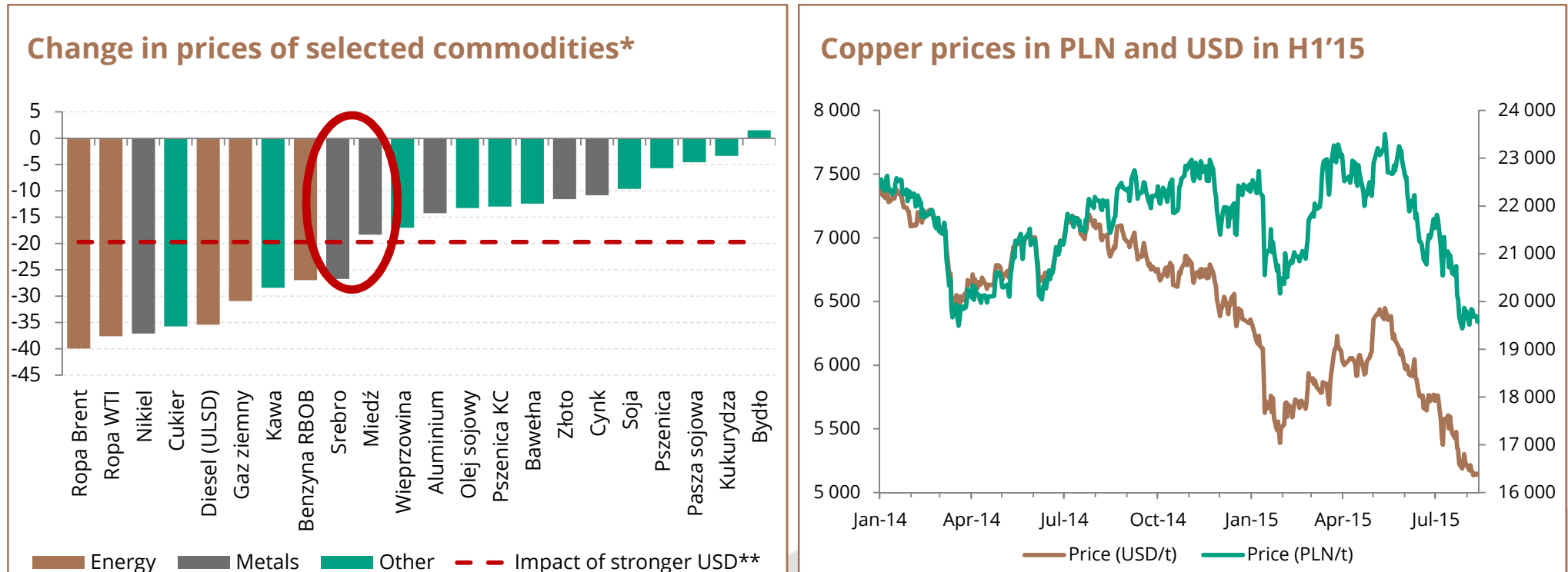
\* Due to the specific nature of work in an operating plant, the process of obtaining building permits and substitute building permits will continue until completion of the investment.



## Macroeconomic environment

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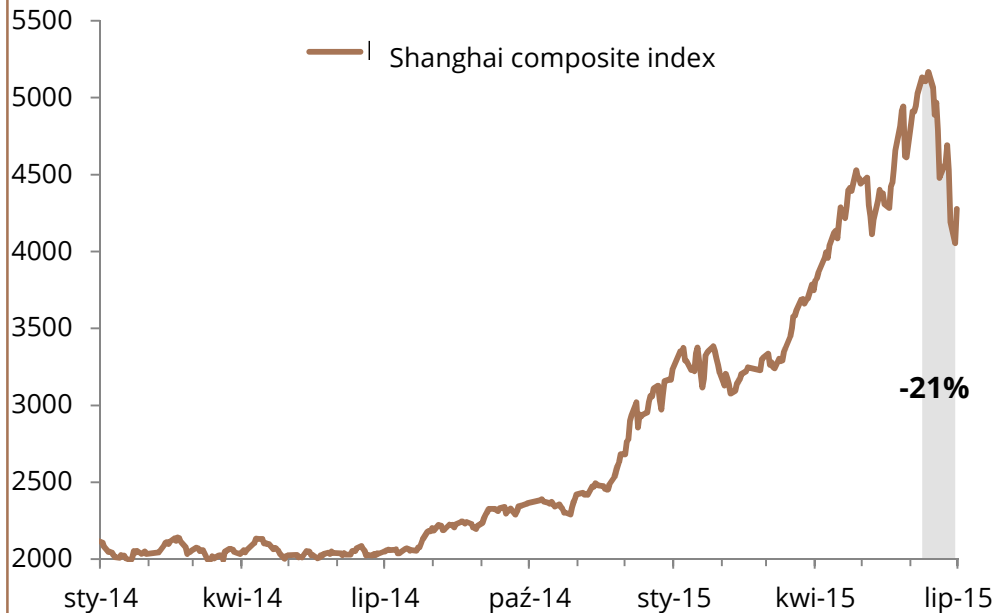
# The drop in commodities prices is largely dictated by the strength of the USD



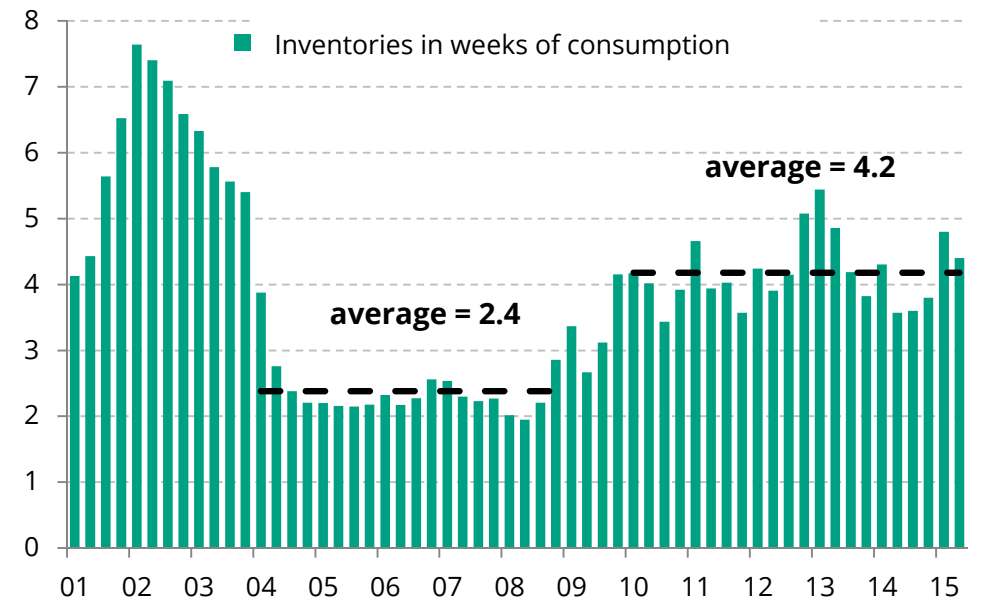
- **The dynamic strengthening of the USD has had a substantial negative impact on the prices of USD-denominated commodities prices** – given the scale of these price changes this factor cannot be ignored. The copper price in the first half of 2015 expressed in the Polish zloty was higher than during all of 2014.
- **The main cause of the strong appreciation of the US dollar is the divergence amongst central banks in their approach to monetary policy.** At the end of 2014 the Fed ended its quantitative easing program and the markets expect the first increase in the cost of money in USD sometime this year. In Europe meanwhile the ECB continues its policy of quantitative easing begun in March, aimed at stimulating inflation and economic growth in the eurozone.
- **Other factors** which continue to impact the financial markets are the **downturn in the oil price and the slowdown in economic growth in China, as well as Greece’s debt problems.**

# Commodities markets are nervously watching Chinese stocks; copper inventories in a seasonal decline

Chinese stocks rose 150% in the first six months, then over a period of 3 weeks lost 21% in value



Inventories\* in weeks of consumption near their average of recent years



- Risk aversion returned to the financial markets in the second quarter. One of the main reasons for this was the **threat of a Greek bankruptcy**. The prolonged negotiations and the lack of a clear direction in them resulted in lowered investor confidence as to economic conditions in Europe.
- For the commodities markets the key month was June. Despite the fears about China's economy, China main stock market index - the Shanghai Composite - from mid-2014 to the start of June 2015 rose by 150%. This led to a speculative bubble, which ended with a **substantial drop in share prices - over 3 weeks the index lost 21%**. While these losses were stopped, such a **volatile reaction by investors had an impact on the prices of commodities** of which China is a large consumer.
- **Official warehouse inventories** (LME, SHFE and COMEX) during 2015 have shown their typical seasonality: in the first quarter they rose by 294 thousand tonnes, followed by a drop to the end of June by 134 thousand tonnes. **Total inventories expressed in weeks of consumption do not however differ from the average level of recent years.**

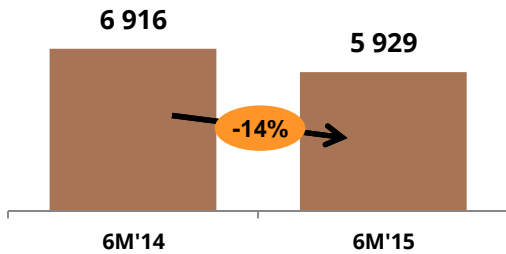


**Economic results**  
**KGHM Polska Miedź S.A. Group**

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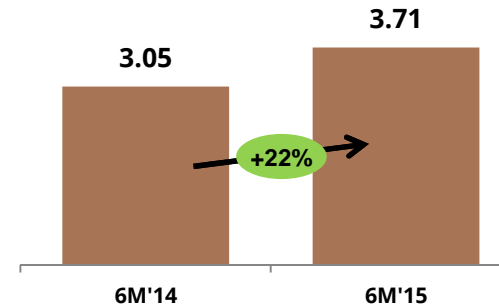
# Metals prices driven by a strong USD; local currencies partially offset the fall in market prices

**Copper prices (USD/t)**



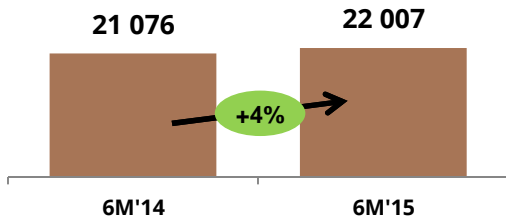
- The clear strengthening of the USD in the second half of 2014 and the first quarter of 2015, has subsided, but remains the main reason for lower commodities prices.
- The price of copper has also fallen due to fears about demand for the metal given the increasingly evident slowdown in the Chinese economy, debt problems in Europe and the tense situation in Ukraine and the Middle East.

**Exchange rate (USD/PLN)**



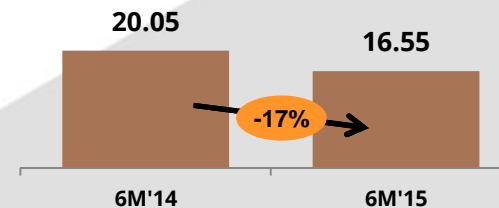
- The global phenomenon of a strong USD is the main factor shaping the USD/PLN exchange rate.
- The Polish economy has been relatively strong as compared to other European countries, making it increasingly attractive to domestic and foreign investors.
- Positive sentiment towards Poland is helping to stabilize the PLN as compared to the main currencies.

**Copper prices (PLN/t)**



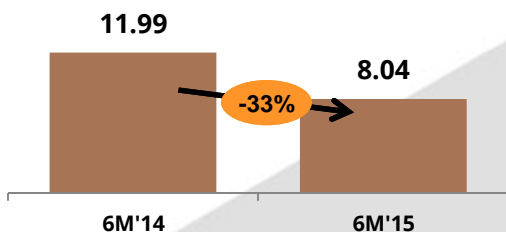
- Copper denominated in PLN is minimally higher than in the same period of 2014, which confirms the theory that the lower USD-denominated price of copper is the result of a strong USD rather than of a loss in value for consumers.

**Silver prices (USD/oz t)**



- The silver price is strongly tied to changes in the gold price.
- Precious metals prices also remain sensitive to the actions of central banks, and in particular to the divergent directions of the US Fed and the ECB.
- Similarly as in the case of copper, the USD-denominated drop in the silver price is to a large degree offset by the weakening in the USD/PLN rate.

**Molybdenum prices (USD/lb)**



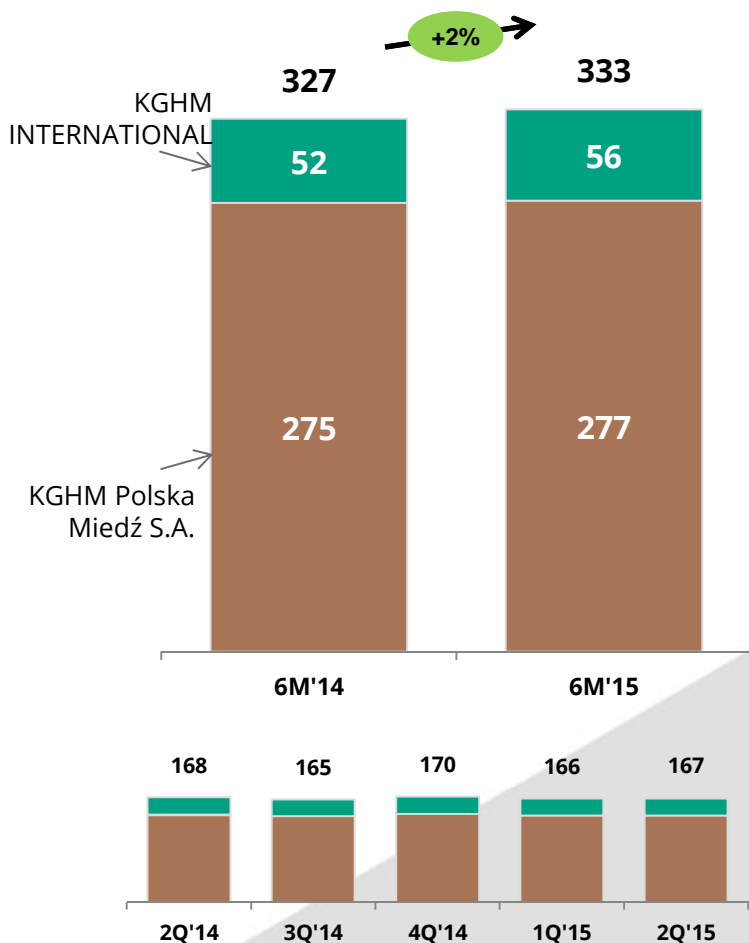
- Weak demand on the spot market combined with a build-up in inventories limits the potential for price rises in the short term.
- The closure of two mines in the USA and one in Canada (a total of 44 mln lbs) and the potential shutdown of production in several others, to a certain extent has restricted the availability of material on the market, which should stabilize the situation in the coming months.

- The growth phase of the global economy appears to have become deferred. Recent macroeconomic data show a certain slowdown in growth by the US economy as well as an improvement in the eurozone.
- A vital question in the coming months will be what steps the Chinese government will take to maintain growth at a solid pace. Of importance will be the progress on the new five-year plan for 2016-2020.
- Geopolitical problems remain a threat to the global economy. For Europe in the short term the Greek situation will be important, and in the long term whether the United Kingdom will leave the EU. There are also stock market-related risks (particularly in China).



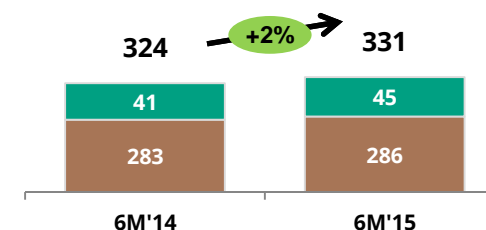
# Production in the Group in the first half of 2015

**Production of copper equivalent from own concentrate (kt)**

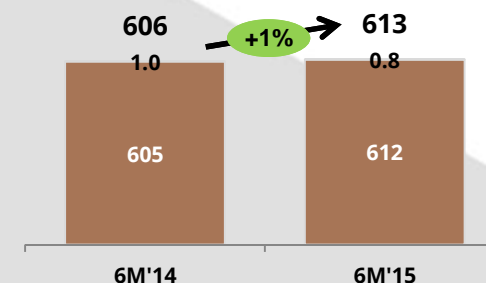


- Copper equivalent production increased as compared to the first half of 2014 in both KGHM Polska Miedź S.A. as well as KGHM International
- In KGHM Polska Miedź S.A., there was an increase in copper, silver and gold production
- In KGHM International the increase was related to higher production by the Robinson mine in terms both of copper as well as TPMs thanks to the mining of ore with higher metals content as well as to an improvement in operating parameters
- KGHM expects production results in the subsequent quarters of 2015 will be at a similar level

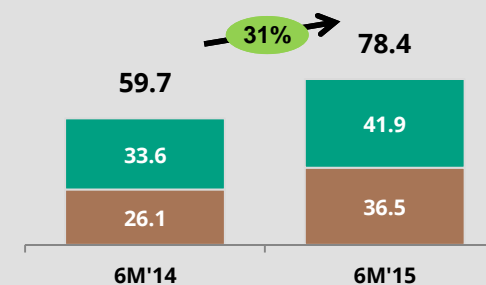
**Production of payable copper\* (kt)**



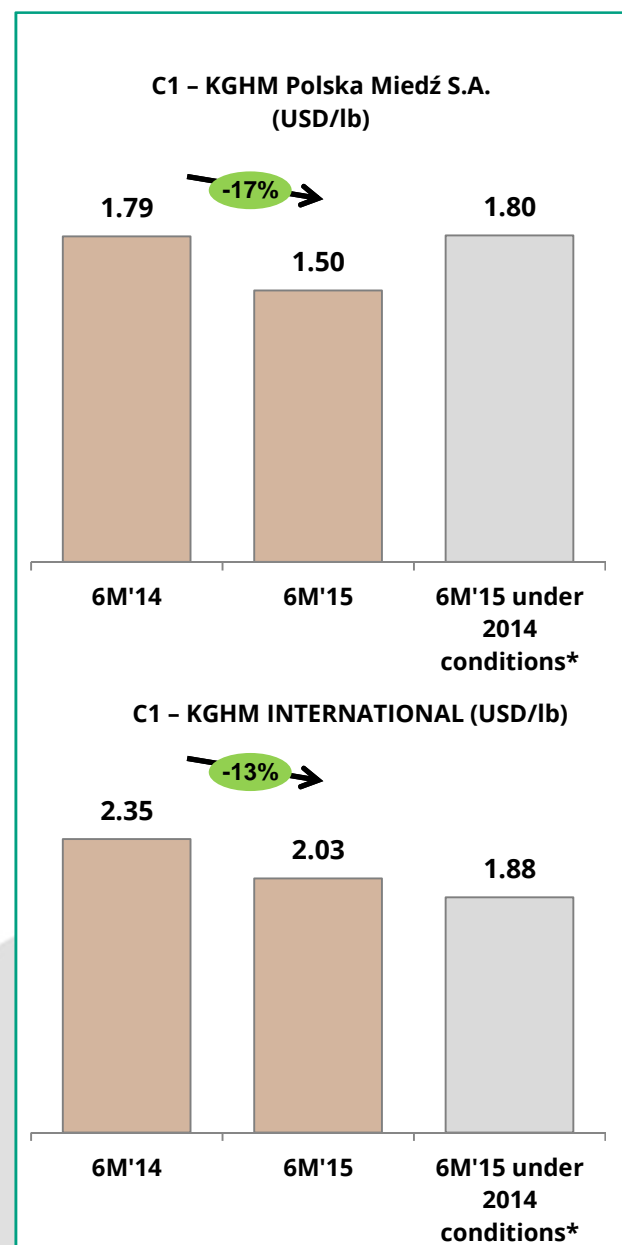
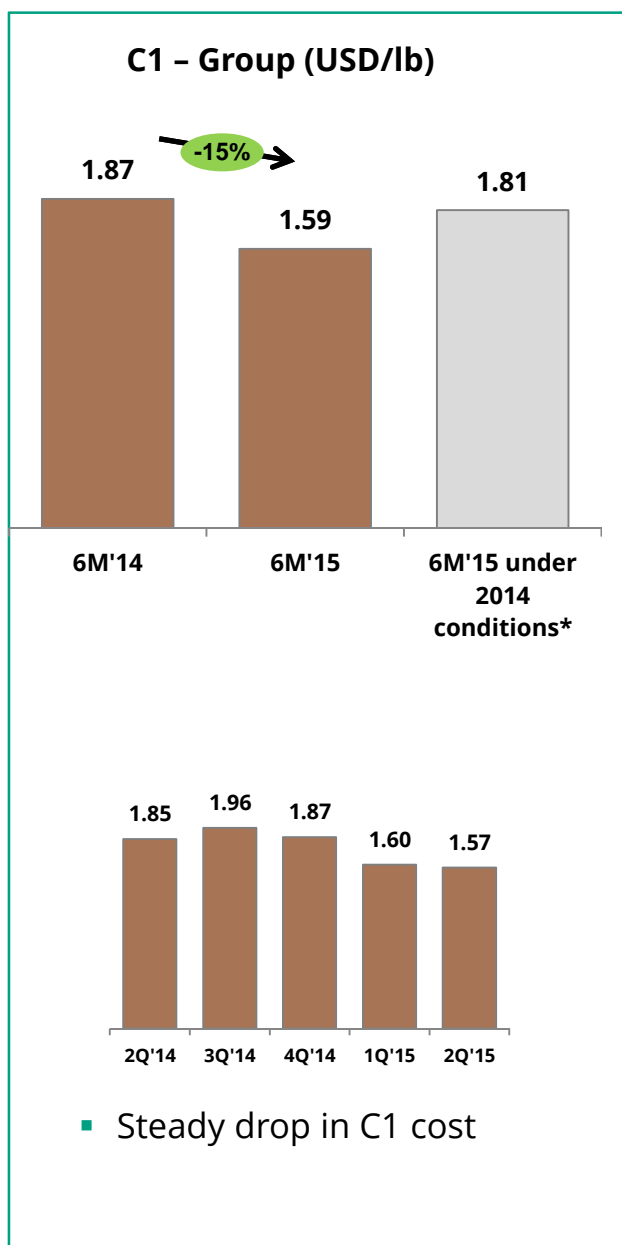
**Silver production (t)**



**TPM production (koz t)**



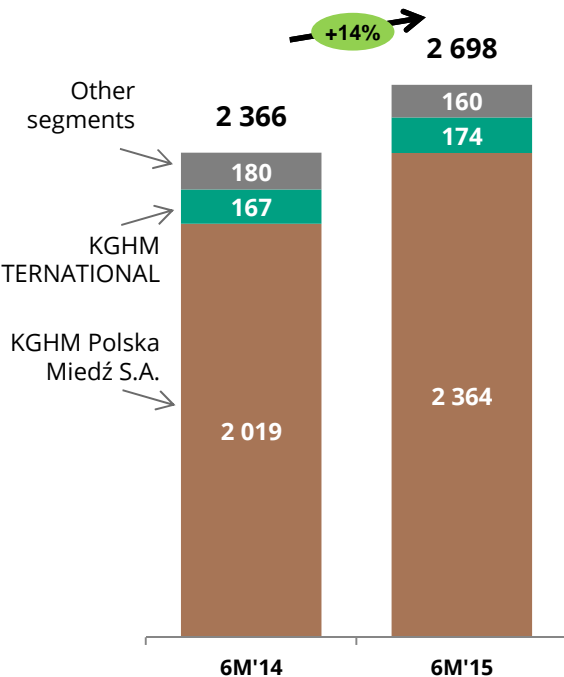
# C1 unit cost in the KGHM Group



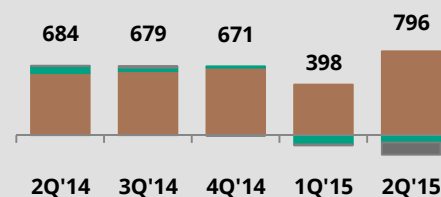
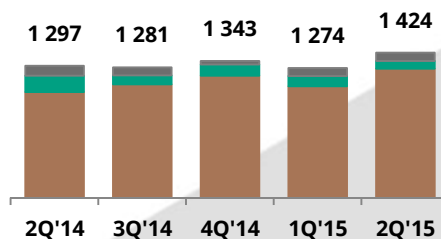
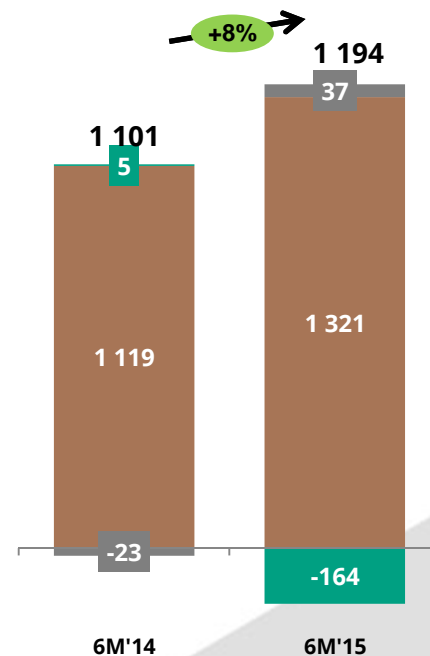
- C1 cost in the Group in the first half of 2015 was lower by 15% mainly as a result of external factors, but even under the metals prices and exchange rates of the first half of 2014, the C1 cost would be lower by 3%
- The drop in C1 cash cost in KGHM Polska Miedź S.A. was mainly due to the weaker PLN as compared to the USD. Under 2014 conditions, C1 cost would have been at last year's level
- The lower C1 cost in KGHM International was due to the higher production of payable copper sold by 25%, mainly in the Robinson mine, alongside a lower valuation of by-products due to the decrease in precious metals prices

# Financial results of the Group

**EBITDA \***  
(mn PLN)

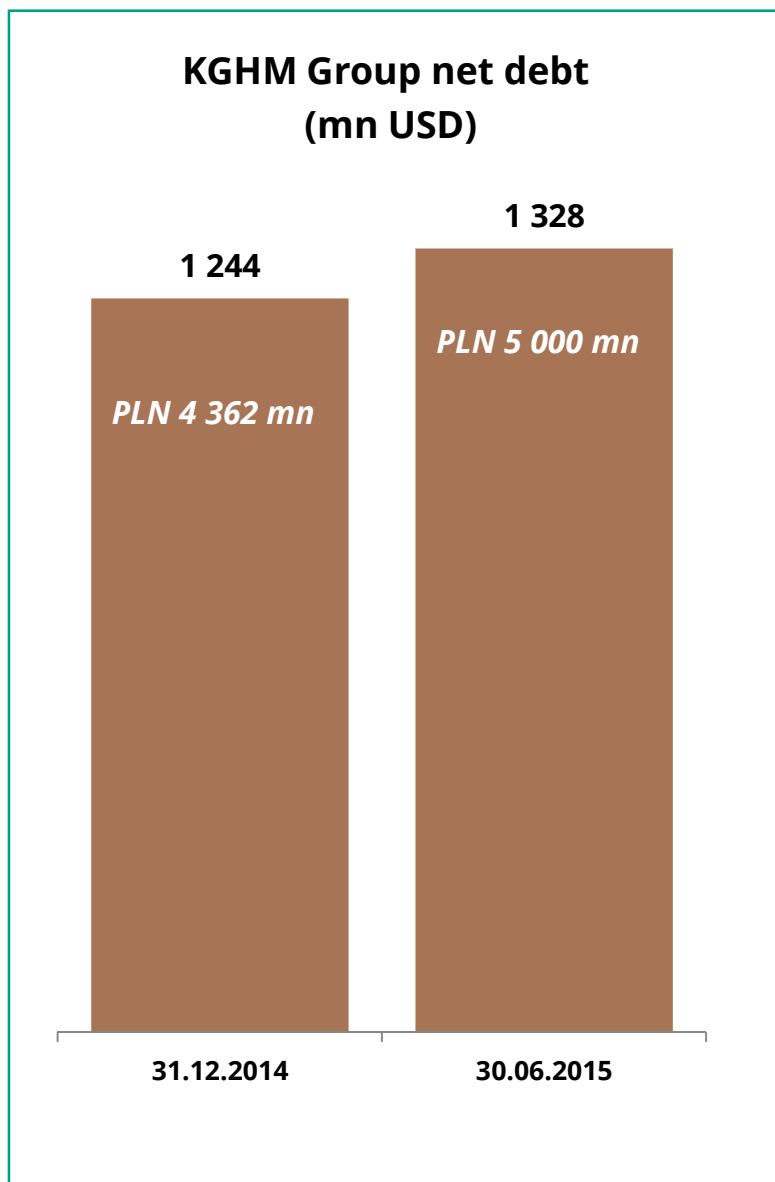


**Profit**  
(mn PLN)



- The increase in EBITDA by PLN 332 million (+14%) and in net profit by PLN 93 million (+8%) was mainly due to KGHM Polska Miedź S.A.
- **KGHM Polska Miedź S.A.**
  - The improved financial results are mainly due to a more favourable USD/PLN exchange rate alongside lower metals prices as well as a higher sales volume while maintaining cost discipline
- **KGHM International**
  - The higher EBITDA by PLN 7 million is due to an increase in sales revenue, mainly due to a higher sales volume while maintaining cost discipline
  - Profit was significantly impacted by:
    - the increase in depreciation by PLN 170 million (mainly due to higher production by the Robinson mine and to capitalised expenditures related to gaining access to new mining areas), and
    - a one-off premium related to the early redemption of bonds by the Company in the amount of PLN 72 million

# In the first half of 2015 the KGHM Group completed the process of debt consolidation



- Pursuant to the financial strategy adopted by the Group, the basic currency in which debt is incurred is the USD (natural hedging).
- The increase in Group debt in the period January 2015 – June 2015 was mainly due to the increase in debt under overdraft facilities (USD 180 million).



## **Economic results** **KGHM Polska Miedź S.A.**

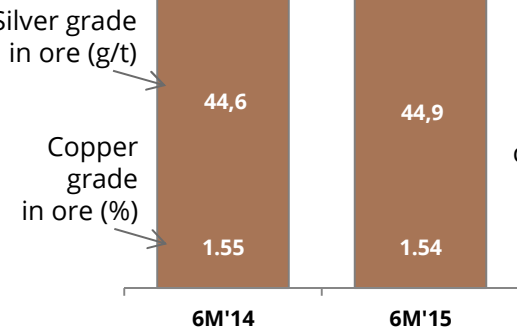
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# Stable level of production

Ore extraction  
(mn t dry weight)

+0,1% →

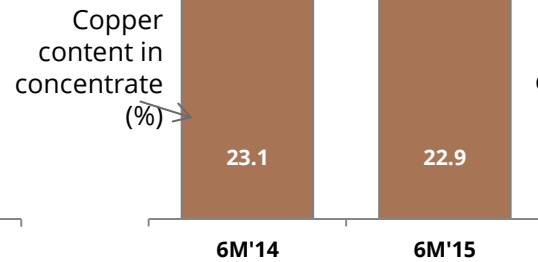
15.7 → 15.7



Production of Cu  
in concentrate  
(kt)

-0,5% →

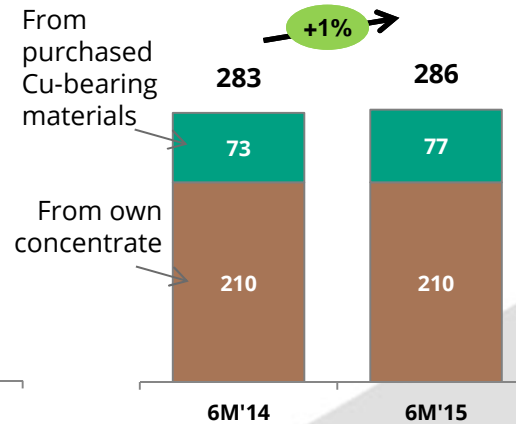
216 → 215



Electrolytic copper  
production  
(kt)

+1% →

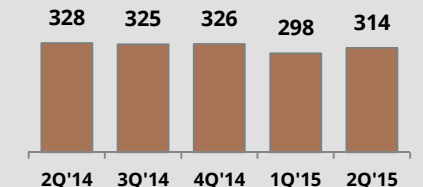
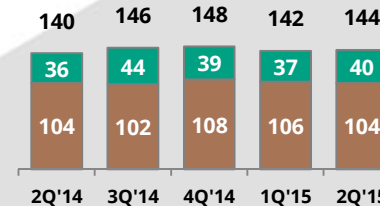
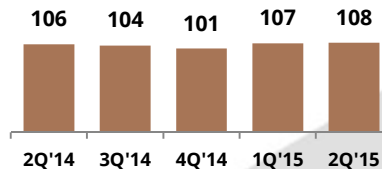
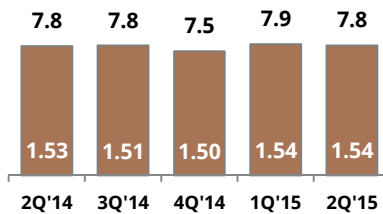
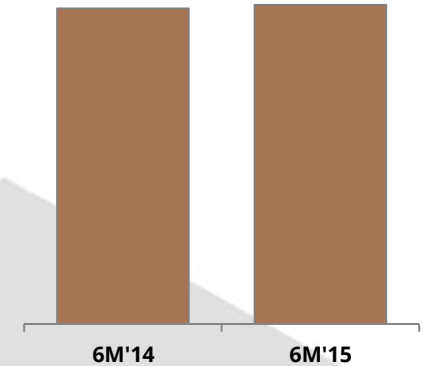
283 → 286



Metallic silver production  
(t)

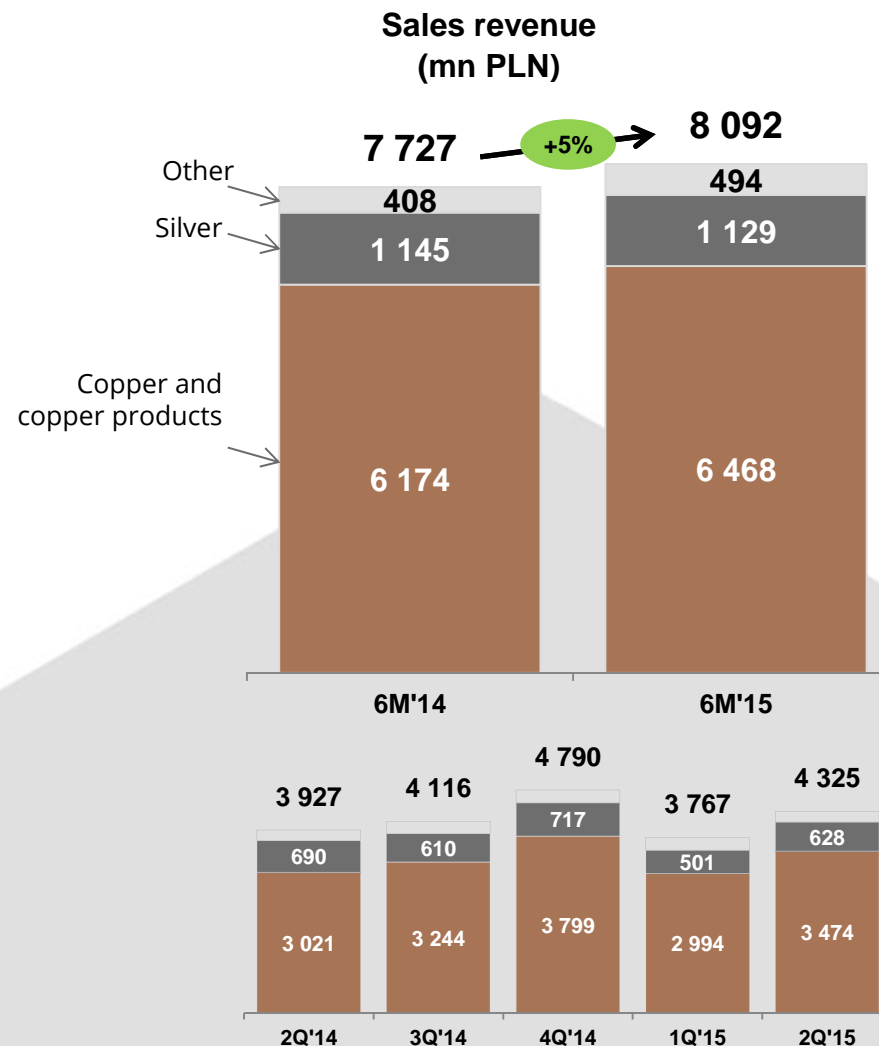
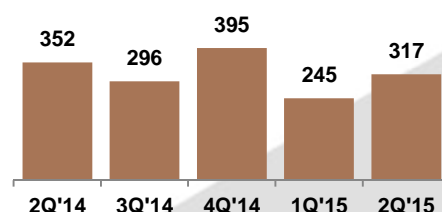
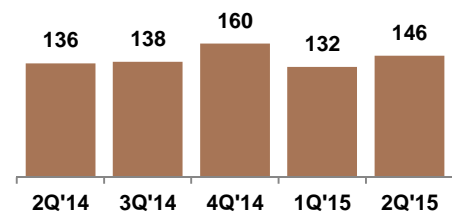
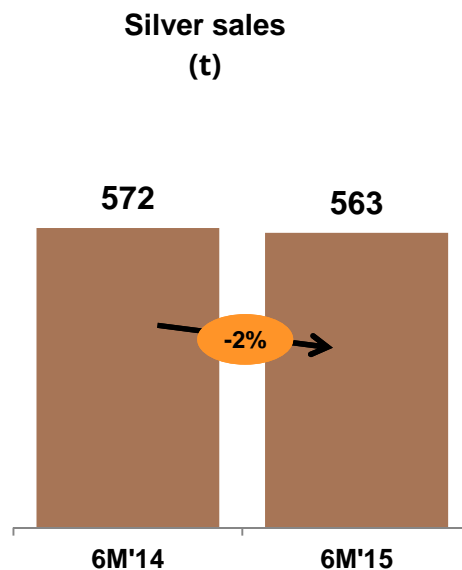
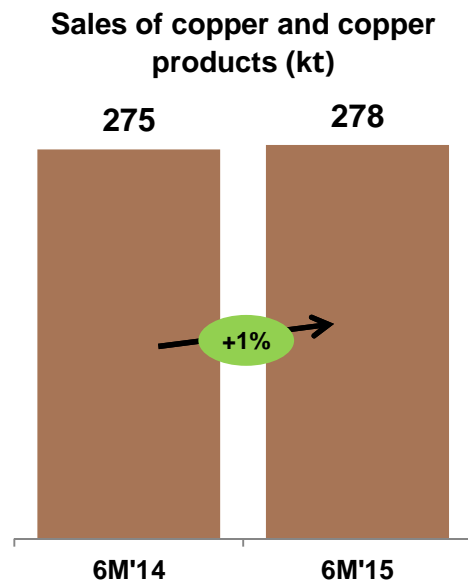
+1 →

605 → 612



- In the first half of 2015 copper content in mined ore decreased from 1.55% do 1.54%
- In coming quarters the Company expects that copper content in mined ore will remain at a similar level
- The lower amount of Cu in concentrate was due to the lower quality feed as compared to 2014
- Electrolytic copper production is at a similar level to that of the comparable period of 2014, while the production of cathodes from purchased materials increased by 4 thousand tonnes.
- The increase in metallic silver production as compared to 2014 is due to the higher content of silver in purchased materials

# Sales revenue in the first half of 2015

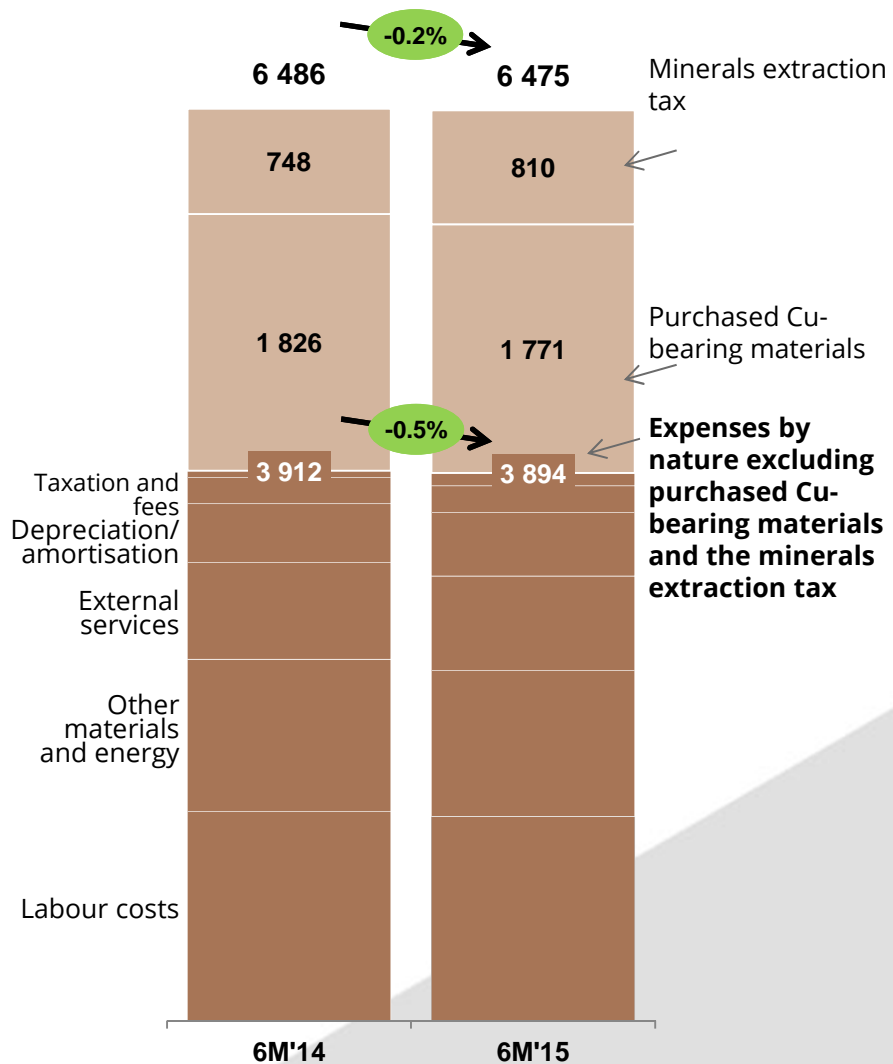


- The increase in copper sales volume by 1% and the increase in gold sales by 25% alongside higher achieved prices (in PLN) of copper (by 4%) led to sales revenue which was 5% higher than in the comparable period of 2014

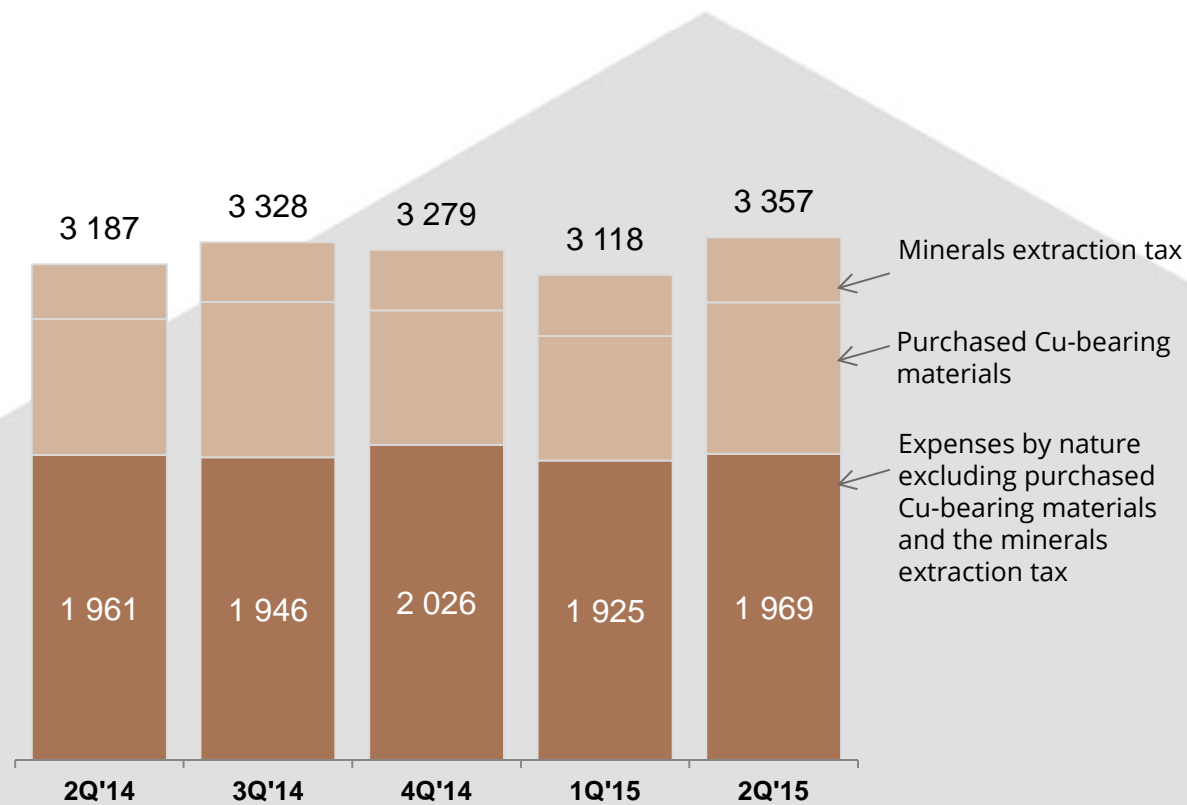
- Sales revenue in the second quarter of 2015 was 15% higher than in the prior quarter, mainly due to a higher volume of Cu and Ag sales (respectively by 13.5 thousand tonnes and 72 tonnes) as well as to a more favourable price of copper expressed in PLN by 3%

# Costs in the first half of 2015

Expenses by nature (mn PLN)

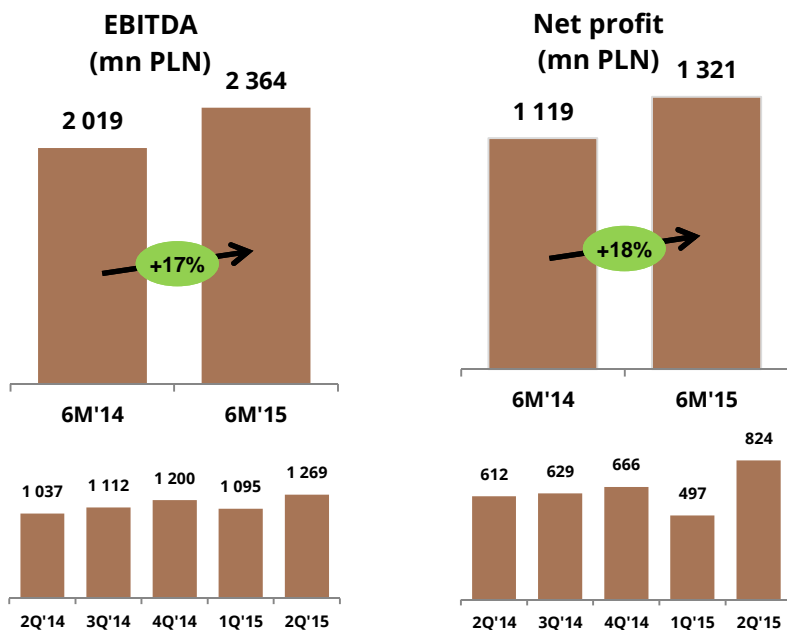


- Total expenses by nature are at a similar level as in the comparable period of 2014 (-PLN 11 million) and have a similar structure

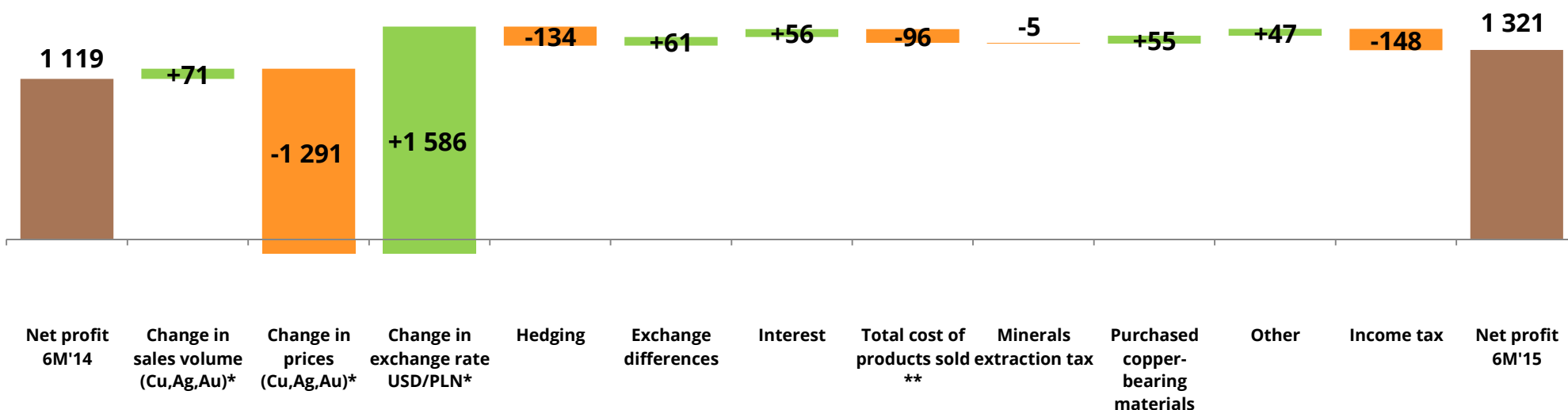




# Financial results in the first half of 2015



- The increase in EBITDA by PLN 345 million (+17%) and in net profit by PLN 202 million (+18%) is mainly due to a more favourable USD/PLN exchange rate alongside lower metals prices
- The improved results were mainly due to the increase in sales volume and a better result on exchange differences and interest



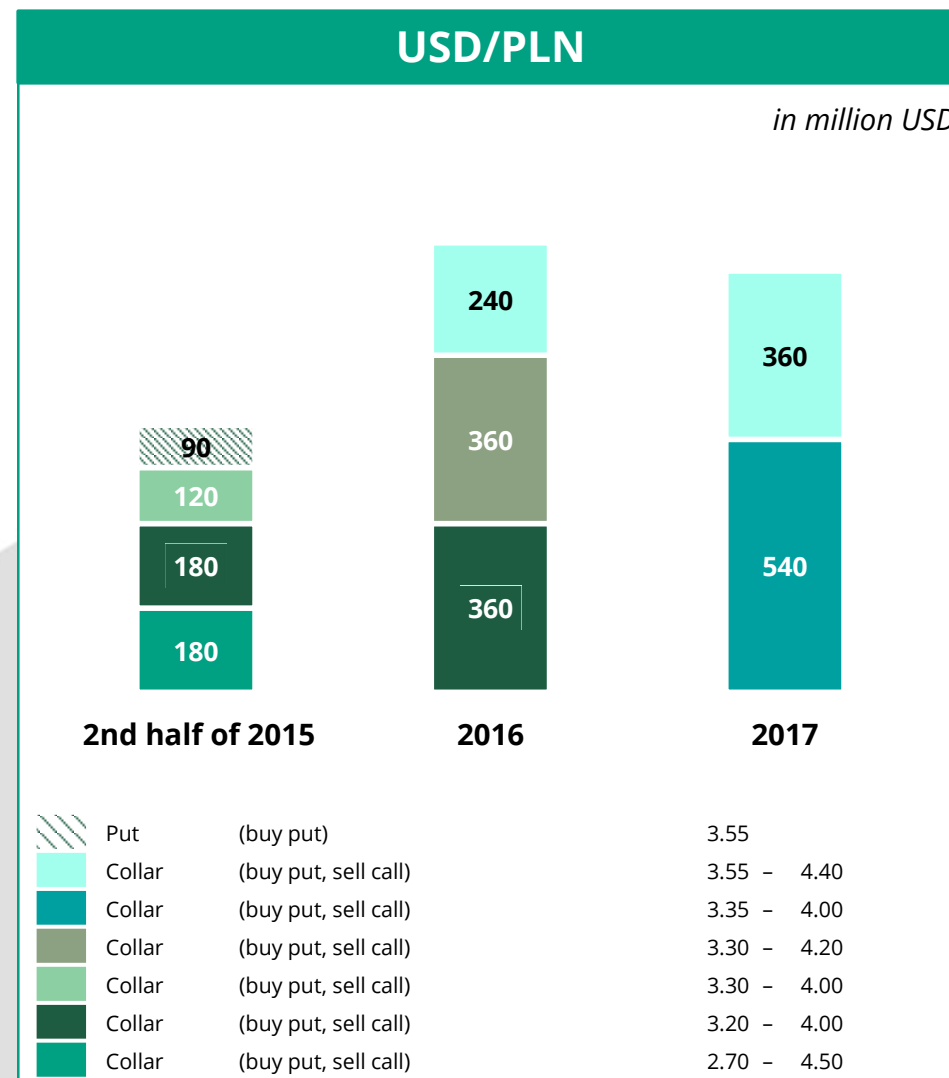
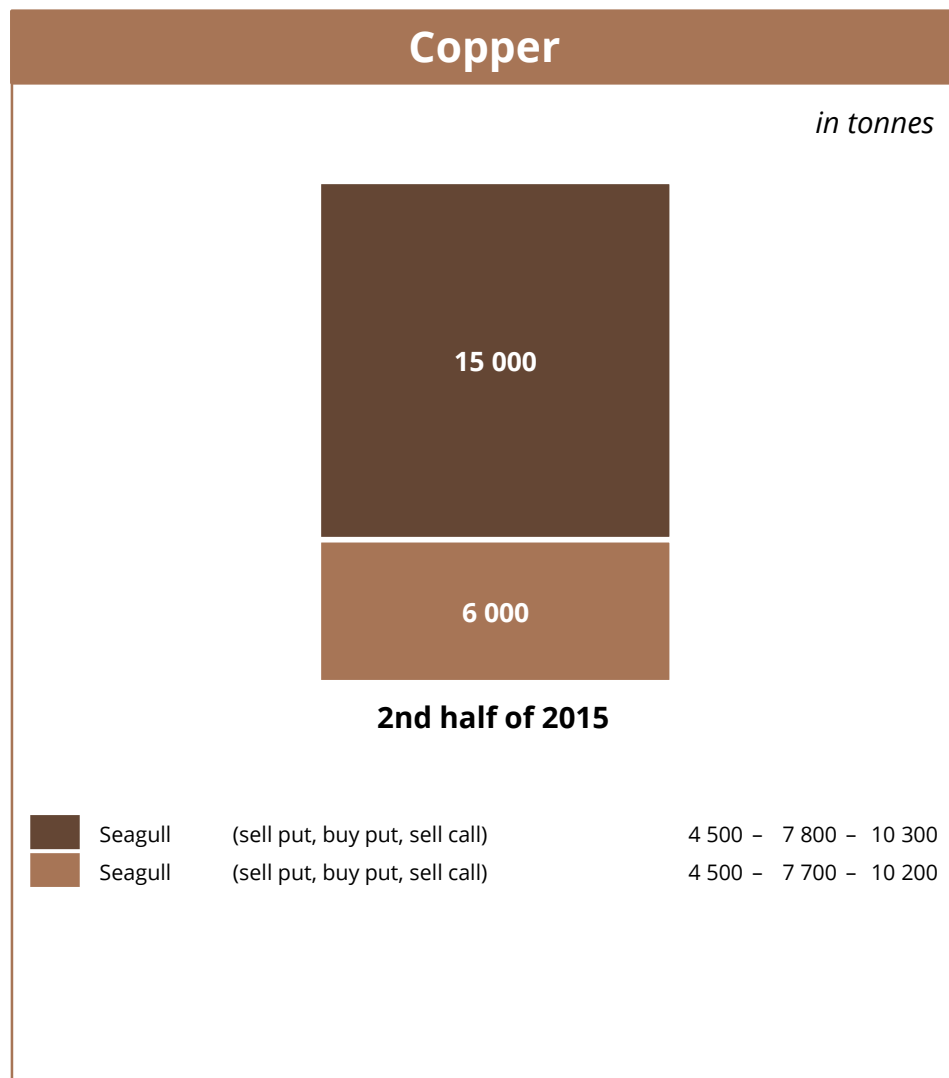
\* Impact on revenue from the sale of copper, silver and gold

\*\* Excluding the minerals extraction tax and the consumed amount of purchased copper-bearing materials

# The accrued result on derivatives achieved by KGHM Polska Miedź S.A. as at 30 June 2015 amounted to PLN 26 million

## Market risk management – hedging position (as at 30 June 2015)

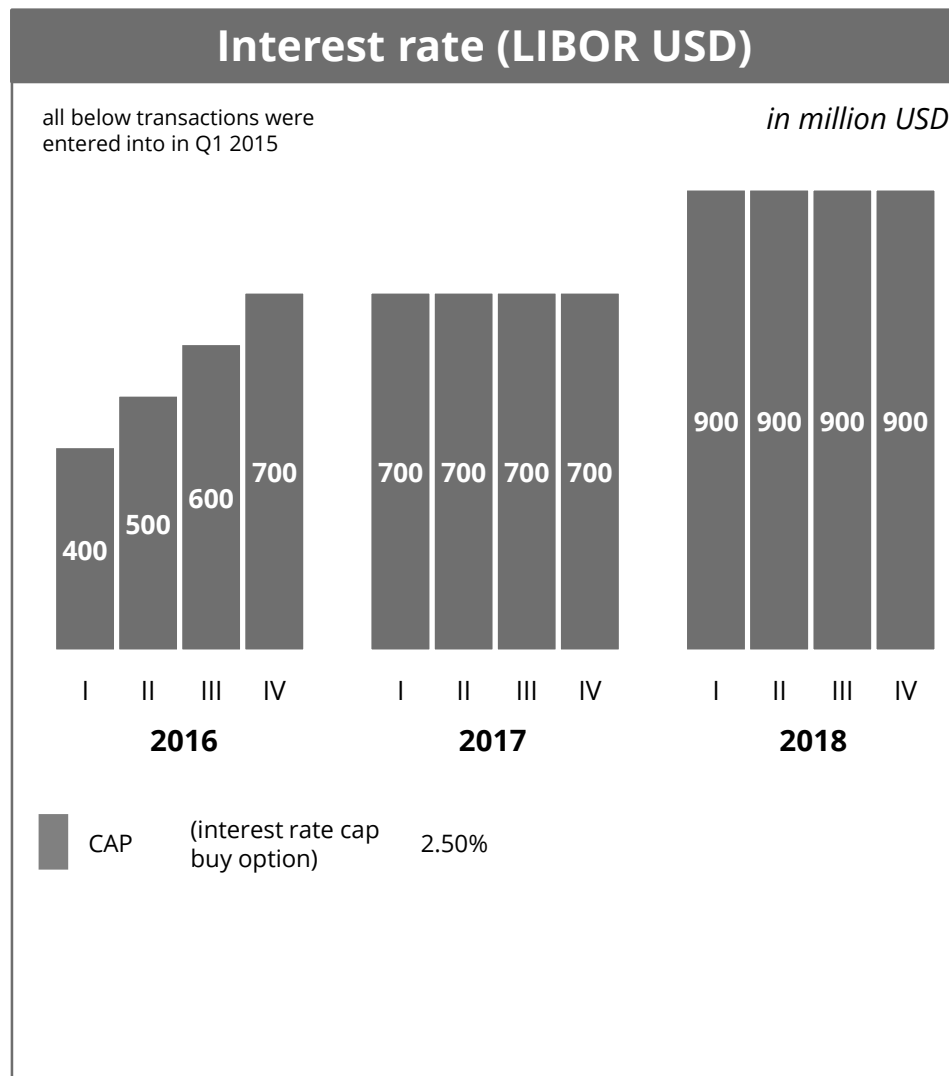
Position in derivatives on the commodities and currencies markets



# KGHM maintains its position in hedging instruments against the risk of an increase in interest rates

## Market risk management – hedging position (as at 30 June 2015)

Position in interest rate derivatives



## Result on derivatives

- In the period January-June 2015, KGHM Polska Miedź S.A. recorded a positive result on derivatives in the amount of PLN 26 million, of which :
  - PLN 221 million increased sales revenue (transactions settled in the first and second quarters),
  - PLN 195 million decreased the result on other operating activities (mainly a change in the measurement of open transactions as at 30 June hedging the period to the end of 2018).
- The fair value of derivatives (MtM) in KGHM Polska Miedź S.A. as at 30 June 2015 amounted to PLN 83 million.
- The revaluation reserve on cash flow hedging instruments as at 30 June 2015 amounted to PLN 201 million.

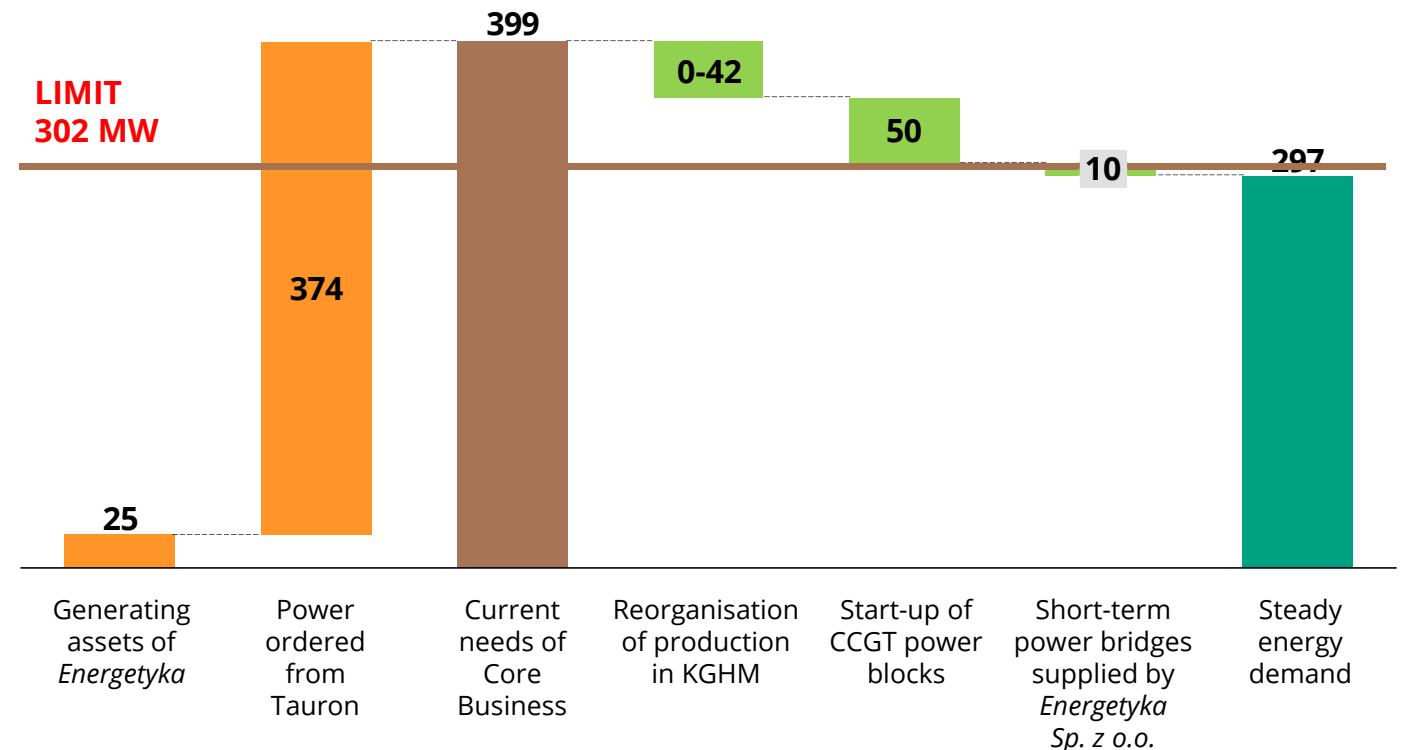
# Energy security for KGHM



- On 10 August 2015 a 20th-degree power restriction level was introduced – the largest possible level of restriction on drawing energy from the National Energy System
- For KGHM this means the necessity to reduce the amount of power drawn from the network by 72 MW
- KGHM generates approx. 80 MW from its own sources of energy, which covers approx. 25% of KGHM's needs under a 20th-degree power restriction situation, and assuming disciplined behavior by the Divisions, this allows us to maintain stable planned production levels



Structure of energy supply to KGHM (20th-degree power restriction)



## KGHM's energy system:

- Power demand (374 MW)
- 18 power stations of 110/6kV + 3 stations of 110/10kV
- 51 110 kV power lines
- High ability to configure connections in the 110 kV network between KGHM and Tauron Dystrybucja

# Securing power supply for KGHM in an emergency (*blackout*)

**In case of a shortfall in energy supply, KGHM is able to independently ensure power to safely evacuate 4.5 thousand mine workers to the surface.**



Thanks to the completion in 2014 and 2015 of projects aimed at enhancing energy security (including the CCGT blocks in Polkowice and Głogów and the natural gas engine in Legnica), KGHM is able to ensure itself of a „minimum security” level, understood as:

- Mining – ensuring power for the transport of people out of the mines.
- Processing - ensuring power to enable the pumping of water and slimes.
- Metallurgy - ensuring power to assure the controlled shut-down of the production line.

# Significant factors posing a threat to the KGHM Group's plans

Area	Measure	Potential impact
1 Risk of changes in metals prices	$Cu < \$5000/t$ $Ag < \$15/oz t$	<ul style="list-style-type: none"> <li>Review of capital expenditures (CAPEX)</li> <li>Probable decrease in the value of production-related assets</li> </ul>
2 Risk of impairment	$\frac{Capitalisation}{Net\ assets} < 0,8$ (for $\geq 12$ months)	<ul style="list-style-type: none"> <li>Need to perform testing for impairment of assets</li> </ul>
3 Risk of changes in economic conditions	$GDP\ China < 7\%$ $\uparrow$ USD index	<ul style="list-style-type: none"> <li>A slowdown in China would lower the rate of growth of copper consumption</li> <li>Further strengthening of the US dollar would put pressure on the USD-denominated prices of commodities</li> </ul>

## Actions undertaken:

- Review projects and investment programs (possible deferment of projects and/or shelving of certain investments)
- Optimise OPEX under the VCP program
- Scenario analysis of the long-term continuation of prices at low levels



**Thank you!**

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