

# Layers of possibilities



**Group results**  
**1st Quarter 2016**

*16 May 2016*

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# Highlights of Q1'16 in the KGHM Polska Miedź S.A. Group

## Key events

**The strategy of KGHM for the years 2015-2020 with an outlook to 2040 was analysed, and the process of revising it was commenced**

Actions were initiated to review the long-term operating plan of the Sierra Gorda mine as well as the operating and development assets of KGHM International

**Sierra Gorda** is implementing a program to cut costs and to enhance operational efficiency

**Deep Głogów** – work continued on sinking the GG-1 shaft (at the end of Q1 2016 the depth had reached 748 meters)

**Pyrometallurgy Modernization Program** – work is on schedule for start-up of the installation in Q4'16.

## PMP – part of the Cu concentrate drying installation



## Production highlights

- |                   |            |
|-------------------|------------|
| ▪ Payable copper  | 166 kt     |
| ▪ Metallic silver | 299 tonnes |
| ▪ TPM             | 55.7 koz   |

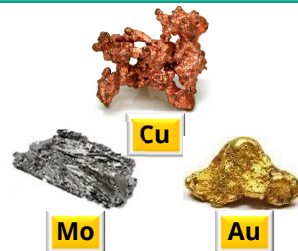
## Economic results

- |                         |            |
|-------------------------|------------|
| ▪ Sales revenue         | PLN 3.9 bn |
| ▪ EBITDA                | PLN 987 mn |
| ▪ Profit for the period | PLN 163 mn |

# Sierra Gorda – challenges related to achieving target financial and production parameters

## Sierra Gorda

- **Mined metals**



- **Ownership**

55% KGHM  
45% Sumitomo

- **Mine profile**

Open-pit



*Extraction of ore from the Sierra Gorda mine*

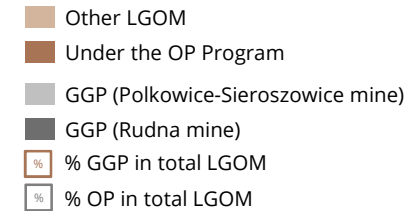
## Key events update

- In the first quarter of 2016 production of copper in concentrate by the Sierra Gorda mine was around 26 thousand tonnes, while production of molybdenum in concentrate was around 9 million pounds.
- Under the proceedings being conducted by the Chilean Environmental Enforcement Agency (SMA) involving a review of the mine's compliance with the issued environmental permit, on 5 April 2016 the position of the JV Sierra Gorda was submitted.
- Key challenges involve achieving target Phase I production levels as well as efficient production parameters, including recoveries and stable processing plant operations.



# Legnica-Głogów Copper Belt\* ore access program (OP)

## Deep Głogów\*\* deposit



### Work performed in Q1 2016

#### Program Status

- The sinking of the GG-1 ventilation (input) shaft continues. At the end of Q1 2016 **the shaft depth had reached 748 m** (of a target 1 340 m). Construction of the shaft includes a concrete lining. A cascade drainage system, together with research holes for further sinking, was completed.
- Since 2006, **98 091 thousand meters of tunnel together with necessary technical infrastructure have been built**. In Q1 2016, 8 160 meters of mine tunnels in the Rudna and Polkowice-Sierszowice mines were excavated.
- Work continues on **Stage II of the Surface-based Cooling Station at the R XI shaft as well as development of the central underground cooling system**, which will enable an increase in the production of cooled air to the mine for the level of 1200 m to 25 MW. Planned date of completion is the second half of 2016.

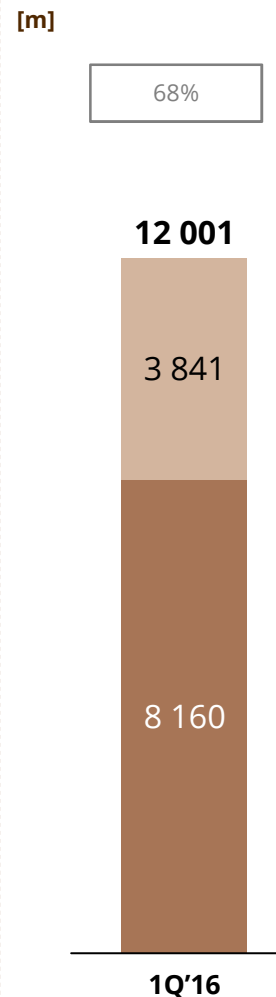


Cooling tower and heat transfer building



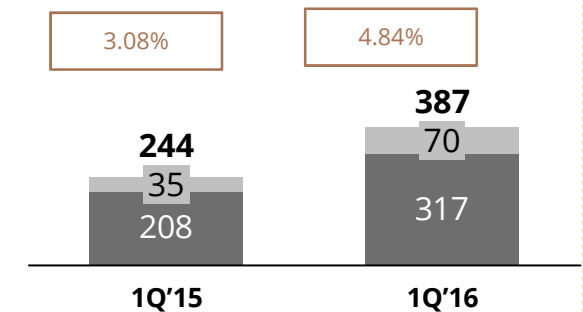
GG-1 shaft sinking site

#### Areas excavated by the Mining Divisions in LGOM

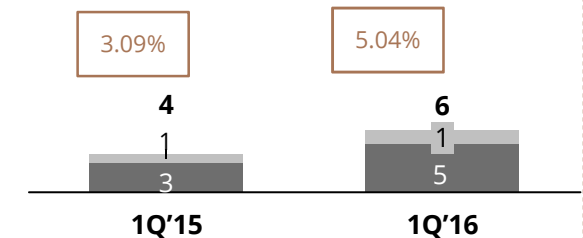


#### Share of production from Deep Głogów in LGOM results

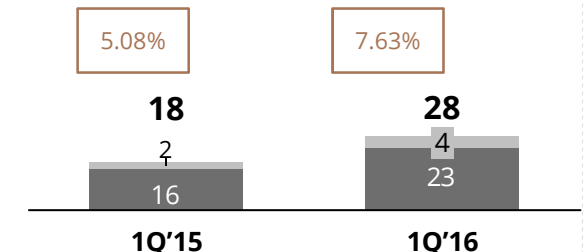
##### Ore extraction dry weight [kt]



##### Amount of Cu in extracted ore [kt]



##### Amount of Ag in extracted ore [k kg]



# Metallurgy Development Program in KGHM

## Construction of a Flash Furnace and associated infrastructure at Głogów I

### Work performed in Q1 2016

#### Status of PMP\*

- Equipment and installations were assembled with respect to:
  - **the Flash Furnace,**
  - **the Electrical Furnace,**
  - **the Power Building, and**
  - **parts of the Charge Preparation Section at the Głogów I smelter/refinery.**
- The majority of construction work has been completed. Work is currently focused on **equipment related to automation and power.**

#### Major facilities realised

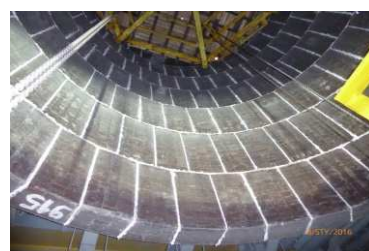
- Work commenced on lining the Flash and Electrical furnaces.
- The Concentrate Drier was handed over.
- The air cooler of the Electrical Furnace Deduster was completed.
- Final assembly of the Electrofilter in the Electrical Furnace unit continues.
- Programming of the Main Control System has commenced.

#### Expected impact in LGOM

- Will account for approx. 80% of copper production using the **best available and most cost-efficient technology.**
- **Elimination of environmental and cost-related risks for approx. 40% of pyrometallurgical production by the Głogów metallurgical complex:**
  - Dust emissions lower by approx. 55%,
  - Gas emissions lower by approx. 58%,
  - Decrease in the amount of tailings to be stored.
- **Improved workplace safety.**
- Possibility to **intensify processing of imported chalcopyrite concentrates.**



Concentrate Drier



Lining of the Electrical Furnace

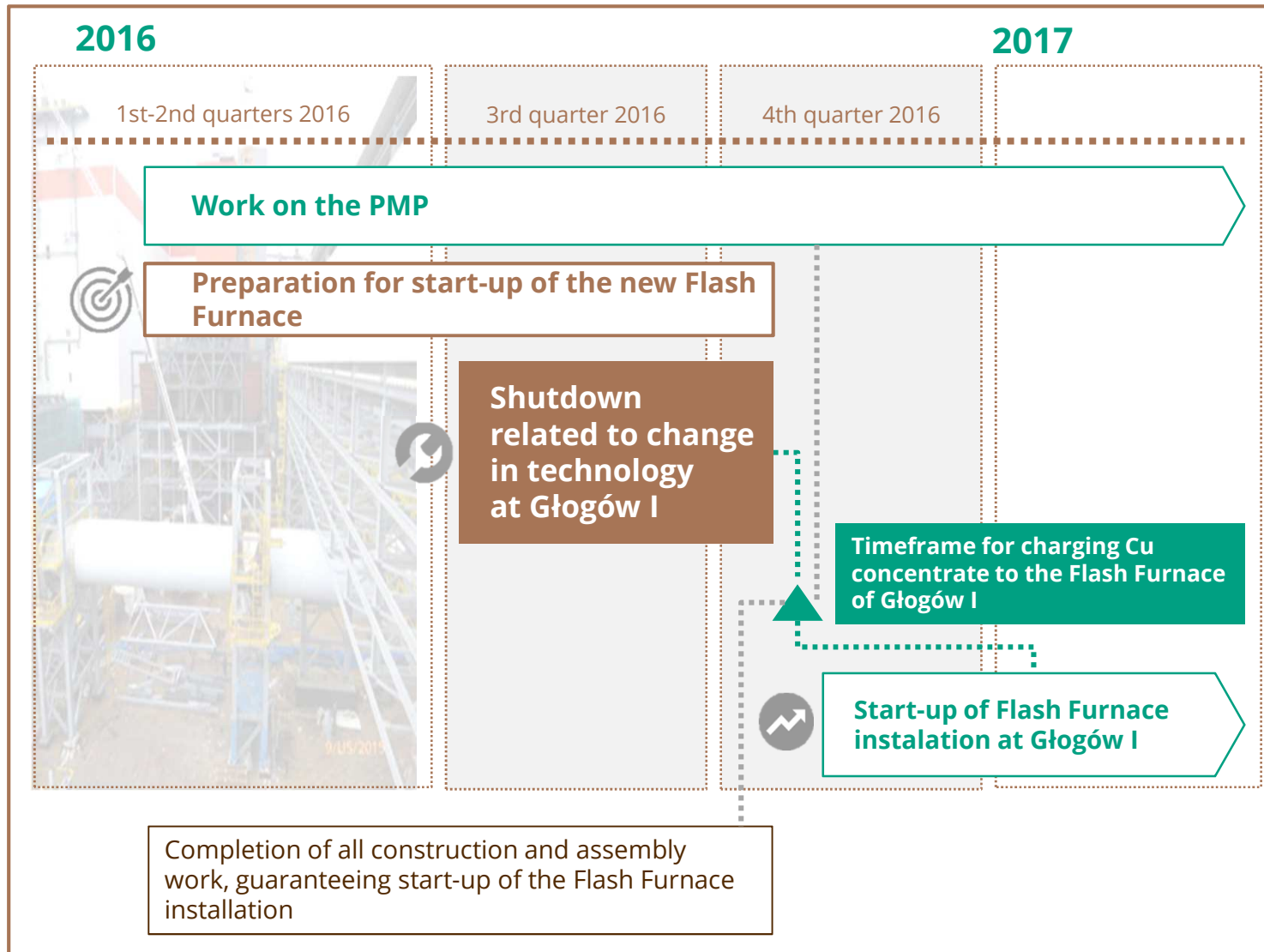


Main Control System

# Metallurgy Development Program in KGHM

Work begun to prepare the Głogów I smelter/refinery for its shutdown related to the change in technology

## Completion schedule



- Final details and optimisation of the shutdown schedule for Głogów I are being finalised in terms of the transfer of operations from the shaft to the flash furnace while at the same time **minimising shutdown time**.
- The shutdown will result in a decrease in electrolytic copper production from own concentrates by **45 kt Cu, or 11%**.
- To maintain the volume of sales of copper and silver produced from own concentrates, KGHM plans to **sell payable Cu and Ag in concentrate** while at the same time optimising the level of inventories at the end of 2016.



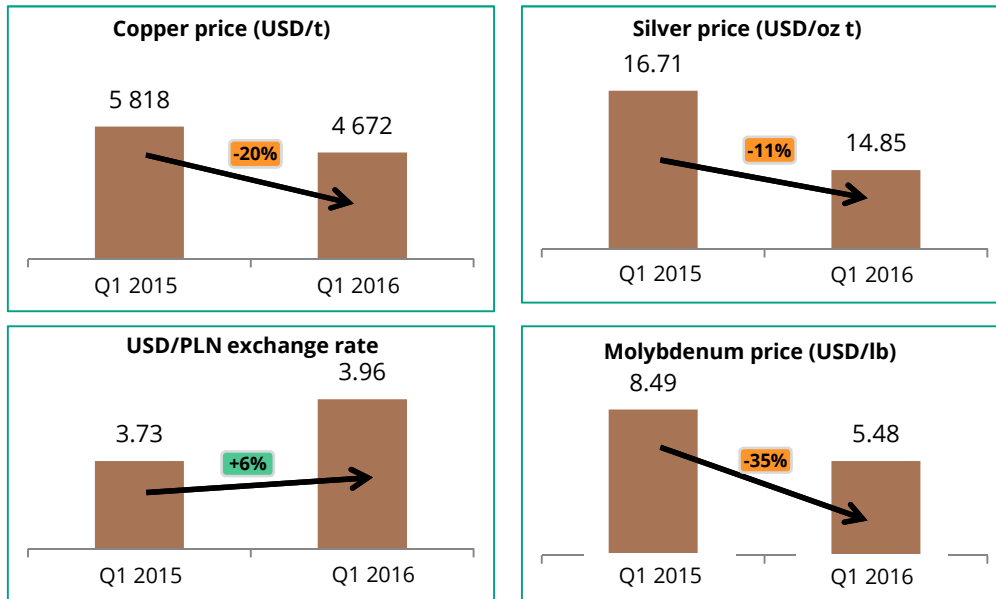
## Macroeconomic environment

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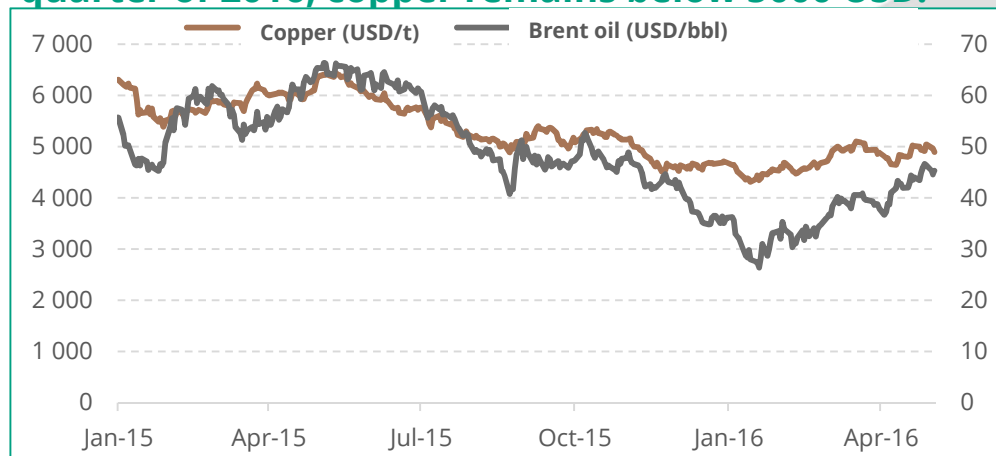
# PLN weakness; Commodities gaining alongside oil, but copper remains below 5000 USD/t

## Lower metals prices alongside a weaker PLN



Source: Thomson Reuters, KGHM

## Despite the 50% recovery in the oil price in the first quarter of 2016, copper remains below 5000 USD.

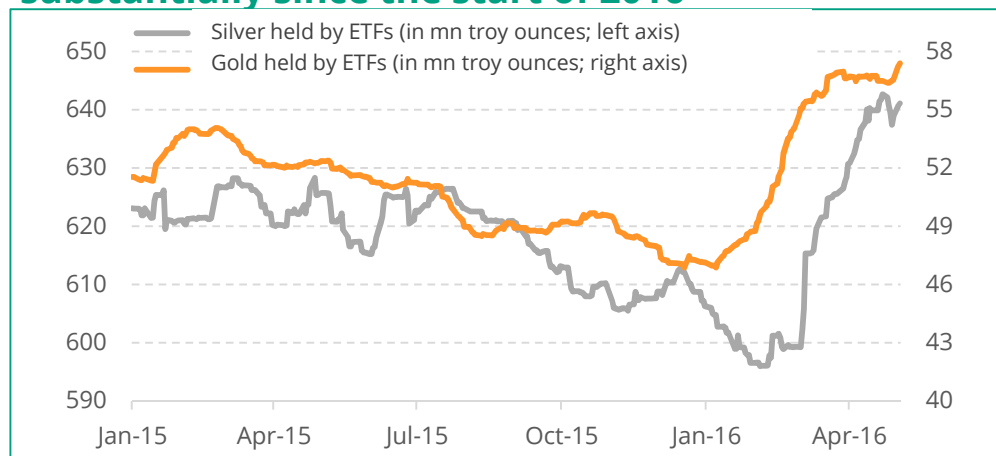


Source : Bloomberg, KGHM

- Following the evident weakening in the PLN in January, the value of the Polish currency strengthened, while the EUR/PLN rate at the end of the quarter was close to the medium-term average (approx. 4.20). The USD/PLN exchange rate also clearly decreased compared to its January peaks (4.1475) to approx. 3.70. However, since the start of April another wave of PLN weakening has been underway.
- Despite the fact that commodities prices remain relatively low, general sentiment to commodities has improved somewhat – most metals have gained since January, although regrettably copper prices remain below 5000 USD/t. The main cause of the rise in the prices of most metals appears to be the clear recovery in the price of oil observed since the start of the year. The weakening of the USD also certainly remains a factor.
- Precious metals recorded solid gains in Q1 2016, thanks among others to more dovish announcements by the Fed regarding the tempo of interest rate rises in the USA.
- No recovery is to be seen in the molybdenum market. The dynamic increase in the price of iron ore (by over 45%) may however be a sign of recovery in the steel industry, which could potentially impact the production of stainless steel, in which molybdenum is used. A higher oil price may also lead to a stimulation in the exploration sector, in which this metal is used.

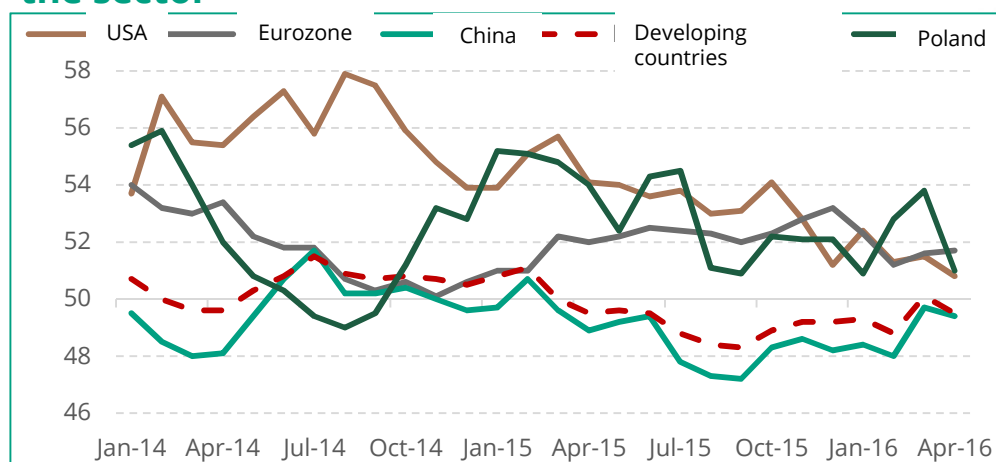
# Greater interest in precious metals; Central banks still at center of attention; Leading indicators without clear direction

## Precious metals resources held by ETFs\* grow substantially since the start of 2016



Source : Bloomberg, KGHM

## Manufacturing PMI still shows no clear direction in the sector



Source : Bloomberg, KGHM

- Since the start of 2016 we have seen a clear increase in new funds flowing into precious metals ETFs. This appears to confirm the better sentiment towards this segment of the commodities market by investors. It is worth noting that investments of this type are usually of a medium- or long-term nature.
- Financial markets remain focused on central banks. In March the European Central Bank once again decreased interest rates, and also increased the assets purchase program to EUR 80 billion monthly (from EUR 60 bn). The US Fed meanwhile is pursuing a policy of increases, though at a lower tempo than assumed at the end of 2015.
- Relatively good data is coming from the USA, in particular from the labour market. Emerging markets remain under pressure. In China the Caixin\*\* PMI has clearly recovered, though it remains below 50 points. In the eurozone there are signals of stabilisation.



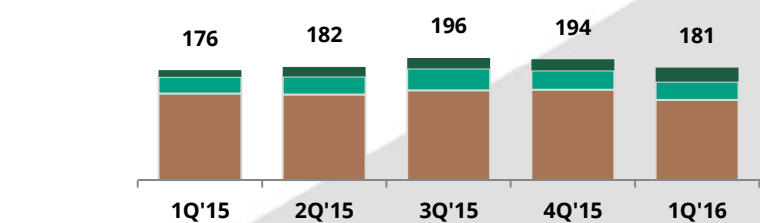
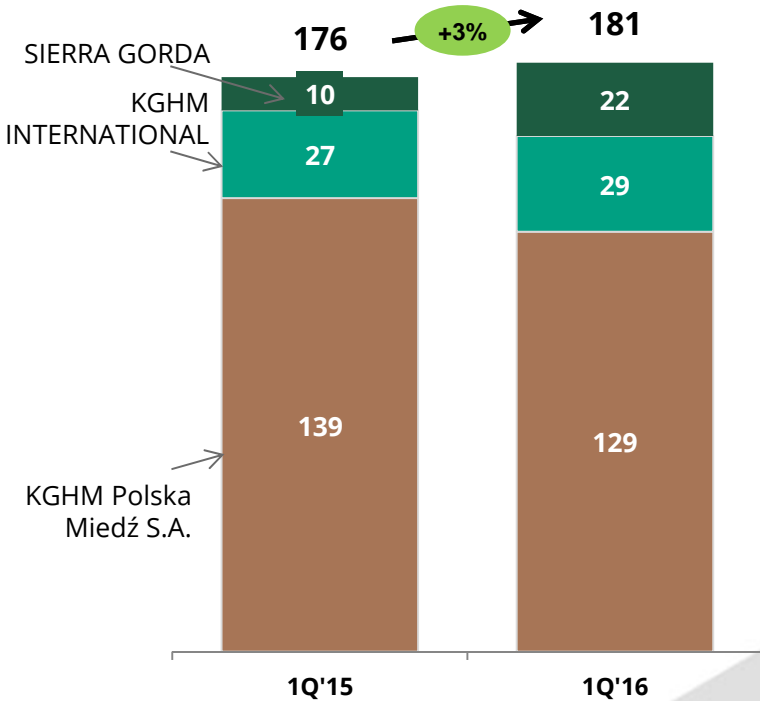
# Economic results

## KGHM Polska Miedź S.A. Group

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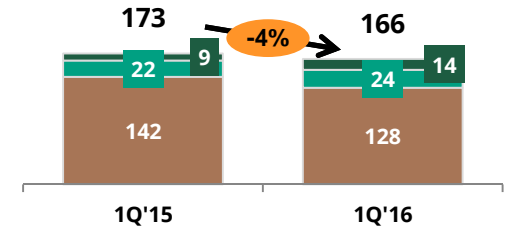
# Higher production by the Group

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

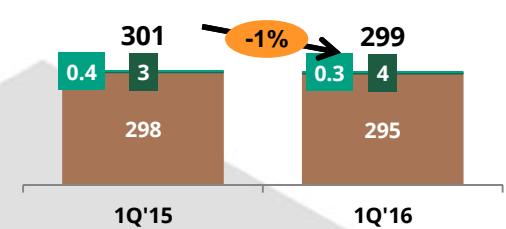


- The higher production of copper equivalent from own concentrates in the Group was due to higher production of gold and molybdenum.
- Payable copper production was lower due to preparations for the start-up of the flash furnace by KGHM Polska Miedź S.A., and the related build up of half-finished products inventories.
- The substantially higher volume of precious metals (by 32%) as compared to 2015 was due to the higher processing of concentrates rich in gold by KGHM Polska Miedź S.A. and to higher production by the Robinson and Sierra Gorda mines.
- Molybdenum – production of this metal by the Sierra Gorda mine commenced in April 2015.

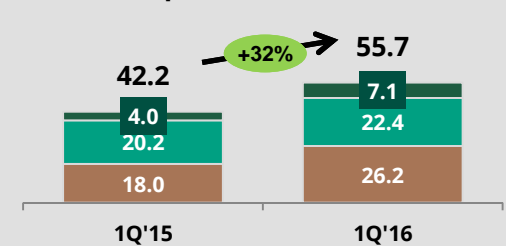
**Payable copper production (kt)**



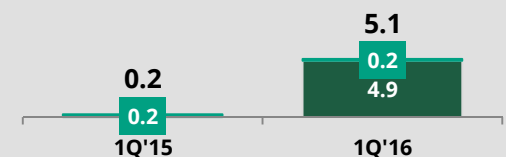
**Silver production (t)**



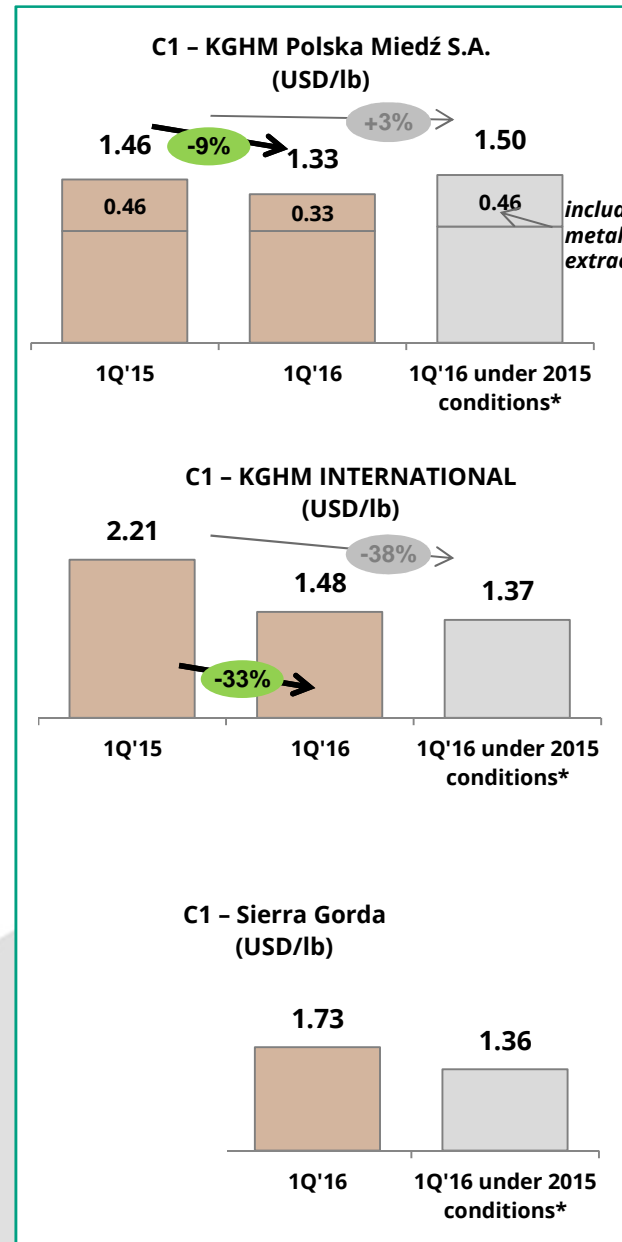
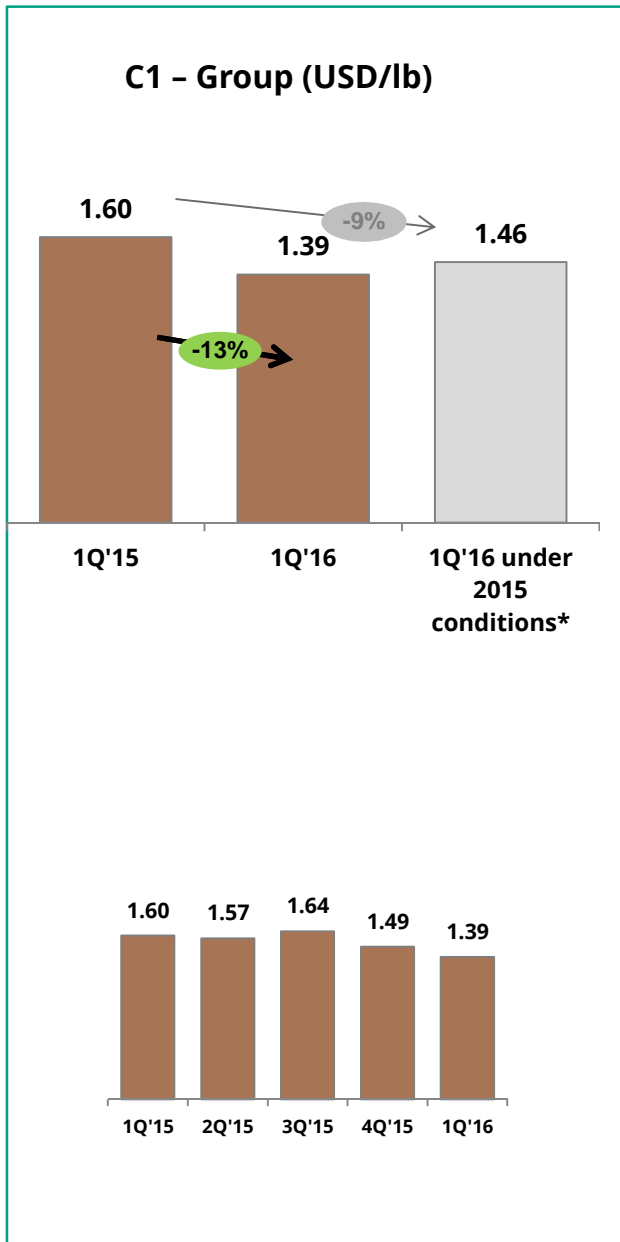
**TPM production\* (koz t)**



**Molybdenum production (mn lbs)**



# Decrease in C1 unit cost in the Group



- C1 cost in the Group in the first quarter of 2016 was lower by 13%, mainly due to a higher volume of copper and associated metals.

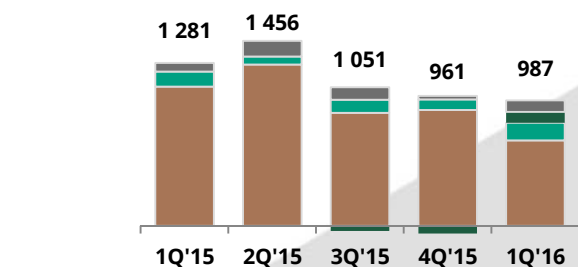
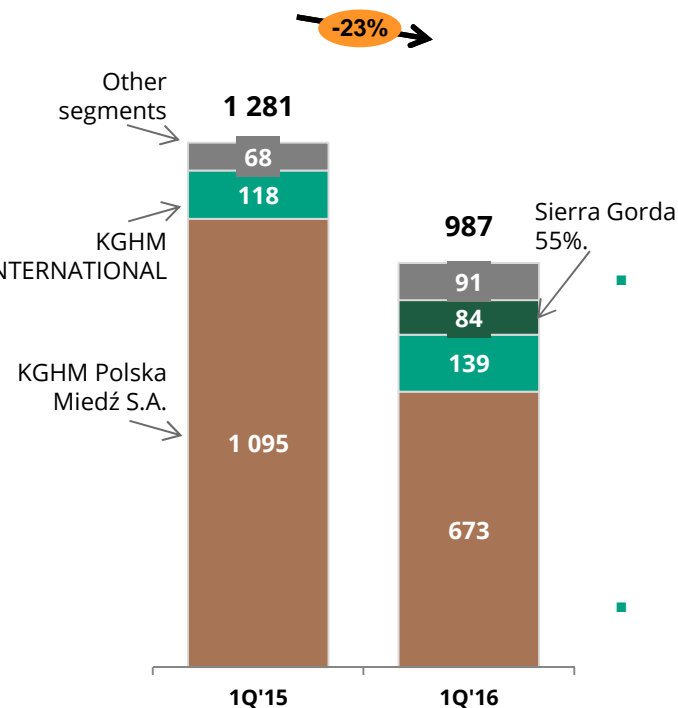
Under the metals prices and exchange rates of the same period of 2015, C1 cost would have been lower by 9%.
- The drop in C1 cash cost in KGHM Polska Miedź S.A. by 9% was mainly due to the weaker PLN as compared to the USD and to a lower metals extraction tax (due to lower metals prices).

Under 2015 conditions, C1 would have amounted to 1.50 USD/lb and would have been slightly above last year's level.
- The lower cost in KGHM International was mainly due to the Robinson mine, in which a high production volume was associated with lower costs.
- Sierra Gorda decreased its C1 cost as compared to the fourth quarter of 2015 (2.56 USD/lb). The lower cost was due to improved efficiency, reflected in a lower number of problems leading to unplanned maintenance shutdowns. In addition, the company substantially decreased the costs of external services as a result of renegotiated contracts, flotation reagent costs due to lower consumption and fuel costs due to lower prices.



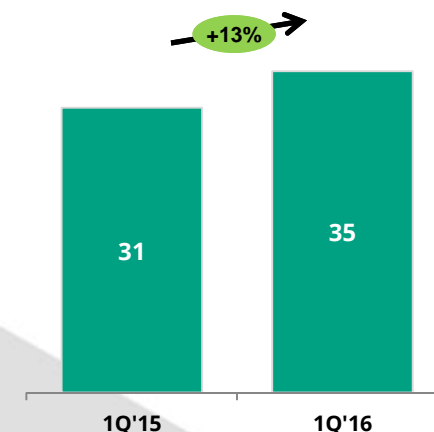
# Operating results of the Group

**Adjusted EBITDA \*  
(mn PLN)**

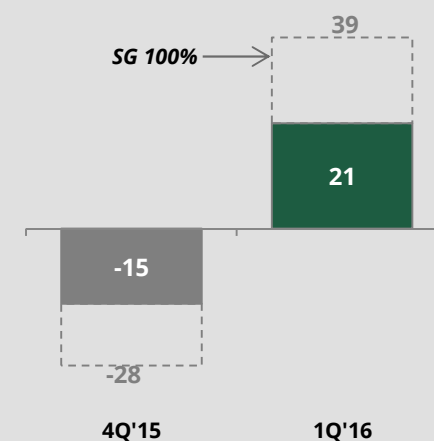


- The decrease in the Group's EBITDA by PLN 294 million was mainly due to the deterioration in macroeconomic conditions.
- KGHM Polska Miedź S.A.
  - The lower EBITDA by PLN 422 million (-39%) was mainly due to the deterioration in metals prices and to the lower sales volume (due to the planned shutdown at the Głogów smelter/refinery) which was partially offset by the weaker PLN versus the USD and lower costs.
- KGHM International
  - EBITDA in the segment KGHM International\*\* in the first quarter of 2016 amounted to PLN 139 million (USD 35 million). The increase in USD terms by 13% compared to the corresponding period in 2015 was the result of consistent cost discipline. The improved EBITDA was achieved despite the lower revenues caused by lower prices.
- Sierra Gorda (55%)
  - In the first quarter of 2016, Sierra Gorda for the first time since the start of commercial production (in July 2015) achieved a positive EBITDA (PLN 84 million; USD 21 million). Higher EBITDA in such unfavourable macroeconomic conditions was possible thanks to the systematic improvement in processing capacity, more efficient utilisation of production assets and lower operating costs.

**Adjusted EBITDA in KGHM International \*\* (mn USD)**



**Adjusted EBITDA in Sierra Gorda 55% (mn USD)**

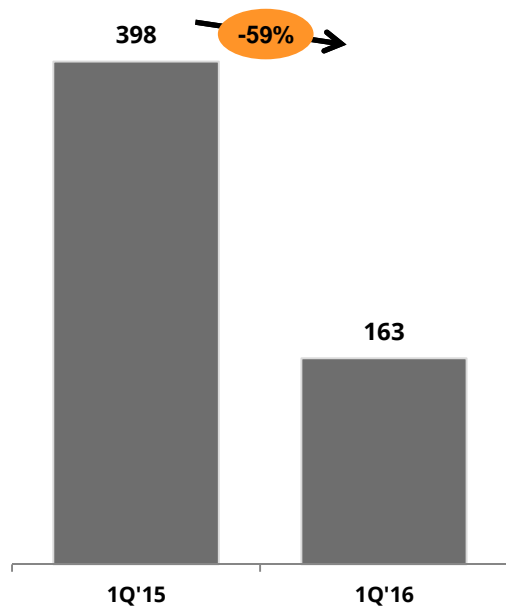


\* Adjusted EBITDA = EBITDA (profit/(loss) on sales + depreciation/amortisation) adjusted by impairment losses on non-current assets

\*\* Adjusted EBITDA reflects the impact of the combination of 0929260 B.C. (amalgamation) and settlement of the purchase price of Quadra FNX (purchase price allocation)

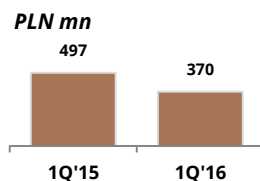
# Financial results of the Group

## Profit for the period (mn PLN)



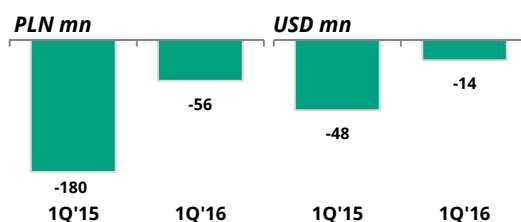
- In the first quarter of 2016 consolidated profit for the period amounted to PLN 163 million and was 59% lower than in the first quarter of 2015.

## Segment KGHM Polska Miedź S.A.



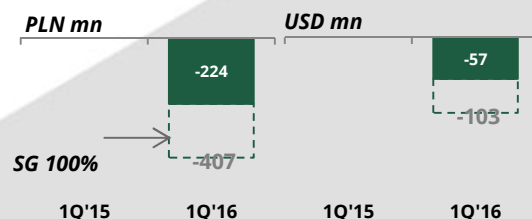
- The net profit of KGHM Polska Miedź S.A. decreased by 26%. Detailed information on the results of the Parent Entity is presented on subsequent slides.

## Segment KGHM International – excluding the results of Sierra Gorda



- The lower net loss of KGHM International (excluding the results of Sierra Gorda) is the result of an improved net result on sales due to an increase in EBITDA by USD 4 million and to lower depreciation by USD 43 million related to the impairment losses recognised in the fourth quarter of 2015.

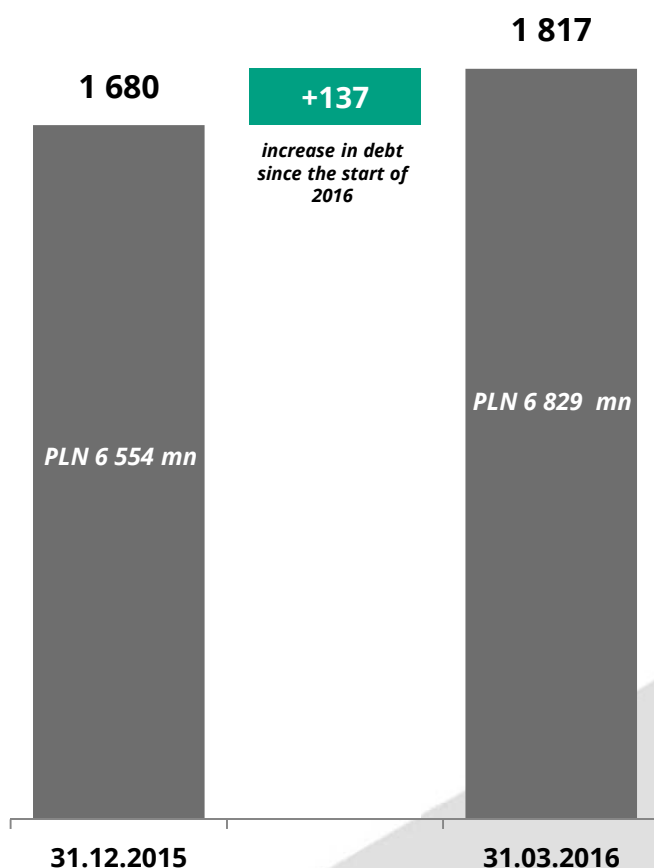
## Segment Sierra Gorda (55%) – consolidated using the equity method



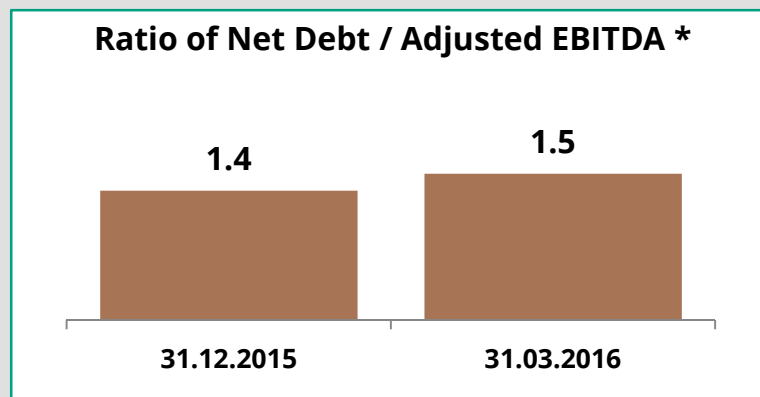
- Apart from operating factors, the net loss recorded in the first quarter of 2016 was mainly impacted by the costs of interest on the owner loans granted by the Partners to finance construction of the mine in the years 2012-2014. Interest on these loans, charged to the financial result for the first quarter of 2016, amounted to USD 73 million (on a 100% basis).
- In the first quarter of 2015, Sierra Gorda functioned under the project stage, and therefore the financial results were not recognised.

# Net debt of the Group – as at the end of March 2016

## KGHM Group net debt (mn USD)



- Consistently, pursuant to the financial strategy adopted by KGHM Polska Miedź S.A., the basic currency in which debt is incurred is the USD (natural hedging).
- Due to its flexible form of financing and to its low cost, the Company also makes limited use of EUR-denominated credit.
- The increase in debt in the first quarter of 2016 was mainly due to the financing of investments, of which the main projects were:
  - PUZ (GGP)** – Deposit Access Program (incl. Deep Głogów),
  - PMP** – Pyrometallurgy Modernisation Program at the Głogów smelter/refinery,
  - Sierra Gorda** – financial support.
- Net debt at the end of Q1 2016 remains at a safe level.



\* Adjusted EBITDA = EBITDA (profit/(loss) on sales + depreciation/amortisation) adjusted by impairment losses on non-current assets



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

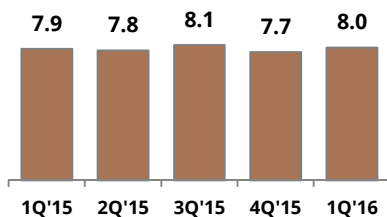
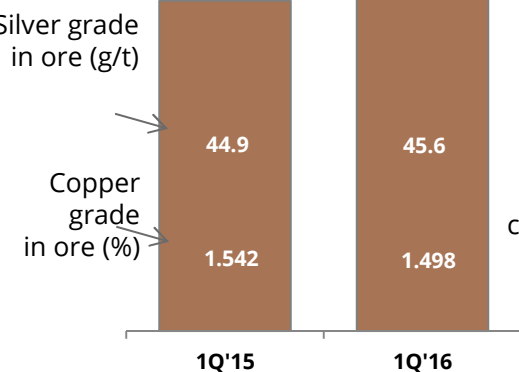
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# Stable level of production

Ore extraction  
(mn t dry weight)

+1% →

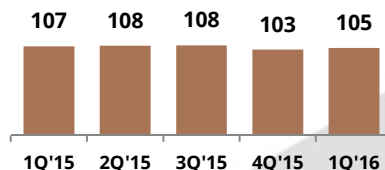
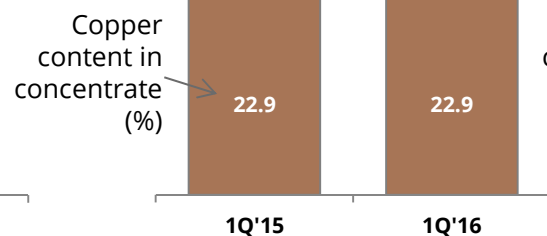
7.9 → 8.0



Production of Cu  
in concentrate  
(kt)

-2% →

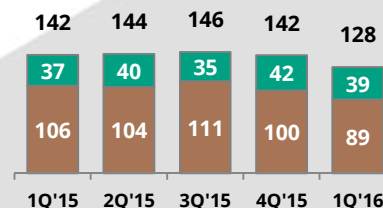
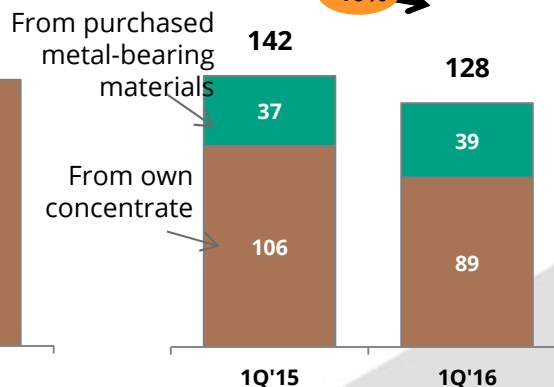
107 → 105



Electrolytic copper  
production  
(kt)

-10% →

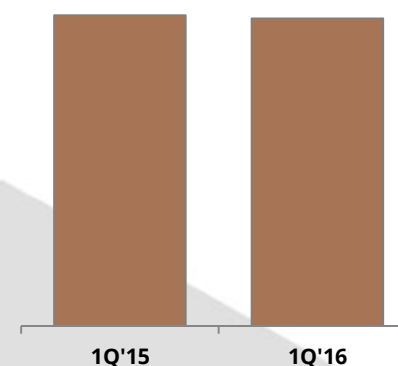
142 → 128



Metallic silver production  
(t)

-1% →

298 → 295

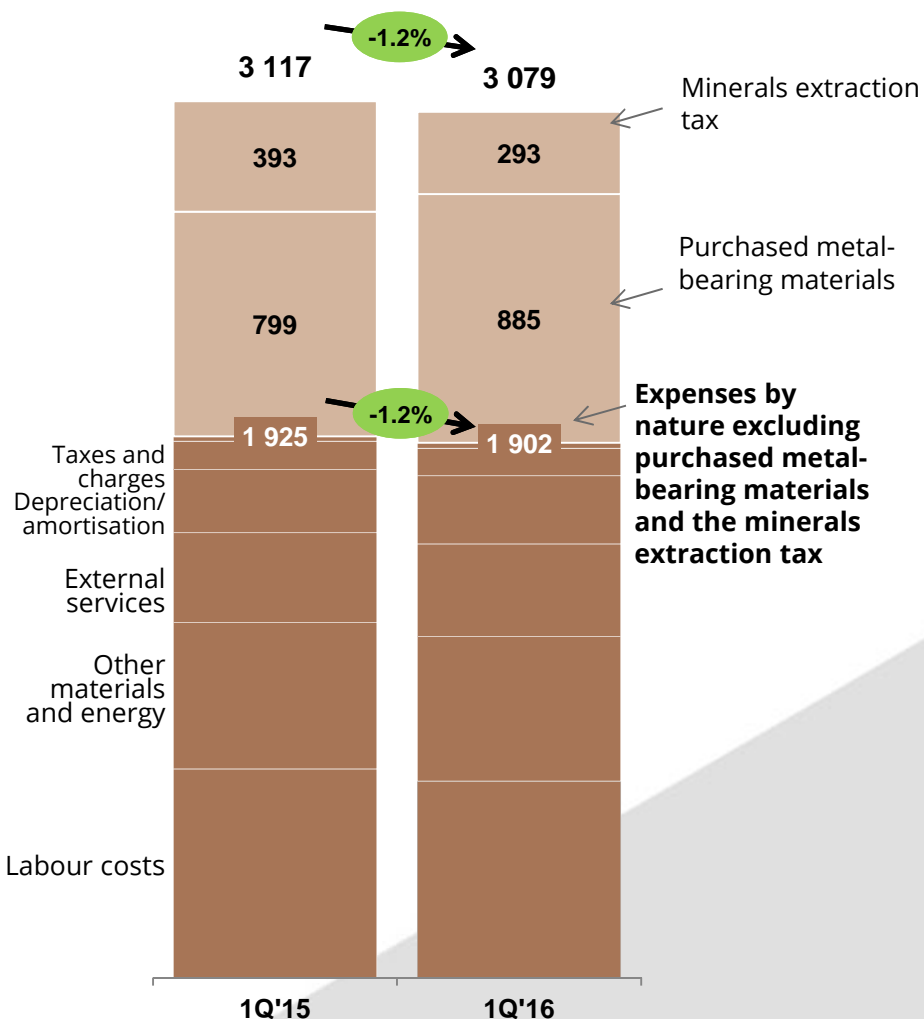


- In 2016 copper grade in ore decreased from 1.542% to 1.498%.
- The Company expects that in subsequent quarters of 2016 copper grade in ore will remain at the level of 1.51%.
- The lower amount of copper in concentrate was due to the poorer quality of ore as compared to 2015.
- Electrolytic copper production was lower due to setting aside half-finished products as inventory (20 kt Cu in the form of anodes), which will be processed in the second half of 2016 during the four-month shutdown at the Głogów I smelter/refinery.
- Silver production remained at a similar level to that in the corresponding period of 2015.

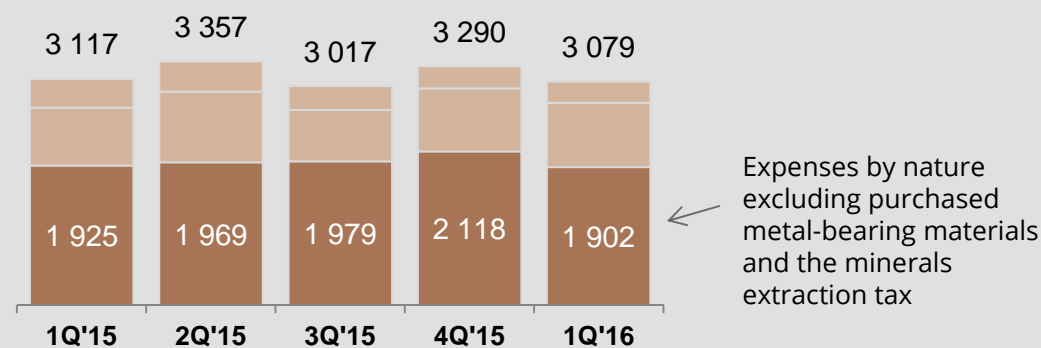


# Expenses by nature in the first quarter of 2016

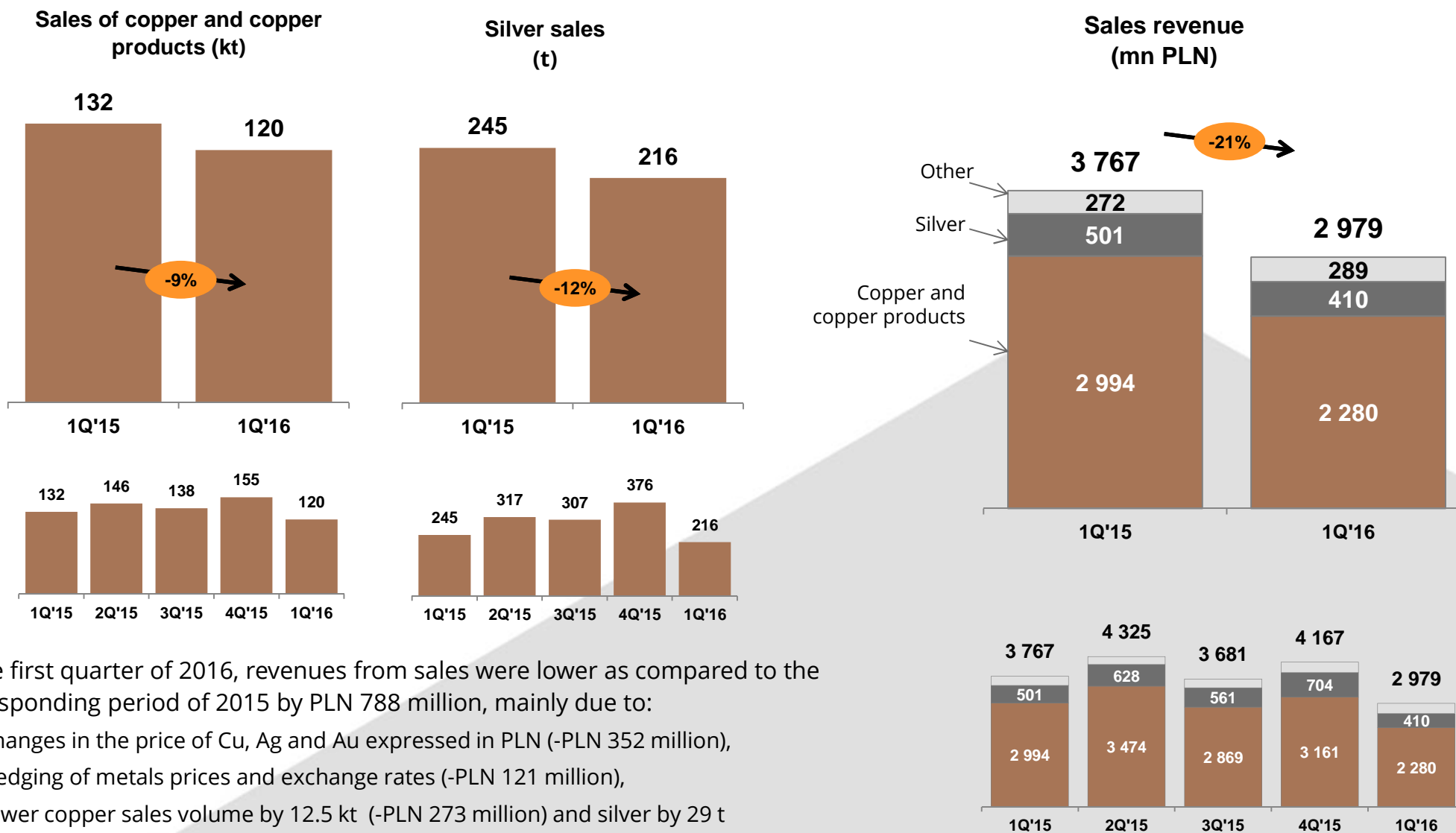
Expenses by nature  
(mn PLN)



- Total expenses by nature as compared to the first three months of 2015 were lower by PLN 38 million, alongside higher costs of consumed metal-bearing materials purchased by PLN 85 million (8 kt more copper consumed and 10% lower purchase price), alongside a lower metals extraction tax by PLN 100 million.
- After excluding the minerals extraction tax and the cost of purchased metal-bearing materials, expenses by nature were at a similar level to that of the corresponding period of 2015 and were lower by 1.2%, or PLN 23 million.

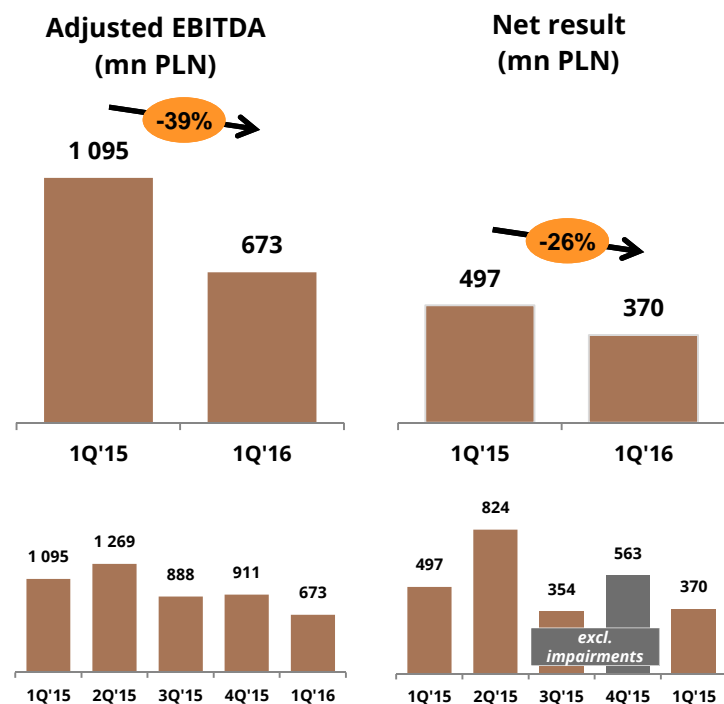


# Lower revenues from sales in the first quarter of 2016

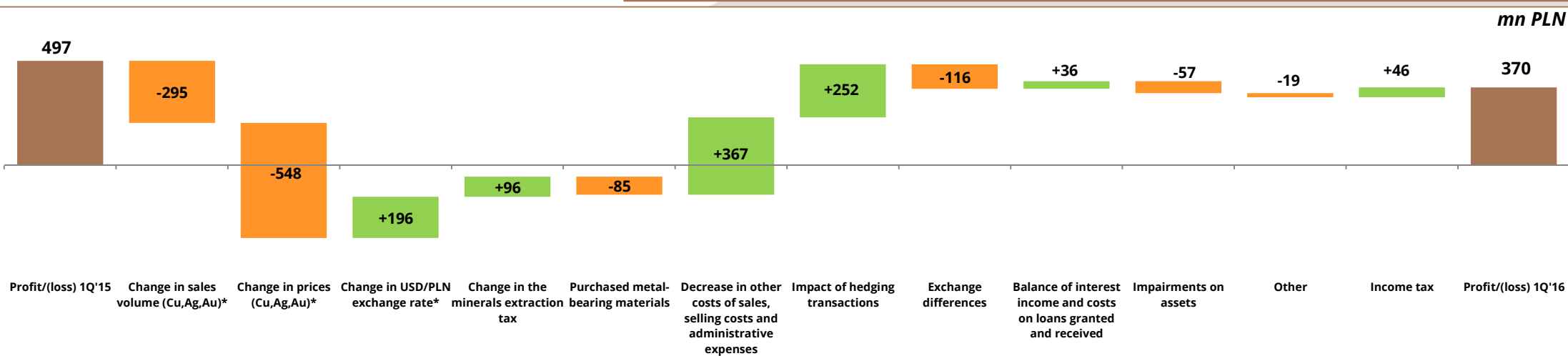


- In the first quarter of 2016, revenues from sales were lower as compared to the corresponding period of 2015 by PLN 788 million, mainly due to:
  - changes in the price of Cu, Ag and Au expressed in PLN (-PLN 352 million),
  - hedging of metals prices and exchange rates (-PLN 121 million),
  - lower copper sales volume by 12.5 kt (-PLN 273 million) and silver by 29 t (-PLN 58 million),
  - lower value of sales of other products by PLN 20 million (incl. sulphuric acid -PLN 8 million, rock salt -PLN 5 million),
- alongside the favourable impact of:
  - a higher volume of gold sales by 246 kg (+PLN 36 million).

# Financial results in the first quarter of 2016



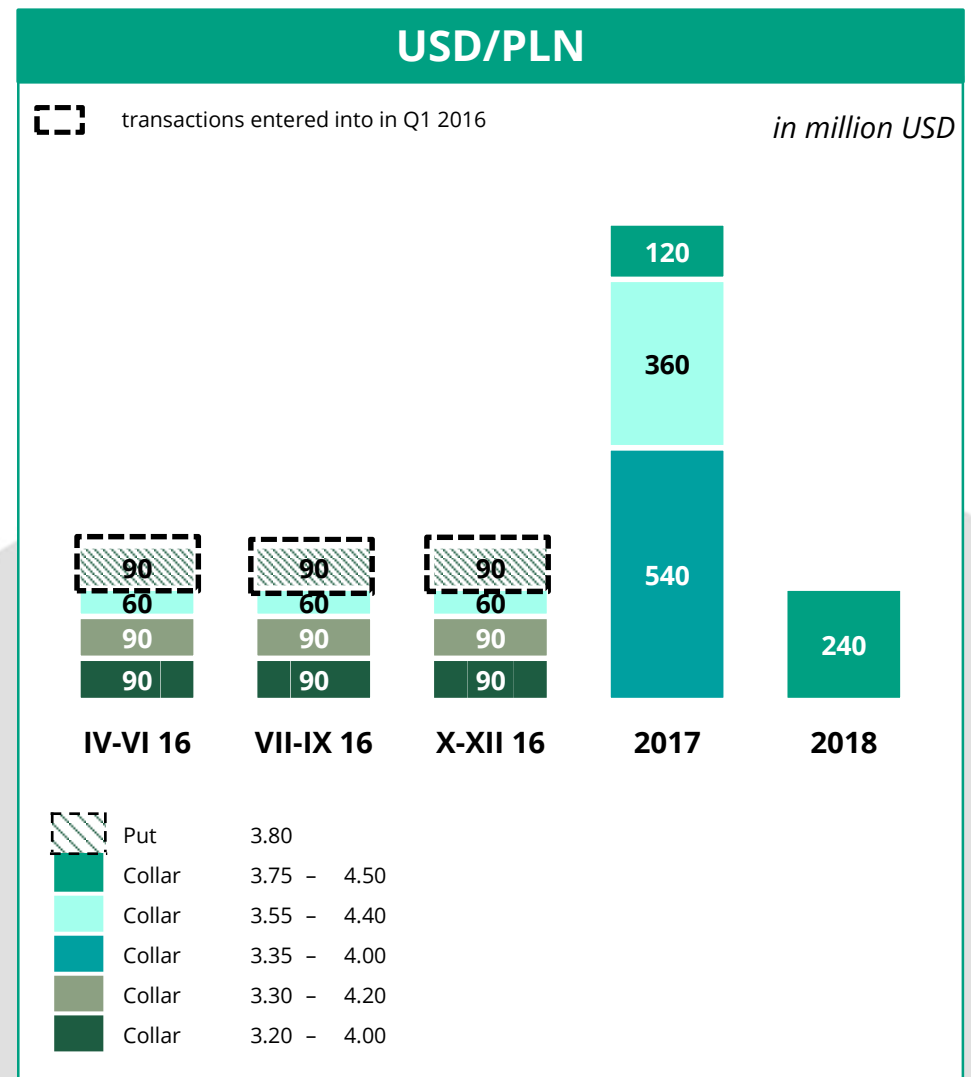
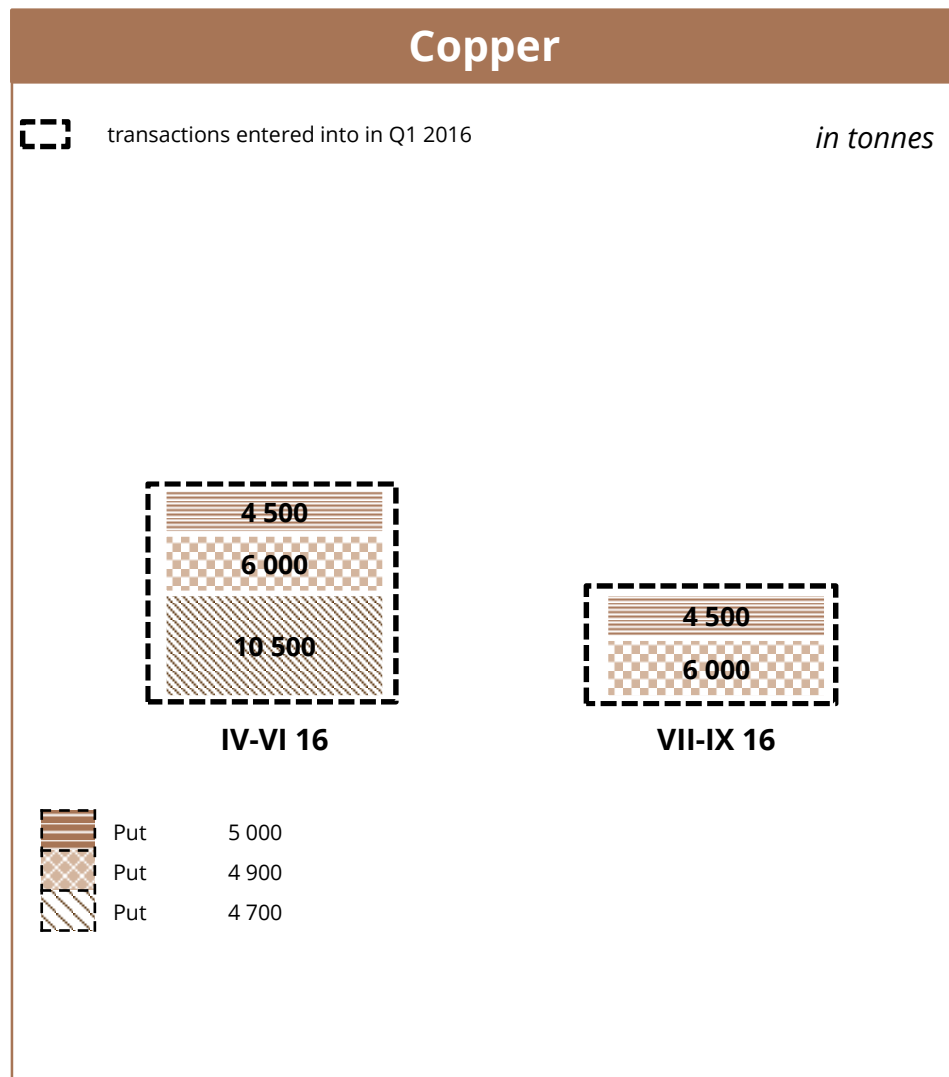
- The decrease in adjusted EBITDA by PLN 422 million (-39%) was mainly due to the deterioration in metals prices and to the lower sales volumes (due to the planned shutdown at the Głogów I smelter/refinery), and was partially offset by a weakening in the Polish zloty versus the US dollar (favourable for the company) and by a lower level of costs.
- The decrease in the result on basic activities was mitigated by hedging transactions and by a lower level of income tax – as a result the net result decreased by PLN 127 million.



# The accrued result on derivatives achieved by KGHM Polska Miedź S.A. as at 31 March 2016 amounted to PLN 118 million

## Market risk management – hedging position (as at 31 March 2016)

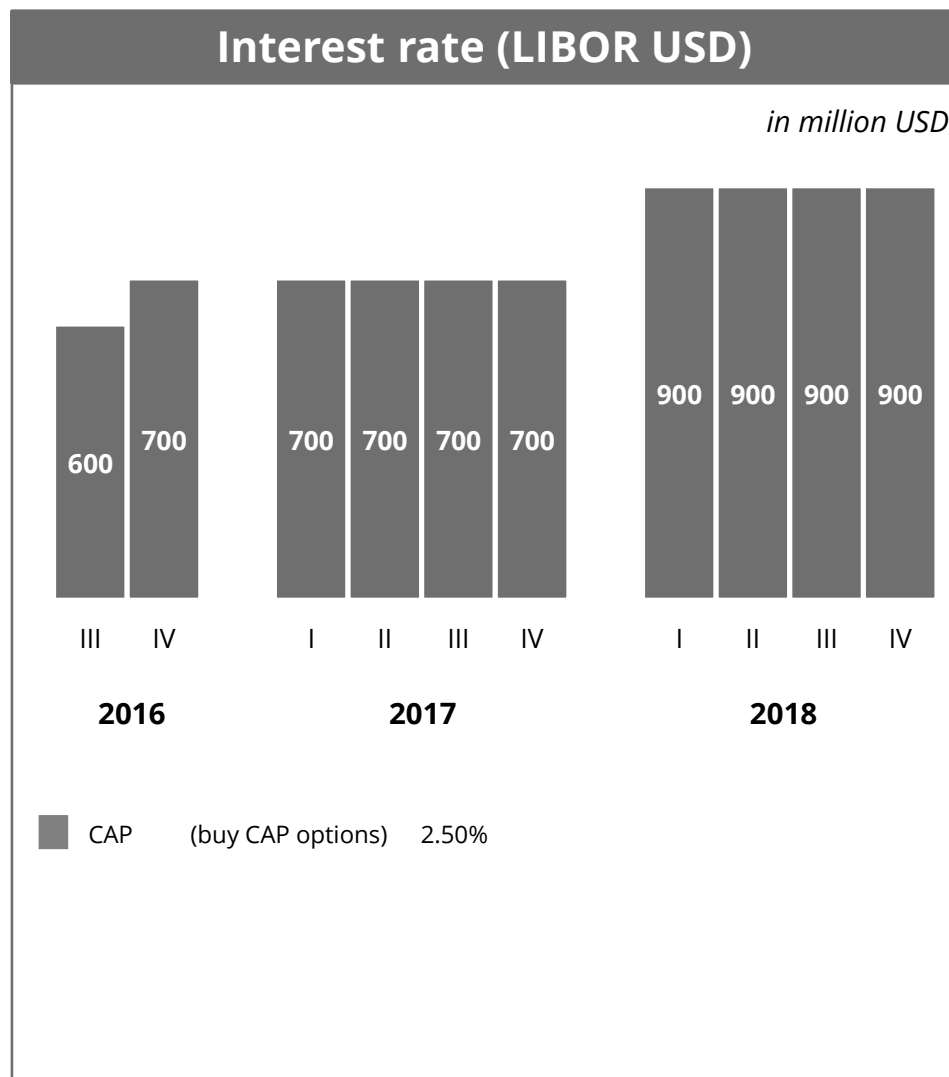
Position in derivatives on the metals and currencies markets



# The accrued result on derivatives achieved by KGHM Polska Miedź S.A. as at 31 March 2016 amounted to PLN 118 million

## Market risk management – hedging position (as at 31 March 2016)

Position in derivatives on the interest rates market



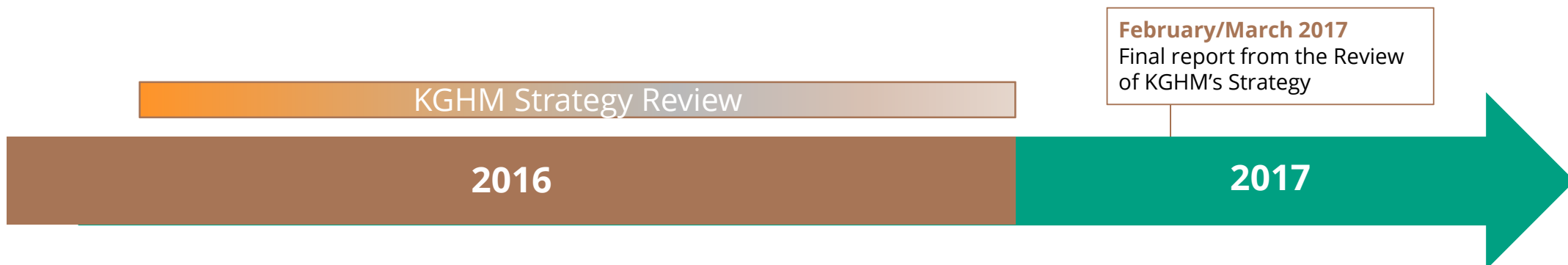
## Result on derivatives

In the period January-March 2016, KGHM Polska Miedź S.A. recorded a positive result on derivatives in the amount of PLN 118 million, of which:

- PLN 4 million decreased sales revenue (transactions settled in the January-March period),
- PLN 122 million increased the result on other operating activities (mainly a change in the measurement of open transactions as at 31 March, hedging the period to the end of 2018).
- The fair value of derivatives (MtM) in KGHM Polska Miedź S.A. as at 31 March 2016 amounted to PLN 99 million.
- The revaluation reserve on cash flow hedging instruments as at 31 March 2016 amounted to PLN 16 million.



# Review of KGHM's strategy for the years 2015 - 2020



## Review of long-term assets development assumptions

- **The Management Board of KGHM Polska Miedź S.A. has decided to undertake work on a review of the Company's strategy.** The existing „Strategy for the years 2015-2020 with an outlook to 2040” announced on 26 January 2015 must be changed due to the facts set forth below and later in the presentation.
- **The Management Board plans to conduct its strategy review over the next 9 months.** It is expected that the results of this work will be announced together with the annual results for 2016 (February – March 2017).

### 1 Macroeconomic conditions

- The actual and expected medium-term prices of key commodities for the Company are below the levels assumed in the long-term strategic plans.

### 2 Capital expenditures

- **Expenditures incurred to-date on investment projects substantially exceed the amounts assumed in initial plans.** In particular this means the actual expenditures incurred on the Sierra Gorda project as compared to the amounts foreseen in the Technical Report. This fact necessitates a review of the anticipated expenditures for the planned investment projects.
- During the process of strategy review, the Management Board will focus in particular on **adapting the company's investment plans to its anticipated financial capabilities, taking into consideration market conditions and the need to optimise costs.**

# Sierra Gorda – challenges related to achieving target financial and production parameters



## Review of the long-term plan for the Sierra Gorda mine

- During the course of operations, Sierra Gorda identified **significantly higher-than-initially-planned levels of copper oxide ore as well as clay and pyrite in the deposit's transition zone**. This fact directly limits the efficiency of processing the ore and reduces the recovery rates for copper and molybdenum during the operation period sourced from the transition zone. Possible impact on the future recovery rate is being assessed.
- **To date, the Sierra Gorda project has not yet achieved a portion of the operating and efficiency parameters set forth in the key contracts related to the project** (comprising in particular debt financing and electricity supply) to be achieved by the end of 2016. In addition to the challenges with achieving efficiency parameters, the current low metal prices are also influencing the level of generated cash flows.

### **Therefore, the following actions have been taken:**

- a review of the Life of Mine operating plan has started,
  - a more robust plan is being implemented to reduce costs and to enhance operational efficiency, and
  - discussions have been initiated to renegotiate the terms of key contracts.
- **Taking into consideration actual molybdenum and copper price levels and the current level of Sierra Gorda's operational efficiency, it is not possible at the present time to make a decision as to the commencement of Phase II.**

# Review of the long-term strategy to develop the assets of KGHM International

While the financial and economic situation of KGHM INTERNATIONAL LTD. remains stable, the **actual level of operating cash flow is insufficient to enable it to independently** (without the support of KGHM Polska Miedź S.A.) **advance the projects Ajax, Victoria and Sierra Gorda Oxide. KGHM International is also unable to independently acquire external financing from the market.** Moreover, it has become necessary to review the profitability of individual projects given current market conditions:

Robinson



- Determination of the optimal life-of-mine for the Robinson mine.

Ajax



- Analysis of the risk of substantially higher capital expenditures in respect of the Ajax project as compared to the amounts initially anticipated, given the review of the feasibility study which is currently underway on this project.

Victoria



- Review of the technical assumptions and risks related to the Victoria project due to the low level of recognition of the orebody (in the category Inferred).



**Thank you for your attention!**

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