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TCK.B.TO - Q1 2018 Teck Resources Ltd Earnings Call

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OVERVIEW:

Co. reported 1Q18 revenues of CAD3.1b and adjusted profit attributable to shareholders of CAD753m or CAD1.31 per share.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Teck’s 2018 Earnings Call. (Operator Instructions) This conference call is being recorded on Tuesday, April 24, 2018.

I would now like to turn this conference call over to Fraser Phillips, Senior Vice President, Investor Relations and Strategic Analysis. Please go ahead, sir.

H. Fraser Phillips - *Teck Resources Limited - SVP of IR & Strategic Analysis*

Thanks very much, Brenda. Good morning, everyone, and thank you for joining us for Teck's First Quarter 2018 Results Conference Call.

Before we begin, I'd like to draw your attention to the forward-looking information on Slide 2. This presentation contains forward looking statements regarding our business. However, various risks and uncertainties may cause actual results to vary. Teck does not assume the obligation to update any forward-looking statement. With that, I'd like to turn the call over

With that, I'd like to turn the call over to Don Lindsay, our President and CEO.

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Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Thank you, Fraser. Good morning, everyone…I'll begin on slide 3 with some highlights from our first quarter, followed by Ron Millos, our CFO, who will provide additional colour on our financial results. We will conclude with a Q&A session, where Ron and I and additional members of our senior management team would be happy to answer any questions.

But before we get into the highlights of the quarter, I would like to note that very sadly, there was a tragic incident at our Fording River operation on April 9th, resulting in the death of an employee of a contract company. We extend our deepest sympathies to the employee's family and friends and colleagues, and a full investigation into this incident is underway to ensure we can do everything we can in order to prevent a reoccurrence.

Turning now to our Q1 results, prices for our key commodities remained strong in Q1, resulting in another good quarter for us. Note that copper prices reached a four-year high in January at US$3.27 per pound, and zinc prices reached a ten-year high in February at US$1.64 per pound.

Sales volumes for all of our principal products increased from a year ago, particularly copper sales, which reflected a higher-than-expected grades at Highland Valley.

Overall, our operations performed well in Q1, and we're pleased that Fort Hills achieved first oil on January 27th and is ramping up to full capacity as expected. In fact, the plant's startup has exceeded expectations with respect to both production volumes and product quality, and we also achieved first sales in Q1.

We continue to return cash to shareholders, repurchasing $58 million of Class B shares to complete the remainder of our $230 million share buyback. We also paid our regular base quarterly dividend of $0.05 per share, which totaled $29 million.

The Prefeasibility Study for NuevaUnión was completed in Q1 and we have included a summary of the results in our press release. I will come back to this shortly.

In April, we acquired an additional 13.5% indirect interest in the QB2 project, through the purchase of IMSA, our minority partner. This simplifies the ownership and capital structure of QB2 and gives us flexibility on financing options for the project. We now have a 90% equity interest and a 100% funding interest in QB2.

The Board will decide on our ultimate ownership level in the QB2 project in due course. There is no fixed deadline for that decision, and in principle, we could commence construction before seeking a partner.

In the meantime, we are continuing to build cash on our balance sheet and progress engineering in preparation for a sanction decision, reducing both funding and execution risk.

Turning to our financial results for Q1 on slide 4.

Revenues were $3.1 billion and gross profit before depreciation and amortization was $1.7 billion. After adjusting for unusual items, Adjusted EBITDA was $1.6 billion.

Bottom line adjusted profit attributable to shareholders was $753 million, or $1.31 per share. That is a decent increase from $655 million, or $1.13 per share in the same quarter last year.

Details of the quarter's earnings adjustments are on slide 5. As you can see, they were minimal in Q1 2018.

I'll move on to Slide 6, where I will now run through highlights by business unit, starting with Steelmaking Coal

We continued to experience logistical issues at Westshore Terminals, particularly the lack of reliability and consistency in vessel loading and unloading of Teck trains.

As a result, sales volumes were lower than expected in Q1. Importantly, demand remains strong. We had orders from customers in place to comfortably exceed our original sales guidance range of 6.3 to 6.5 million tonnes.

Production volumes were also affected by the ongoing poor performance at Westshore, as clean coal stockpiles at mines built up to levels that forced some plants to idle due to a lack of storage capacity.

In addition, operating costs were negatively impacted by an increase in rail fuel surcharges and additional demurrage costs that were primarily attributable to the issues at Westshore.

We are working closely with all of our logistics suppliers to address these issues.

We had returned to a more typical product mix in Q1. However, our average realized price reflects the record spread between hard coking coal pricing and lower grade products.

Looking forward to Q2, steelmaking coal sales are expected to be around 6.7 million tonnes, subject to performance of our logistics chain.

We are accelerating planned upgrades to the Neptune Bulk Terminals facility, and now expect 2018 spending of approximately $120 million. The upgrade program includes an additional approximately $220 million to be spent in 2019 and 2020. Final board approval for the project is expected later in the second quarter. The investment aims to secure a long-term, reliable and globally competitive supply chain solution for our steelmaking coal business.

Before moving on, I'd like to emphasize again, as I did at our recent Investor & Analyst Day the outperformance of steelmaking coal prices relative to expectations and the significant gap between what the equity market is assuming and historical average steelmaking coal prices and the cash that we have actually received.

Over the past 18 months, steelmaking coal prices have exceeded market expectations, and they continue to do so. The current spot price is close to the average of the past 10 years of US$197 per tonne on an inflation-adjusted basis. That compares to long-term prices in the range of US$120 to US$140 that many market participants are still assuming. At current spot prices, we're actually receiving in Canadian dollars around $230 per tonne in cash.

Two recent transactions involving steelmaking coal assets provide more evidence of a gap. The prices paid imply valuations that are materially above current public market valuations. Reports suggest these transactions assumed long-term prices of US$150 to US$175 per tonne, not far off the average of the past 10 years.

Our Zinc business unit results are summarized on slide 7. As a reminder, Antamina's zinc-related financial results are reported in our copper business unit.

In Q1, contained zinc sales at Red Dog were slightly ahead of our guidance, and are indicative of the ongoing tightness in the zinc concentrate market.

Red Dog production was negatively affected by severe winter weather in Q1 but plans are in place to recover the shortfall in the remainder of the year.

Red Dog's unit cash costs after by-product credits were above our annual guidance consistent with normal seasonality.

Overall, gross profit before depreciation and amortization was up 42%, or $87 million, from Q1 2017.

Looking forward to Q2, we expect Red Dog contained zinc sales to be around 80 thousand tonnes.

Our Copper business unit results are summarized on slide 8. Overall in Q1, gross profit before depreciation and amortization was up $220 million from the same quarter last year, reflecting higher prices and volumes, and lower costs. Our average realized price was up US$0.49 per pound in the same period.

Higher than expected grades at Highland Valley persisted through the first quarter, contributing to higher production and sales and lower unit costs. We continue to expect higher annual average grades and production in 2018 versus 2017, but we do not expect the high grades in Q1 to be repeated in the remainder of the year.

Net cash costs after by-product credits were down US$0.40 per pound from the Q1 last year, helped by strong cash credits for by-products.

As I mentioned earlier, we acquired an additional 13.5% indirect interest in the QB2 project in April. We continue to expect EIA approval in the second quarter, and a potential sanctioning decision in the second half of 2018. In the meantime, we are advancing execution and operational readiness on the project, and detailed engineering is around 60% complete.

Please note that we have updated our capex guidance for QB2 from approximately US$100 million for the four months from January to April to approximately US$250 million for the nine months from January to September.

Our Energy business unit results are summarized on Slide 9. As I mentioned earlier, Fort Hills achieved first oil on January 27, and the plant startup has exceeded expectations with respect to both production volumes and product quality.

The first of three trains from secondary extraction has achieved production rates significantly above the design production rate for a single train. The second train started up on March 23rd.

By the end of March, Fort Hills was producing over 100,000 barrels per day of PFT bitumen.

Our share of Fort Hills first quarter production was 1.1 million barrels, including froth used for commissioning.

We also achieved first sales in Q1, and downstream logistics have performed as expected.

Looking forward, we expect to reach commercial production in Q2, and full production by year end.

Before I turn it over to Ron, I would like to spend a couple of minutes on NuevaUnión's Prefeasibility Study, which was completed with our 50% partner, Goldcorp, in Q1.

The Prefeasibility study incorporates key design changes to improve project economics and responds to community and Indigenous peoples input. The new design has reduced environmental footprint, infrastructure requirements and energy and water use. It plans for the use of desalinated water during operations, to protect freshwater resources. We also plan to relocate the tailings facility to the Relincho site in response to feedback from local communities.

We have extended mine life from 32 to 36 years, excluding 205 million tonnes of inferred resources contained within the current pit designs; It also has significant further resource expansion potential and project optimization opportunities.

The Prefeasibility Study contemplates a phased development approach that reduces initial capital investment and execution risk. In Phase 1, we will mine the higher-grade portions of Relincho. This will allow the project to help fund the link to La Fortuna in Phase 2, which will also focus on higher grade areas, providing significant cash flows in the early years of this phase.

As a result, average annual production is estimated to be 224 thousand tonnes of copper, 269 thousand ounces of gold and 1,700 tonnes of molybdenum in concentrate for the first full five years of mine life. That's approximately 283 thousand tonnes per year of copper equivalent production over the first full 5 years of mine life.

C1 cash costs are expected to be low in the first phases of development; Average C1 cash costs are estimated to be US$0.71 per pound payable copper for the first full five years of production, helped by high initial gold and copper grades at La Fortuna.

The initial capital cost for Phase 1 is estimated at US$3.4 to US$3.5 billion, on a 100% basis, excluding working capital and interest during construction.

Overall, NuevaUnión is a long life asset that can operate through multiple price cycles;

And with that, I will pass it over to Ron for some comments on the financial side.

Ronald A. Millos - *Teck Resources Limited - Senior VP of Finance & CFO*

Thanks, Don. I'll start with liquidity on Slide 11, where we currently have approximately $5.1 billion in liquidity. And that includes $1.3 billion in cash in our undrawn US$ 3 billion committed credit facility.

We also expect to receive an additional $1.2 billion in cash proceeds from the Waneta transaction, which is progressing and is expected to close in the third quarter of this year.

We have $220 million of debt maturities prior to 2022 and including the Waneta transaction, our strong credit metrics compare favorably to our diversified and North American peers on a pro forma basis.

And you may have seen on April 18th, Moody's upgraded our credit rating one notch to Ba1 with a stable outlook, so all 3 of the major rating agencies now have us one notch below investment grade.

Moving forward to Slide 12. We have a strong record of returns to shareholders with $4.1 billion in dividend and $1.2 billion in share buybacks since 2003. And approximately 35% of our free cash flow has returned to shareholders over the past 15 years through the dividends and the buybacks.

And in the first quarter, we spent $58 million completing the $230 million of share buybacks that was authorized by our board in November last year. And we also paid our regular quarterly base dividend of $0.05 per share. And on an annualized basis, our regular base dividend is $0.20 per share, and our board is expected to consider a supplemental dividend in the fourth quarter of each year.

On Slide 13, I'll summarize the changes in cash. During the quarter, we generated $1.1 billion in cash flow from operations. We spent $460 million on capital projects, including Fort Hills. Capitalized stripping costs were $197 million, and we paid $129 million in interest and finance charges. And as I just mentioned, we repurchased $58 million Class B shares, and that completed the buyback that we announced in Q4 last year. We also repaid US$22 million on our 2.5% notes that matured in February. And in addition, we paid out $29 million for the regular quarterly base dividend of $0.05 per share.

And after these and other minor items, we ended the quarter with cash and short-term investments of around $1.2 billion.

And with that, I'll turn it back to Don for his closing comments.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Thanks, Ron. 2018 and 2019 promises to be an exciting time for Teck. We have a number of catalysts or valuation milestones that are coming over the next 24 months, and these are detailed on Slide 14.

We have completed the prefeasibility study for NuevaUnión in Q1 and have now published a summary of those results.

The next key valuation milestones are as follows.

First, the startup of train 3 in secondary extraction at Fort Hills and hitting commercial production in Q2. We expect full production at Fort Hills by the end of the year, if not before.

We have anticipate receiving the QB2 permit in this quarter and sanctioning could occur in the second half of 2018.

We expect to close the Veneto Dam sale and receive the initial $1.2 billion in cash in Q3.

And in Q4, we aim to complete the feasibility study at Zafranal and Peru submit the SEIA year.

So we have lots to look forward to for the balance of this year.

And finally, to close, I would like to wrap up with our value proposition shown on Slide 5.

Teck remains focused on strong execution. We have premier operating assets, a proven track record of execution, and we are enhancing profitability at our operations.

We have a solid financial position, with significant liquidity and strong operating cash flow. We are in the right commodities at the right time.

Our approach to capital allocation balances returning capital to shareholders and capital spending with prudent balance sheet management.

Overall, we are focused on generating shareholder value, and we believe that Teck offers a compelling value proposition to investors.

And with that, we would be happy to answer your questions. And please note that some of our management team members are calling in from different locations, so there may be a brief pause after you ask your question while we sort out who is where.

Back to you, operator.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question is from Lucas Pipes of B. Riley FBR.

Lucas Nathaniel Pipes *B. Riley FBR, Inc., Research Division - Senior VP & Equity Analyst*

Ted Beachley here for Lucas Pipes. My first question is, how do you guys expect coal production cost will progress over the course of 2018?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Okay. For that, I'll turn it to Robin Sheremeta.

Robin B. Sheremeta - *Teck Resources Limited - SVP of Coal*

Well, the costs, and I discussed this at the Investor and Analyst Day, they're going to be roughly in line with our guidance. So little higher than last year with a higher strip ratio, slightly longer haul distance and some of the maintenance cost we had talked about. So pretty flat through the year. We're up a little in Q1, so looking forward to roughly the same costs through the end of the year.

Lucas Nathaniel Pipes *B. Riley FBR, Inc., Research Division - Senior VP & Equity Analyst*

Okay, great. And can you give us any more detail on why that cost realizations were US$207 in the first quarter, and what may have contributed to the lower realizations?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Over to Réal Foley.

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

Thanks, Ted. So we mentioned at the Investor and Analyst Day, the main reason is the record spread that we've seen between the high-grade hard coking coal and the other lower-grade products. So for instance, if you look at hard coking coal versus semi-hard, that spread was around US$50 in Q1 compared to around US$10, historical. And if you compare the hard coking coal to the semi-soft, the spread was around US$110 versus around US$30, historical. So if the spreads would've been comparable to historical, we would have achieved similar realized price as our historical levels.

Operator

The next question is from Curt Woodworth of Crédit Suisse.

Curtis Rogers Woodworth - *Crédit Suisse AG, Research Division - Director & Senior Analyst*

I was wondering if you can discuss the consistency of your volume of coking coal into China, and how much of that would be base load or visible on the quarterly basis? I just ask because when you look at the import data, it's fairly consistent quarter-to-quarter, despite fairly wide variance.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

So we missed the last part of the question.

Curtis Rogers Woodworth - *Crédit Suisse AG, Research Division - Director & Senior Analyst*

So question is consistency or visibility of your coking coal volume into China, and how affected, I guess, is the demand you see for that in relationship to the arbitrage.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Over to Réal Foley.

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

So Curt, if you look at our historical sales distribution, we sold as much as around 30% of our sales to China, going back to 2014. Currently, in 2017, we sold about half of that. So around 15%-or-so of our sales have gone to China. The demand in China continues to be strong. However, demand is also strong in other market areas. So what we've tried to do is allocate our available products to all the growth markets around the world. So that includes India, where we've doubled our sales from around 5% in 2014 to 10% in 2017. We've also increased sales to Eastern Europe, as some Eastern European mines are getting depleted and producing at lower levels. So we've increased those sales from around 15% to 20% in 2017. And we've continued to support our long-term customers in the Asian market plus developing new customers in Southeast Asia. So that -- does that answer your question?

Curtis Rogers Woodworth - *Crédit Suisse AG, Research Division - Director & Senior Analyst*

Yes. I guess, I'm trying to understand some of the structural need for high-quality met into China. And I guess, the question would be, is the China buy for you just sporadic, on the arbitrage level? Or is the volumes you're selling into China a fairly consistent baseload supply, where you're selling to the same mills over a period of time? But kind of the structural component of that business for you, if that makes sense?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

Yes. So to answer the first part of your question. Over 2/3 of large steel mills are located on the coast. So those steel mills do rely on seaborne-imported, high-quality hard coking coal. In terms of our business, we have a number of established customers to whom we supply to, pretty stable over the years. So those sales have not changed. What is changed is, some of the customers we have developed were maybe more on a spot basis. We've developed new demand in other markets. For instance, India demand is growing very quickly. So we have increased our sales to the India market. And as I said earlier, we've also increased sales to European steel mills and to Southeast Asian customers. So we're basically reallocating, depending on where we see long term demand for coking coal.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Yes, I might just add an overview comment. Going back 4, 5 years when our coal sales to China peaked, as Real said, over 30%. We actually hit 8 million tonnes in 1 year. We concluded that since anybody in the commodity business is always subject to Chinese price risk, since China's the incremental buyer of almost everything and selling at good price, we didn't also want to be exposed to too much Chinese commercial risk or volume risk. And so we made a deliberate decision to cut our sales from that peak level in half, and we're now even below that. So we're at a much smaller level now. We're much comfortable with it. And even though sales are to core customers, as Real's described, that we've had relationship with quite some time now. So it's a much more stable part of our sales book. And we've diversified even further, so we like having the risk spread amongst different countries, different customers. It's just better diversification.

Operator

Your next question is from Greg Barnes of TD Securities.

Greg Barnes - *TD Securities Equity Research - MD and Head of Mining Research*

Yes, just wanted to follow up on the increase in CapEx for QB2 for the first 9 months of the year, US$ 250 million. What is the spend going to be on, the increase spend?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Yes, Dale Andres.

Dale E. Andres - *Teck Resources Limited - SVP of Base Metals*

Yes. Thanks, Greg. For the first 9 months and leading up to potential sanction decision in second half of 2018, we're really focused on advancing, for one, getting the permit. We still expect that to be in the second quarter, in this current quarter. But still advancing detailed engineering. As part of advancing that detailed engineering, we do need to enter into contracts mainly for vendor information. And there's some costs associated with that. But primarily, it's getting ready for execution, both on construction and operational readiness basis. So we've got the teams working hard. And it's progressing well.

Greg Barnes - *TD Securities Equity Research - MD and Head of Mining Research*

Are you actually doing any physical work on the ground there?

Dale E. Andres - *Teck Resources Limited - SVP of Base Metals*

There's a minor amount of work, refurbishing some old camps up on side. But outside of that, no, we're waiting for the EIA approval.

Greg Barnes - *TD Securities Equity Research - MD and Head of Mining Research*

Okay. And Don, I know you said you're going to provide more details on the way you're doing the economics when you come out with the feasibility study. But can you give us some ballpark numbers around, I know you hate it, IRR and other metrics like that?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

I think we're going to leave that to the analysts and investment community who choose their own commodity prices and exchange rates. And we see a lot more to be done from this point of prefeasibility publication through feasibility in terms of optimizing the project, and numbers like that would soon become kind of academic. So we're leaving it to you guys for that to make those assumptions.

Greg Barnes - *TD Securities Equity Research - MD and Head of Mining Research*

So other than high-pressure grinding rolls, what other things can you do to optimize the project?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Oh, you've got to see those conveyors. Dale or Alex, you want to talk about this? This is so cool.

Alex Christopher - *Teck Resources Limited – SVP, Exploration, Project and Technical Services*

Yes, I guess, there's 2 or 3 things that we're working on here. Certainly, the high-pressure grinding rolls is a substantial difference in terms of our operating costs. So that's certainly one thing. And that's, right now, inside the PFS, and we're working on our engineering on that. We have the hybrid conveyors that were in Phase 2 that are going to be moving the crushed ore from La Fortuna down to the Relincho site in a combination of both on-the-ground conveyers and suspended conveyers. And essentially, we're there. We're going to be a positive in terms of energy consumption in that. So essentially, we're going to be producing energy from those conveyors. So that's certainly something that's going to impact growth. So we're working on several other engineering opportunities, including things like some of our autonomous haul truck assessments and certainly looking at some of our recoveries and potential at La Fortuna. So got quite a number of things on the opportunity list here that we're working on both between PFS and feasibility, as well as within the prefeasibility study itself.

Greg Barnes - *TD Securities Equity Research - MD and Head of Mining Research*

So the HPG and the conveyors were not included in the prefeasibility? Or you're optimizing in the prefeasibility?

Alex Christopher - *Teck Resources Limited – SVP, Exploration, Project and Technical Services*

They are included in the prefeasibilty, but we'll be optimizing in the feasibility.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

I should remind just people the timeline in this that we now, after bit of a pause, we'll move to feasibility, which takes about a year. And we wouldn't file the SEIA until December, I think, as a target. Just looking to confirm that.

Dale E. Andres *Teck Resources Limited - SVP of Base Metals*

Yes. Sometime between preparation of the feasibility study. So at the very earliest, would be the end of this year and -- but sometime before we anticipate to finish the feasibility study, which would be mid-2019.

Greg Barnes - *TD Securities Equity Research - MD and Head of Mining Research*

That's when you apply for the EIA?

Dale E. Andres *Teck Resources Limited - SVP of Base Metals*

Exactly.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

So it's a good couple of years before there's any significant capital decisions.

Operator

The next question is from Chris Terry of Deutsche Bank.

Christopher Michael Terry - *Deutsche Bank AG, Research Division - Research Analyst*

Don, yes, couple of questions from me. On the CapEx, just following up from Greg's question there, can you talk a little bit about Neptune and the timing on decision and the CapEx there? I know you talked about it a little bit at the Investor Day. Just wanted to get your latest thoughts on that. And then with QB2, as we head out to 2019, can you give some sort of indication on the ramp-up of how CapEx might look? I don't want to jump to conclusions that you plan to go ahead with it. But just trying to get, conceptually, an idea of what the CapEx delta above the sustaining model look like into the next year or so. That's my first question. I'll ask you another in a minute.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Okay. So on the Neptune question, we will be accelerating the program there. And we'll now spend approximately $120 million this year versus the $85 million we had disclosed before. And we expect the board to approve, very soon, the $220 million from here to complete the project. So I think that's that. And on the QB2, who wants to take that one? The ramp up of capital? Is that the question, like, once it's sanctioned?

Christopher Michael Terry - *Deutsche Bank AG, Research Division - Research Analyst*

Yes. I mean, given the updated guidance for this year, I guess, on what you're going to spend on the pre-sanctioned numbers, I assume. And then if that was to be approved, just what we could expect to get into late, late '18 and then into '19? Just a rough trajectory on how the spending might look into those years.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

So we have those numbers, but we may not have them right here. We'll either come back to you at the end of this call or get back to you directly. Okay?

Ronald A. Millos *Teck Resources Limited - Senior VP of Finance & CFO*

We did give the capital spend growth profile. We published the feasibility results in Q1 2017. And I need to pull those direct numbers back and back a number on that.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

They're in the public domain, but we'll find them and get back to you.

Christopher Michael Terry - *Deutsche Bank AG, Research Division - Research Analyst*

Okay, okay, sure. And then the other one's on coal. You talked a bit about what happened in 1Q, but given we're quite away now through 2Q and the lag on the process, how do we think about the likely realized price for 2Q, specifically?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Réal hates questions like that in the third week of April.

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

So we're about -- we're a bit more than halfway through the quarter, Chris. So the lag indexed-linked price for the quarter is still sitting above US$205 today. It's a bit tough to say what will happen to the spot prices for the rest of the quarter. This morning, it's a bit over US$177. So it's corrected over US$15 since the beginning of April. In terms of demand, the demand is still strong across all market areas, whether it's China or the rest of the world. So we see customers continuing to take coal on a ratable basis. And then on the supply side, there's still issues, whether it's logistics or production disruption. So overall, we still see the market as being tight. It's just difficult to see where exactly the spot prices may end up by the end of the quarter.

Christopher Michael Terry - *Deutsche Bank AG, Research Division - Research Analyst*

Okay. And maybe just on the realized price versus the indexed price. Just on, I think, it was 87-odd percent last quarter. Do you think that, that comes up for this quarter a bit more towards the historical average, or where would you see that?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

Yes. We're no longer going to give guidance on realized prices, Chris, because it's just been too volatile. If you look at our history from Q2 of 2010 until now, it has ranged from 75% to 104% of the assessments. And that's a function of price spreads as we've seen in this past quarter. But it's also timing of sales. It's directional, the spot market, which can change at any time during the quarter. It's timing of vessel arrivals, product mix. So there is a lot of different variables that come into play

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Yes. One other problem, Chris, was that if we gave out a percent, and people would use that for the balance of the quarter when, in fact, it was only good for that hour. And now particularly, as we've seen in other product qualities, the spreads, as Real's talked about, can be quite volatile. So we're encouraging analysts on The Street to follow the trade journals that publish not just the index link, sort of, rolling 3-month average for hard coking coal, but also to look at the spreads for the semi-hard and semi-soft and PCI and come up with your own estimate for the quarter.

Operator

The next question is from Orest Wowkodaw of Scotiabank.

Orest Wowkodaw - *Scotiabank Global Banking and Markets, Research Division - Senior Equity Research Analyst of Base Metals*

Just, actually, a follow-on from the previous question. Two things: one, are you seeing, I mean, the spot price falling for coal in the last couple of weeks, are you seeing any of your spot customers pull back orders in anticipation of continuation in spot pricing? I'm curious how that will impact your realizations for the quarter. And then secondly as well, can you give us an idea, is there a big difference in your coal quality mix, say, in the second quarter from what we saw in the first quarter? Or is this here pretty similar on a quarterly basis from a mixed perspective?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

Okay. So maybe starting with the second question, Orest. So our product mix is back to normal since Q1. So in Q4 last year, we had a higher proportion of thermal sales, as we've indicated when we reported our Q4 results. But now we're back to around 75% of our production as hard coking coal, and the remaining 25% is semi-hard, semi-soft, PCI. Thermal is typically couple percentage points. Now that can vary quarter-to-quarter, as I answered on the previous question. I mean, there are releases that can impact that. But overall for 2018, we're expecting around 75% of our production to be high quality hard coking coal. To the first question on the spot price, as steel pricing and steel demand remain strong in the world, we're seeing regular demand in the market. It's a little bit different from what we had seen in the past, whereby there was a massive pullout for the market when there was a big price correction following Cyclone Debbie last year. So you'll recall that at that time, spot prices had reached over US$300, and they corrected to somewhere around the US$140, US$150 level. So it was a massive pullback. This time, the pullback is smaller and as steel demand is good and steel pricing is good, steel producers still require the hard coking coal to produce.

Orest Wowkodaw - *Scotiabank Global Banking and Markets, Research Division - Senior Equity Research Analyst of Base Metals*

Okay. So it sounds like you're saying that from a realization perspective, we shouldn't see a repeat of what we saw the last time coal pricing really declined on a spot basis.

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

Yes, I guess, you need to look at the spreads. And it will be impacted by the various other factors I've mentioned earlier.

Orest Wowkodaw - *Scotiabank Global Banking and Markets, Research Division - Senior Equity Research Analyst of Base Metals*

Okay. And just, again, on quality. Because of the closure, I guess, of Coal Mountain, which is supposed to increase the quality your mix, does that mean that the front end of the year is actually a weaker mix of product?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

So as we're mining into the recently permitted areas, of course, the product mix can be a little bit different. So your expectation is probably appropriate. When we look at 2018, overall, we'll be around 75% hard coking coal. It can vary quarter-to-quarter.

Orest Wowkodaw - *Scotiabank Global Banking and Markets, Research Division - Senior Equity Research Analyst of Base Metals*

And just finally, what was the actual mix in Q1 between premium hard coking coal and the rest?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

Production was pretty close to the 75% level. The main issue was actually getting the coal to market as we've indicated with the logistics issues and mainly the impact of Westshore.

Orest Wowkodaw - *Scotiabank Global Banking and Markets, Research Division - Senior Equity Research Analyst of Base Metals*

I see. And your guidance for the second quarter, 6.7 million tonnes, does that assume an improvement at Westshore? Or is that just basically a status quo?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

No, it assumes that Westshore will continue to improve. We have seen some improvements since the start of April. We've also seen improvements on the rail side. So it's subject to that continuing. The 6.7 million tonnes is based on that.

Operator

The next question is from Oscar Cabrera of CIBC Capital Markets.

Oscar M. Cabrera - *CIBC Capital Markets, Research Division - Research Analyst*

With the increased expenditures in QB2 this year, in terms of thinking of your capital structure, have you changed your priorities in terms of returning cash to shareholders? i.e. will a supplemental dividend be viewed as a priority in 2018 versus spending more capital at QB2 towards the second half of this year?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Thanks, Oscar. Nothing has changed in terms of our approach there. The board will consider the supplemental dividend and buybacks at the November board meeting, and it will be based on our outlook for the business. But based on first, how good the year was. Second the outlook for commodity prices and financial results in the coming year. And then third, the capital needs of the business going forward, including QB2. And this is April and that’s in November so lots of time between now and then. So I can't predict what they're going to do, but I suspect that if things carry on anywhere near where they are today, that we would have something similar in terms of discussion around it, as we did last year.

Oscar M. Cabrera - *CIBC Capital Markets, Research Division - Research Analyst*

Okay. And then back in 2013 or '14, I forget now, but when the price participation from coal was removed and you increased the availability from CP and CN, you provided a map of the flows of coal to the coast. It seems like, with the additional expenditure at Neptune, you're looking at going back to some of the figures. Can you remind me of what the actual capacity of Neptune and Ridley can be, and would you consider moving more out of Westshore to prevent all of these things that we're seeing here?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

So the current capacity at Neptune is 12.5 million tonnes. And as we've said, the upgrades that we're investing in will take it formally to 18.5 million tonnes. But with the upside, certainly, beyond 20 million tonnes and more. We do have volume contracts in place at Ridley, and we will see what the numbers are there. 3 million tonnes of contracts at Ridley as well. So where everything ends up, you'll have to wait, probably, till 2021 to see how that goes. But we'll certainly have more capacity.

Oscar M. Cabrera - *CIBC Capital Markets, Research Division - Research Analyst*

Right. And then just lastly, the clarification the figure that you provided for Neptune in this year, that was $220 million. If I remember correctly, the original estimate that we had back in 2014 was like $250 million. Is that still the ballpark that we should be looking at?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Not quite so. We earlier said that we had approved $85 million. We have now updated things, saying we will spend $120 million this year and we are asking the board for approval for an incremental $220 million to complete the project. And we expect to get that approval shortly. So we're accelerating our work at Neptune and those are the numbers. So if you are up the total cost to the project including what we have spent to date would be $345 million.

Operator

The next question is from Alex Hacking of Citibank.

Alex Hacking *Citi Investment Research (US) - Analyst*

I have a quick clarification on the potential CapEx profile at NuevaUnion. The US$3.6 to US$3.7 billion major enhancement CapEx, how much of this would be required to bring La Fortuna online, so to Phase 2 versus much longer dated for Phase 3?

Dale E. Andres - *Teck Resources Limited - SVP of Base Metals*

It's Dale. I'll take that. And consistent with what we've said in the release, there's US$2.6 billion to US$2.7 billion tied to Phase 2 and approximately US$1 billion tied to Phase 3, which, under the current scenario, would be probably [2028 or 2029]. So quite a bit down the road. And so leading up to Phase 2 production in year 4, it would be that US$2.6 billion to US$2.7 billion which is the connection up to the La Fortuna site and would include mining equipment and pre-stripping activities at La Fortuna.

Operator

The next question is from Ralph Profiti of Eight Capital.

Ralph Profiti *Eight Capital - Analyst*

Don, is your view of these logistical questions, if I can come back to them, more related to performance? Or are these bring to light some of the structural issues? And are you seeing potentially significant investment required by your logistics partners in order to get Teck to the desired movement of coal to where it needs to be? I'm thinking larger vessels, longer trains, stuff like that.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

The main answer to that question would be performance. Of course, in any logistical chain, it’s going to be different to where it might require a little bit of capital here and there. We know Westshore has been investing some capital in things. And CN Rail clearly has some issues that they'll be working on. But overall, I'd say, the answer to that question is that it's about performance.

Operator

The next question is from Karl Blunden of Goldman Sachs.

Karl Blunden *Goldman Sachs Asset Management (US) – Fixed Income Security Analyst*

It sounds like you have lot of a different options with regards to capital allocation coming forward. You have a lot of cash coming in the door from operations and from asset sales. And so a question I have for you is, could you refresh us on how you came up with your target for debt? It's a US$5 billion number. Now we're looking at coal market conditions that are staying tighter for longer, and some people think that, that could continue. Does a tighter coal market or more earnings power in the form of QB2 change how much corporate debt you want? And I'm thinking about this in terms of how you go ahead with financing, strategy or decision around QB2?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

I'm going to turn that over to Ron Millos. But first, I want to say, less is better. But over to you, Ron.

Ronald A. Millos - *Teck Resources Limited - Senior VP of Finance & CFO*

Yes. We lost our investment-grade credit rating a few years back, and we would like to get that back. But we are at the mercy of the rating agencies. And one of the comments they've made over the years is, they cut back the ratios. We were at sort of a 30% debt-equity and a 2.5x leverage ratio. And the debt-equity ratio is not an issue for us. The leverage ratio is a big problem for us in a low commodity price environment where we don't have the EBITA to support that. So the general view is that we needed to get our debt down, and we've done that to get it below that US$5 billion target level there. The agencies have also, sort of, reduced a little bit on the leverage ratio by about half a turn as well is the indication. To get back to investment grade, the big outstanding items that they're looking for now is a bit more clarity on what we're going to do with QB2, what the final costs are, the ownership structure and how we intend to finance QB2. We're in the process of looking at the financing options, and we're kind of riding 2 horses right now, looking at both the project financing option and whether we might go to the bond market at some point down the road.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Our ratios are well into investment-grade territory. Our CDS is well into investment-grade territory and the bonds are trading at investment-grade levels.

Karl Blunden *Goldman Sachs Asset Management (US) – Fixed Income Security Analyst*

That's very helpful. Just a quick follow-up. On the project financing, realizing it's still early days, but any complications, anything you found, as you're gone down that path. There have been other projects and efforts in the market that haven't succeeded recently. Just any color you can share there would be helpful.

Ronald A. Millos - *Teck Resources Limited - Senior VP of Finance & CFO*

Sure. We're sort of at the front end of that, and there's been nothing at this stage that's been playing that's causing us any great grief.

Operator

The next question is from Mark Levin of Seaport Global.

Mark Andrew Levin - *Seaport Global Securities LLC, Research Division - MD & Senior Analyst*

Two questions. When you think about your investment in Neptune going forward, maybe could you give us some parameters or at least the way to think about of what the potential cost savings, opportunities might be, if you were to shift more volume away from Westshore toward Neptune? And then my second question, then I'll just hang up and listen, relates to Quintette. Have you had any further thoughts around Quintette? If you were to green light QB2, does that necessarily take Quintette off of the table? Would you be willing to do two major capital projects concurrently?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Okay, on the first one, we haven't disclosed the magnitude of the potential savings, but you can expect that they would be significant. On the Quintette, we continue to look at it. We know there are customers that would be eager for us to bring it online, but it is not something that we see in the near term. And frankly, QB2 is still our priorityy for the long-term building of the company, so that's probably where we stand.

Mark Andrew Levin - *Seaport Global Securities LLC, Research Division - MD & Senior Analyst*

So last one, actually, this one is more for Real. Has there been any customers reaching out concerned about the Aurizon situation in Australia? How do you see that situation, if it stays in the way it is, meaning the draft decision turns into the final decision? What might that mean for Teck from your perspective?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

So Mark, everybody is watching what might happen with Aurizon. So far Aurizon has said that the impact could be up to 20 million tonnes, and half of that impact could be on the Goonyella line, which is the line that carries mostly high-grade hard coking coal. So it could definitely have an impact on the market from a supply point of view. We haven't seen major shifts from customers yet. But it is definitely a concern.

Operator

The last question is from Lucas Pipes of B. Riley FBR.

Lucas Nathaniel Pipes - *B. Riley FBR, Inc., Research Division - Senior VP & Equity Analyst*

I wanted to circle back to Neptune one more time, and I wanted to ask specifically, is there reasonable business case where it would not make sense to go ahead with capital at this stage?

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Given the results of Q1, I would say, no. But we're always open to consider options and, we will always be balancing any other opportunities against the current investment. But we're pretty committed and you know that they're going to be significant cost savings, but beyond that, and probably more than that is the reliability factor. It's so important in being able to ship the coal, particularly when prices are high. When you build in that factor, the modest investment in Neptune is pretty compelling. And it's really about having a long-term, reliable supply chain for various businesses. So that's how we think about it.

Lucas Nathaniel Pipes - *B. Riley FBR, Inc., Research Division - Senior VP & Equity Analyst*

That's very helpful. And maybe just to pick on you said there on the loss during the first quarter. You may have mentioned it earlier, but is it possible to quantify the loss in revenue due to the logistic issues in Q1? Or maybe just boil it down to one number, what would your realized price have been if you had shipped all the tonnes that you had demand for?

Réal Foley - *Teck Resources Limited - VP of Coal Marketing*

So Lucas, as I said earlier, if it would've been a normal quarter, in terms of volume and spreads, keep in mind that the spreads between the high-grade hard coking coal and the lower-grade materials were at record levels. So if you factor all that in, our realization would've been comparable to historical levels.

Operator

Thank you. There are no further questions registered at this time. I would now return the meeting back over to Mr. Lindsay. Please proceed, sir.

Donald R. Lindsay - *Teck Resources Limited - President, CEO & Director*

Well, thank you all for joining us this morning. We look forward to speaking to you again in July and look forward to having some of these valuation milestones or catalysts, as you like to call them, to announce in the meantime. Thanks very much, all.

Operator

Thank you. The conference has now ended. Please disconnect your lines at this time. We thank you for your participation.