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Teck Resources Ltd. (TECK)

Q3 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. Welcome to Teck Resources Q3 2018 Earnings Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. This conference call is being recorded on Thursday, October 25, 2018.

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

H. Fraser Phillips

Senior Vice President, Investor Relations and Strategic Analysis, Teck Resources Ltd.

Thanks very much, Ileana. And good morning, everyone. I'm sorry for that brief delay. We're having a little technical difficulty with some of our folks dialing-in from a remote location, but we think we've got that sorted out.

Thanks for joining us for our third quarter 2018 results conference call. Before we begin, I would like to draw your attention to the caution regarding forward-looking statements on slide two. This presentation contains forward-looking statements regarding our business. The slide describes the assumptions underlying those statements. Various risks and uncertainties may cause actual results to vary. Teck does not assume the obligation to update any forward-looking statement.

I would also like to point out that we use various non-GAAP measures in this presentation. You can find explanations and reconciliations regarding these measures in the appendix.

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

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Thank you, Fraser, and good morning, everyone. I will begin on slide three with some highlights from the third quarter followed by Ron Millos, our CFO, who will provide additional color on our financial results. We will conclude with the Q&A session as usual where Ron and I and additional members of our senior management team would be happy to answer any questions.

Turning now to Q3, we continue to advance our key growth initiative Quebrada Blanca Phase 2, and we continue to strengthen our financial position. We received regulatory approval for QB2, which is a major step forward in advancing the project. And importantly, it was a unanimous vote from Chilean authorities, which is a testament to the level of support for the project locally.

We also closed the sale of our two-thirds interest in the Waneta Dam in July, resulting in receiving \$1.2 billion in cash. And then we reduced our outstanding notes by USD 1 billion, which further strengthens our balance sheet. And all of this puts us in very good position ahead of a potential sanctioning decision on our QB2 project later this year.

In addition, we received regulatory approval to renew our normal course issuer bid or NCIB in early October, and this allows us to purchase up to 40 million Class B shares over the next one-year period. Our operations continue

to perform well, although, commodity prices for our key products did decline during third quarter, which impacted our profitability compared with the last quarter.

Fort Hills continues to ramp up towards exceeding nameplate capacity of 194,000 barrels a day and we expect full production in Q4. And as a result of our solid operating performance year-to-date, we have improved our production guidance in each of copper and zinc for 2018. And finally, we were very pleased to be named to the Dow Jones Sustainability World Index for the ninth consecutive year.

Turning to our financial results for the third quarter on slide four. Revenues were \$3.2 billion. Gross profit before depreciation and amortization was \$1.4 billion. And after adjusting for unusual items, adjusted EBITDA was \$1.2 billion. Bottom line, adjusted profit attributable to shareholders was \$466 million, or \$0.81 per share, or \$0.80 per share on a diluted basis.

I'll now run through some highlights by business units starting with steelmaking coal on slide six. Global steel production and demand for seaborne steelmaking coal remains strong. And as a result, steelmaking coal prices are continuing to outperform market expectations with a spot price at USD 217 per tonne currently and that was as of yesterday. In fact, this morning, that spot price is USD 225 a tonne.

In the third quarter, we generated significant cash flow based on a continuing solid operating performance. Customer sales were strong. We had sales orders in hand to significantly exceed our guidance of 6.8 million tonnes. However, once again, logistical issues at Westshore Terminals negatively affected our ability to deliver coal to customers. And as a result, delivery of some 250,000 tonnes was delayed into Q4 negatively impacting our revenues by about \$55 million.

Fourth quarter sales are expected to be around 6.7 million tonnes subject to the performance of our logistics chain. Production was lower in Q3 2018 than it was in Q3 2017, largely as a result of the end of mining activity at Coal Mountain. However, we are well-positioned to meet our full-year production guidance. The equipment utilization and productivities are continuing to achieve historical highs and the majority of our planned plant shutdowns are now behind us.

Operating costs increased in third quarter relative to both Q3 2017 and relative to Q2 2018. And this is due to increased use of contractors to capture additional margin in the current strong steelmaking coal price environment and inflationary pressures on consumables, particularly diesel. On top of this, in Q3 2018, costs increased due to maintenance shutdowns of two of our larger plants and also mining and higher cost areas of our pits, something that varies from quarter-to-quarter. I would note that these costs are not permanent. They're not a permanent part of our cost structure. In the current strong coal market, where we'll now be receiving almost \$300 per tonne, we are using contractors to capture incremental production that is helping to generate very strong profitability and strong cash flow.

If coal prices were to decline, we would reduce the use of contractors. The majority of our planned plant shutdowns are now behind us and we expect to move to lower cost areas of our pits in due course. But that being said, we have increased our site cost guidance for the full year to \$60 to \$63 per tonne from \$56 to \$60 per tonne due to higher use of contractors and higher diesel costs than previously anticipated.

Perhaps most importantly this quarter, we are very excited to report that we have had promising initial results for our saturated rock fill project at Elkview Operations. Saturated rock fill is a new form of water treatment resulting from our ongoing investment in water quality research and development. Our Elkview facility is achieving near complete removal of selenium and nitrate in 10 million liters of mine-infected water per day, and that number, 10

million liters, exceeds the 7.5 million liters per day design capacity of our West Line Creek active water treatment facility, and it does so at a fraction of the cost.

Saturated rock fill has the potential to augment or, in fact, even replace traditional water treatment technology for treating large volumes of mine waters at significantly reduced capital costs and significantly reduced operating costs. We are continuing to prove out the results of the Elkview facility and to work towards broader implementation of that technology. This is a very exciting long-term development.

Turning to our copper business unit. Our Q3 results are summarized on slide seven. On QB2, as I mentioned earlier, we received regulatory approval for the project during the quarter, which was based on a unanimous vote from Chilean authorities. And this is a major milestone for the project. The partnering process for QB2 is progressing very well.

We are encouraged by what we have seen so far and we continue to believe a transaction could be announced in the fourth quarter that is in this quarter. Sanctioning of the project could also occur at that time. At the same time, work is underway to further optimize the initial mine life of QB2 as well as the production rates in the early years of the operation.

And in addition, engineering studies are underway to assess the expansion potential beyond QB2 including a potential doubling of throughput capacity in the future, which we now refer to as QB3. And this will position Teck to have growth in our copper division for a long, long time to come.

Overall, in the third quarter gross profit before depreciation and amortization was up modestly from the same quarter last year. Sales were up 1,000 tonnes and strong cash credits for byproducts helped to offset a small increase in unit operating costs.

Highland Valley had lower copper grades and mill throughput as anticipated in the mine plan. Also Carmen de Andacollo set a new monthly record for mill throughput in September. And for the full-year, we now expect copper production to be in the range of 285,000 to 295,000 tonnes, compared with 270,000 to 285,000 tonnes at the start of the year. We have also lowered our corporate unit cost range to USD 1.25 to USD 1.30 per pound after byproducts compared with USD 1.35 to USD 1.45 at the start of the year.

Finally, on the technology front, our autonomous haulage pilot at Highland Valley now has two trucks fully operational in Lornex pit. And it is on track to have six trucks operational by year-end. Our zinc business units are summarized on slide eight. And as a reminder, Antamina zinc-related financial results are reported in our copper business unit. The zinc market remains tight. Reported exchange zinc inventories are at their lowest levels since 2008 and reported zinc stocks held on the LME and the Shanghai Exchange fell close to 100,000 tonnes combined during the third quarter.

In Q3, contained zinc sales for Red Dog were 9,500 tonnes lower than our guidance due to timing of sales and shipments. We expect Q4 sales for Red Dog to be 180,000 tonnes, which reflects our normal seasonal pattern. Mine zinc cash unit costs after byproducts were up USD 0.09 per pound, compared with the same period last year. And operating costs increased primarily due to high diesel costs at Red Dog.

Red Dog's concentrate shipping season is expected to be complete in late October. We expect to ship approximately 1 million tonnes of zinc concentrate and 175,000 tonnes of lead concentrate, representing all of the concentrate available to be shipped.

At Trail, refined lead production was impacted by temporary shutdown due to smoke from forest fires. On top of this, a planned major maintenance shutdown started in mid-September and is expected to continue to mid-November. These factors had a negative impact on Trail's operating costs during the quarter and Trail's operating costs were also reflecting higher electricity costs related to the sale of the Waneta Dam. Looking forward, based on our strong performance at Red Dog, we have increased our overall zinc and concentrate production to the range of 660,000 to 675,000 tonnes, compared with 645,000 to 675,000 tonnes at the start of the year.

Our energy business unit results are summarized on slide 9 and as a reminder, commercial production was achieved at Fort Hills on June 1. The planned start-up has continued to exceed expectations with respect to both production volumes and production quality. And as I mentioned earlier, Fort Hills is continuing to ramp up towards nameplate capacity. In Q3, our share of Fort Hills bitumen production was around 2.5 million barrels or around 27,400 barrels per day. And this reflects some unusually wet weather that impacted my mine production in July and planned maintenance that restricted the plant to 50% capacity in the last two weeks of September.

During the maintenance period, the mine operations focused on overburden stripping and exposing more ore to support full production in the fourth quarter. Our sales of blended bitumen were 3.1 million barrels in Q3. Looking forward, we now expect to be at the high end of our full-year production guidance range of 8.5 million to 10 million barrels of bitumen for the full-year compared with a range of 7.5 million to 9 million barrels at the start of the year.

We are also expecting to be at the high end of our operating cost guidance of \$28.50 to \$32.50 per barrel for the year this year. One final note, the Frontier Project public hearing before a federal and provincial panel, which commenced on September 25 is essentially complete before closing arguments to come in December. The earliest that we would see a federal decision statement is probably mid-2019.

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

Ronald A. Millos

Chief Financial Officer & Senior VP-Finance, Teck Resources Ltd.

Thanks, Don. I'm on slide 10 and I'll start with a summary of changes in our cash during the third quarter. So, we generated \$882 million in cash flow from operations and, of course, we received roughly \$1.2 billion in proceeds from the sale of investments. Almost all of that was from our two-thirds interest in the Waneta Dam. We spent \$1.3 billion buying back some of our notes with near-term maturities, spent \$397 million on capital projects and our capitalized stripping costs were \$162 million. We paid \$140 million in expenditures for investments and other assets of which USD 60 million or \$78 million was for the second payment of the acquisition of IMSA that was required upon receipt of the regulatory approvals for QB2 that Don mentioned earlier.

We also paid \$133 million in interest and finance charges, \$29 million for our regular quarterly-based dividend of \$0.05 per share. After these and other minor items, we ended the quarter with cash and short-term investments of about \$1.5 billion and our current cash balance is now approximately \$1.8 billion.

Turning to liquidity on slide 11, our liquidity is currently \$5.7 billion and that includes the \$1.8 billion of cash and the USD 3 billion of our undrawn committed credit facility. We now have no significant debt maturities prior to 2024. And our strong credit metrics, which are shown on the bottom right, compared favorably to our diversified and our North American peers.

And as Don mentioned earlier, we also received regulatory approval to renew our normal course issuer bid in early October and that allows us to purchase up to 40 million Class B shares prior to October 9 of next year. And overall, we're in a very good position ahead of a potential sanctioning decision on our QB2 project.

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

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Thank you, Ron. I'd like to wrap up by looking forward to the next key catalysts or valuation milestones, if you like, for the remainder of 2018. First, we expect full production at Fort Hills in the fourth quarter. We may complete the partnering process for QB2 and be in a position to announce the transaction towards the end of the quarter, and then sanctioning of the project could also occur at that time.

In addition, we aim to complete the Highland Valley 2040 prefeasibility study in Q4. And in early 2019, we aim to complete the feasibility study at Zafranal. We also aim to complete the feasibility study on NU by Q3. And in addition, we expect to complete the prefeasibility study and submit the SEIA for San Nicolás in the second half of 2019. So, lots to look forward to over the next year.

And with that we would be happy to answer your questions and I should say that that some of our management team members are calling in from a number of different locations, so there may be a brief pause after you ask your question, while we sort out who's going to be answering it.

And with that, I'll turn it over to you, operator.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] The first question is from Chris Terry with Deutsche Bank. Please go ahead.

Chris Terry

Analyst, Deutsche Bank Securities, Inc.

Q

Hi, Don and team. Thanks for taking my questions. The first one is just around QB2, you gave some color there around – that you still expect it to be in the fourth quarter? Just wondered whether can you talk a little bit about the competitive tension, the different parties? I think, previously, you've mentioned that there's three main groups, trading groups, potential operating partner, et cetera, I was wondering whether you could talk through how that process is evolving in the wake of the current copper price environment? That's my first question. Thanks.

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Okay. While I appreciate the question and there would be a lot of curiosity on the issue, but I need to say that we really aren't in a position to disclose much about that other than what we've said already that the process is going very well, we're moving along. At this stage, we are on track for announcing a transaction this quarter. At the end of the day, of course, that depends on who we select as that partner and different aspects of their own schedule and their own board meetings, so we'll see how that works out. But we are very pleased with things looking forward. This is going to make a big difference to us in terms of reducing any financial obligations we have going

forward by a very significant amount, a couple billion dollars U.S., that order of magnitude and really leave us with a lot of financial flexibility and cash coming in.

And we're getting really good validation of both the quality of the project. People are now starting to see the data on QB3, which is very exciting and the perception of the project is changing quite dramatically into a project that is likely to be in the top 5 copper producers in the world when we move on to QB3 and what we think will be a doubling or a twinning of the concentrator there. So we're in the midst of it. We can't say much more than that other than we're very pleased.

Chris Terry

Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Thanks. Thanks, Don. And then just on the coal division, you mentioned that the higher costs are more of a one-off nature. I'm just wondering if you can give a little bit more color on that. I guess heading into the budgeting process for 2018 and setting the guidance for the coal division over that period, I'm just a little bit confused on the use of the contractors and planning versus what actually happened in that quarter? So just looking for a little bit more color on how to think about the next few quarters and into 2019 on the cost side? Thanks.

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Yeah. No. Important question and I'm going to turn it over to Robin Sheremeta to go through some of the details on that. But an overview comment, I would say, is that we're very pleased with how the coal business is running and shaping up for next year and thereafter. And quite excited exactly about what we're able to deliver to our customers in the context where my coal guy this morning earlier said, you know what, there's no coal out there. That's why we're seeing USD 225 or close to \$300. The operations are performing well on that context.

So Robin, over to you.

Robin B. Sheremeta

Senior Vice President-Coal Operations, Teck Resources Ltd.

A

Yeah. Thanks for the question, Chris. I'm going to walk you through a number of the different components, because I expected you want to understand this in a bit more detail. So if we look at the difference in cost of sales from Q2 to Q3, and there was quite a jump of about \$8. The first one is really associated with our scheduled plant maintenance shutdowns at our two largest operations, Fording River and Elkview. This impacted our cost by about \$2 a tonne. We've got no further major shutdowns scheduled through the end of the year, so these costs are pretty much behind us now.

The second is associated with their use of contractors. And the best example of this, and I think I've spoken to this in the past is with Coal Mountain shutting down, we've got latent capacity at that operation in the plant. They don't have – the mining portion is shutdown, but the plant still fully operational, and it's close enough to Elkview. It's about 30 kilometers south. We can deliver the additional raw coal that we have available at Elkview, because of the strong mining performance there and process it through Coal Mountain. But that does cost more money to ship it that distance by highway.

And so if you take that and a number of other use of contractors we've had to maintain equipment availability at high level, things like that, that's impacted our cost by about \$2 a tonne. And then in the quarter, somewhat unique to the quarter we were generally mining in higher cost areas and that's just the mine plan.

It's simply a timing issue with pit development. So, we expect this to balance out through the year. And that for the quarter was actually around \$3 a tonne, between \$3 and \$4 a tonne.

So, those are the three main components to it. And then as far as, maybe I'll just speak to the guidance change. There are – again, there are the two main areas that have affected our year cost, different than I guess we had guided to earlier in the year. First being diesel. Diesel alone consumption and pricing has added about \$2 a tonne for the year over what we had originally guided to. And diesel is what it's going to be. And then certainly the other area has been the use of contractors. So as Don mentioned with the strong margins we're seeing, we're chasing those last few tonnes of coal that deliver exceptionally good value in this kind of a market. The Elkview example is probably the best one for that, so. Then I think that's pretty much the big buckets.

Chris Terry

Analyst, Deutsche Bank Securities, Inc.

Q

Okay. I appreciate the detail there. Thanks. That's all for me.

Operator: Thank you. The next question is from Orest Wowkodaw with Scotiabank. Please go ahead.

Orest Wowkodaw

Analyst, Scotia Capital, Inc.

Q

Hi. Good morning. I've also got some questions really about the coal. The first one just on the cost side. So, if I heard what you just said I think, it sounds like we should think about higher costs moving forward for at least diesel and contractors of, call it, in the range of \$4 to \$5 a tonne, higher than maybe we were thinking about before, is that? Then kind of fair to say if we kind of eliminate this hauling distance issue and maintenance in the quarter?

Robin B. Sheremeta

Senior Vice President-Coal Operations, Teck Resources Ltd.

A

I think on the diesel, it is what it is. On contractors, I guess, one key piece of the contractors I should mention is we've been ramping up our internal capacity around trades but that takes time. So, that means developing apprenticeships. It means recruiting. And the time it takes to do that, we've supplemented a lot of our on-site labor around maintenance with contractor use.

So, you're going to expect that to reduce over time as we get additional trades on track. So again, that's a cost we incurred today because we're not going to put production at risk in this kind of market environment. So, we expect that kind of costs to come back down.

Our cost like hauling coal from Elkview to Coal Mountain, again, that will change in time as we build up the capacity of the Elkview plants. So, that operation will move from 7 million tonnes to 9 million tonnes as we look ahead to the plant to replace tonnage out of Coal Mountain. And as Elkview capacity increases, we'll likely reduce the amount of coal we hold to Coal Mountain, because it'll be a lower cost. So, those are a couple of the key things that will change in time.

Orest Wowkodaw

Analyst, Scotia Capital, Inc.

Q

Okay. And then...

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

I mean, just to put in perspective, the swing factors in where we are in the mine plant or the coal price itself was up more in a single day today than the total of the cost increases that we're talking about. And looking through quarter-to-quarter, you could have significantly greater changes just by where you are. Strip ratio is coming down from 10.7% to 10% over the next year or so, and that will overwhelm this kind of cost numbers that everyone is focused on. And we do have the flexibility to stop using contractors if there was a very significant downturn. So, it's not a permanent part of the cost structure that can't be addressed or something.

A

Orest Wowkodaw

Analyst, Scotia Capital, Inc.

Okay. Now, I appreciate the color there. And just sticking with the coal, I mean, this is I think the recurring theme of volumes being constrained by logistical issues. Should we start to worry that this is going to impact 2019 and 2020 volumes, given that you're still beholden to Westshore? And is there anything that can be done in the interim to, I guess, ease some of those constraints, or is there being anything done?

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Yeah. I would just turn it over Andrew Stonkus in a moment, but we are in constant dialogue with the management of Westshore. They have taken some steps to improve. We've actually seen better performance over the last quarter or so. But Andrew, you want further color on that?

A

Andrew A. Stonkus

Senior Vice President-Marketing & Sales, Teck Resources Ltd.

Yeah. Thanks, Orest, for the question. As you know, we have multiple terminals that we use to move our coal. So, we have Neptune facility, and Ridley. We also have Eastbound shipments as well. So, we have some flexibility to move our coal to the market using other service providers. So, Westshore has had the unplanned maintenance downtime in Q3, which impacted our shipments, but we're in dialogue, as Don says, with Westshore to make sure that their performance meets our expectations. So, we have flexibility, and we utilize that flexibility when required.

A

Orest Wowkodaw

Analyst, Scotia Capital, Inc.

Okay. Thank you.

Q

Operator: Thank you. The next question is from Lucas Pipes with B. Riley FBR. Please go ahead.

Lucas N. Pipes

Analyst, B. Riley FBR, Inc.

Hey. Good morning, everyone, and thank you for taking my question. I'm still a little hesitant to ask a question about capital returns, but Don, you received the regulatory approval for 40 million of Class B share repurchases and obviously, this is a board decision, but could you please put this figure in context, and how you think about capital returns at this time? Thank you.

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Sure. Thanks, Lucas, and we continue to appreciate all the good work that you've been doing. We changed our policy a year ago, last September, to a more flexible dividend and buyback. Our capital returns policy is more like the companies that we compete with, particularly the London-listed ones. We have a base dividend of \$0.20 per share which is sacrosanct. And then, each year as we get to the November board meeting, we look at how the year was and what the capital needs are going forward, and determine the quantum of capital that we would return to shareholders and then, how we would split that between a cash dividend and buybacks.

And also, as part of our policy, we canvassed the shareholders during that September-October period, which we have been actively doing, and we've received a lot of feedback. While I can't speak for the board, it's very clearly a board decision, but I can say is that in the feedback from shareholders, as most of you will know already, there is a heavy bias towards buybacks and so we renewed our normal course issuer bid. And we doubled the size of it in terms from a regulatory point of view. And that is a strong signal, both what we intend to do and we intend to do shortly. So I think that's something that we would want to have in place all year long. And we think at this stage that it's a very attractive allocation of capital to do larger buybacks than last year.

Order of magnitude, it's hard to say. It's a board decision. But clearly, this year is a good year, it was a record first half. We did see significant declines in copper and zinc so it may not be a record year but it could be our second or third best year. So that suggests a pretty healthy capital return. But the final amount won't be decided until the November board meeting. And we won't quite have the partnership deal on QB2 decided by then, but we anticipate a reasonable amount of cash coming in the door related to that in a sense. And so you could see the decision adjusted related to that as well depending what the board's thoughts are on future allocation of capital.

But certainly at these share price levels, we were sitting here thinking, the company's operations are doing quite well, customer demand is very strong. My coal guy says there's no coal out there. My zinc guy says there's no zinc out there. My copper guy says, soon there's going to be no copper out there. So we think it's a pretty interesting opportunity right now.

Lucas N. Pipes
Analyst, B. Riley FBR, Inc.

Q

That's very helpful. Thanks Don. To turn it maybe back to coal, I noticed in the release there was a mentioning of a notice from the Canadian federal side in regards to the Fisheries Act. Any color as to the potential financial impact from that notice? And then to put that in context with your announcement regarding the saturated rock fill development, does that speed up the process or deployment of that technology? And if you could maybe remind us on the financial impact of the saturated rock fill versus your previously disclosed initiatives? That would be very helpful. Thank you.

Donald R. Lindsay
President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Okay. Another good question. I'll turn that over to Peter Rozee.

Peter C. Rozee
Senior Vice President-Commercial & Legal Affairs, Teck Resources Ltd.

A

So I'll start with the Fisheries Act charges. We are in discussions with federal regulators and prosecutors, and unfortunately there's really nothing more we can say in terms of providing color on that issue. At the moment, I would say we expect that it will take a number of months to play out. And in terms of the saturated rock fill, that

issue I think is quite unrelated to progress on saturated rock fill. And I'll turn it over to Robin to talk about the financial impacts of the saturated fill trials.

Robin B. Sheremeta

Senior Vice President-Coal Operations, Teck Resources Ltd.

A

Yes. I guess now try and put it in context of the saturated rock fill cost compared to the active water treatment facilities that – and the best example of that is one we're building at Fording River right now. So Fording River South facility is designed for 20,000 cubic meters of water a day. So 20 million liters a day, and it will cost just over \$300 million to construct.

The Elkview saturated fill right now in a pilot stage is running at 10 million liters of water a day throughput. It costs \$40 million to put in place. And it has a capacity, we think, easily around 60 million liters of water a day, so 6 times what the pilot is right now.

The next active water treatment facility that we were – which is a part of our – I'm sorry – water quality plant to construct would be the Elkview plant. So that saturated fill at Elkview has a potential to replace the Elkview plant that we had planned to build, which would be roughly \$300 million. And it will cost a bit more to bring water from the same location that we would feed the Elkview plant from, so there is some capital associated with that. But again, it will be a fraction of the cost of what it would take to treat or to construct an active water treatment facility. And it is treating significantly more water than we anticipated.

And as Don mentioned today, I think we've been running for nine months. We're getting virtually 100% removal of selenium and nitrate from that project. So it's extraordinarily exciting in terms of the potential that this has. It's still working its way through the proving stage. So we still have to work through that but at this stage, we're very confident this has a lot of potential for us.

Lucas N. Pipes

Analyst, B. Riley FBR, Inc.

Q

That's fantastic. Great job on that and continued best of luck. Thank you.

Operator: Thank you. The next question is from Greg Barnes with TD Securities. Please go ahead.

Greg Barnes

Analyst, TD Securities, Inc.

Q

Yes. Thank you. Robin, I just want to understand for 2019, can you support the 27 million to 26 million tonnes of coal production without the high use of contractors that you had to use this year?

Robin B. Sheremeta

Senior Vice President-Coal Operations, Teck Resources Ltd.

A

Yeah. Well, I'm just thinking through that – you went the other way on me on the tonnage, 26 million to 27 million tonnes. I had to think about that for a second. I mean, we're still working through our budget plan. I think certainly, the initial plans I've seen we're trying to reduce contractors on maintenance. That's just a matter of hiring and we're in that process, we're hiring trades, we're building apprenticeships. So, I would expect there to be less contractors associated with maintenance labor.

As far as things like hauling coal from Elkview to Coal Mountain, I think that would be discretionary additional tonnage and we could support a tonnage profile of 26 million to 27 million without doing that. We would do that

because it would return exceptionally good value if it was a continued strong market. If the market pulled back, we wouldn't spend that kind of money to do that additional tonnage. But a mine plan between 26 million and 27 million is achievable without the level of contractors that we're currently using.

Greg Barnes

Analyst, TD Securities, Inc.

Q

But is it supportable without trucking the coal to Cold Mountain or not? Or do you have to ship to Coal Mountain to get to the 27 million tonnes?

Robin B. Sheremeta

Senior Vice President-Coal Operations, Teck Resources Ltd.

A

We don't.

Greg Barnes

Analyst, TD Securities, Inc.

Q

Okay.

Robin B. Sheremeta

Senior Vice President-Coal Operations, Teck Resources Ltd.

A

We don't have to ship to Coal Mountain to achieve that range of tonnage for next year.

Greg Barnes

Analyst, TD Securities, Inc.

Q

Okay. I just want to follow up on the coal market, Don or Réal. Obviously, the coal price looks very good today. Is that just the fact that at Goonyella, the fire there has stripped out potentially 3 million tonnes of coal, or is it higher demand out of India? And how is Indian demand tracking this year relative to what you expected?

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Okay. I'll turn it over to Réal.

Réal Foley

Vice President-Coal Marketing, Teck Resources Ltd.

A

All right, Greg. So, I guess the main reason why coal prices are where they are, I mean, demand continues to be really strong. If you look at crude steel production around the world, September year-to-date, it's up nearly 5% compared to last year. And out of that, India is up over 6%, very similar to China actually, and the rest of the world is running plus 3%. So we continue to see very strong demand fundamentals. On steel per se, steel pricing is also very high, not only in China but everywhere in the world. And that is continuing to support the steelmaking coal market.

On the supply side, supply is actually very tight and as soon as there is a little disruption, we see that reflected in price. We know of logistics limitations and also of production challenges. On the logistics side, we've talked about Westshore earlier. But in Australia, there is also logistics limitations with Horizon and DBCT.

On the production side, there has been a fire at the Goonyella. That mine produced 2.8 million tonnes in 2017. And then in the States, Mission filed for Chapter 11, and they shut down their Pinnacle Mine, which

produced 1.2 million tonnes in 2017. So steelmaking coal supply continues to be impacted. And as a result of pricing for coal, it's still somewhere around USD 220.

Greg Barnes

Analyst, TD Securities, Inc.

Okay. Great. Thanks, Réal.

Q

Operator: Thank you. And the next question is from Oscar Cabrera with CIBC. Please go ahead.

Oscar Cabrera

Analyst, CIBC World Markets, Inc.

Thank you, operator, and good morning, everyone. If I may just go back to – I was really surprised to see this move by the Canadian federal prosecutors. I mean, if memory serves, you guys have been super proactive and spending a lot of money with this water treatment. And I understand that it's difficult to provide guidance on the financial impact, but would it be possible just to differentiate what the Fisheries Act or – the things that they're looking at on selenium versus what you have been working on?

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Thanks, Oscar. I would like to reinforce it. We certainly believe we have been super proactive too. And I think evidence of that as just what Robin Sheremeta has been talking about. And a lot of dollars spent on R&D that looks like it's going to be very successful and that's in addition to the large capital spending on plant construction already. But in terms of the more specifics of your question, I'll turn it back to Peter Rozee to answer that one.

A

Peter C. Rozee

Senior Vice President-Commercial & Legal Affairs, Teck Resources Ltd.

Yeah. Oscar, unfortunately, we just can't give you any further color on the issue, given the status of our discussions with regulators.

A

Oscar Cabrera

Analyst, CIBC World Markets, Inc.

Okay. No. Fair enough. Then if I may just continuing on the coal side, you talked about your valuing the McKenzie Redcap design, which may give you about 1.8 million tonnes of additional production by 2020. Could you talk about the scope of the project in terms of capital? I know that the other project that you were working on, I think the intensity of capital was about \$250 a tonne. Any color you can provide on this one?

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Sure. So, that project up until I guess last year, we were anticipating closure at Cardinal River and that would have occurred around 2020. So, the plan that we're working on is to advance it a little farther out. And that would support that 1.8 million tonnes a year.

A

Through to about 2027, I think, is the year so eight or nine additional years. And as far as the order of magnitude on capital costs, it would be less capital intensity than Quintette. So it's actually a pretty strong project and I don't want to speak too much about this stage. We're going through an approval process and the final economics on it, but it would fall on that range. It would be a better project than Quintette would be.

Oscar Cabrera

Analyst, CIBC World Markets, Inc.

And in terms of level of magnitude, a better project 20% lower capital or we have – there was actually some – we have some numbers for Quintette but...

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Yeah. It's going to roughly fall in a range of between \$100 million to \$150 million.

A

Oscar Cabrera

Analyst, CIBC World Markets, Inc.

Okay. Perfect. And then last but not least, like you, we've been surprised by what appears to be still a strong physical market. And I was wondering if you guys could comment on what you're seeing for both zinc and copper in terms of refined premiums and in spot premiums?

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Okay. Over to Andrew Stonkus.

A

Andrew A. Stonkus

Senior Vice President-Marketing & Sales, Teck Resources Ltd.

Yeah. Thanks, Oscar. I'll start off with zinc. Zinc continues to be drawn down the LME inventory as we're watching. It's a significant drawdowns in the LME inventories and SHFE inventories. So on the back of Chinese smelting underutilization rates that the smelters in China, with the environmental regulations in place being enforced, so Chinese metal production is down about 5% year-to-date based on the last statistics. And domestic Chinese mine production is down roughly around 10%. So in China, both metal and concentrates are being drawn down or not being produced. And we are going into the winter season in China so the Northern Chinese mines will tend to reduce their production. So, there'll be an ongoing draw down of inventories of China we suspect. So, metal inventories have been drawn down. The arbitrage is attracting metal from LME inventories, New Orleans, specifically to China and strong pricing in the Asian marketplace.

A

In North America, demand is very strong as Réal pointed out. The steel mills are running at strong utilization rates and that includes galvanized production. So, galvanized global production is up about 3%. So, demand globally for galvanized steel is strong.

On the copper side as well, the inventories as we all know are really at extremely low levels. Metal premiums have been going up. They are approximately a \$100 on the spot market and the annual cathode premiums have been – already been established at \$10 higher than last year. So, the metal inventories are tight.

We still have smelters down and some smelters down in India, specifically. And some other smelters are struggling with their production. So, supply is being a constraint on the metal side and demand remains to be strong. So, it's all shaping up to be a fundamentally very strong markets for both metals and concentrates.

On the zinc concentrates, TCs have gone up, Oscar, reflecting some of the additional new mine production coming on stream but they are still very low TCs relative to historical levels.

Oscar Cabrera

Analyst, CIBC World Markets, Inc.

Great. Well, thank you, everyone.

Q

Operator: Thank you. The next question is from Mark Levin with Seaport Global. Please go ahead.

Mark Andrew Levin

Analyst, Seaport Global Securities LLC

Thanks. My questions have been asked and answered. I appreciate it.

Q

Operator: Thank you. The next question is from Matthew Fields with Bank of America. Please go ahead.

Matthew W. Fields

Analyst, Bank of America Merrill Lynch

Hey everyone. You obviously made – on the balance sheet, you made a lot of progress with the USD billion dollar tender in the quarter. Is the last step – the sort of agencies have talked about clarity on QB2 from a partner and a funding perspective as kind of the last hurdle towards upgrading you back to IG. Is that your understanding as well? And do you think that kind of, if you sort of resolve everything in the fourth quarter, we could see the agencies move by maybe 1Q 2019?

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

I'll turn that over to Scott Wilson, please.

A

Scott R. Wilson

Treasurer & Vice President, Teck Resources Ltd.

Thanks for the question, Matthew. The credit rating agencies don't tell us anything differently than what they publish in their reports and indeed you've captured our understanding of what the agencies are looking for before potentially moving on their positive outlooks on our rating, that being the QB2 partnering, the timing of sanctioning and the financing. And so we do anticipate, as Don said, being able to provide clarity on those things, potentially as early as later this quarter or in early Q1. And we would hope that the agencies would then act on the positive outlook.

A

Matthew W. Fields

Analyst, Bank of America Merrill Lynch

And your sort of intent to sort of pursue that upgrade, given that it frees up a tremendous amount of LC capacity for you?

Q

Scott R. Wilson

Treasurer & Vice President, Teck Resources Ltd.

You're correct. It would lower our costs. Our requirements for letters of credit for certain contractual arrangements would fall away. So, we are very interested in having our investment grade rating reinstated.

A

Matthew W. Fields

Analyst, Bank of America Merrill Lynch

All right. Thanks. That's it for me. Thanks very much.

Q

Operator: Thank you. The next question is from Brian MacArthur with Raymond James. Please go ahead.

Brian MacArthur

Analyst, Raymond James Ltd.

A couple of questions. Good morning. First of all, there's a comment made on Trail that costs were up partly because of higher electricity costs. Can you just remind me where we stand now, post the sale of dam? Are you net short power for Trail and that's why the cost was up? Was it just you don't have the third-party power sales now or is it like there's just plain higher costs in BC or what combination of where we stand on this going forward?

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

No. So we're not net short power at all. It's just simply a reflection of the deal that we did on Waneta. Maybe I'll turn that over to Dale on the phone.

A

Dale E. Andres

Senior Vice President-Base Metals, Teck Resources Ltd.

Yes. Sure. Thanks. Thanks, Brian. Yeah. As part of our negotiated PPA, as part of the sale agreement, our power cost at Trail will increase around \$70 million to \$75 million a year. So, it reflects that starting in Q3.

A

Brian MacArthur

Analyst, Raymond James Ltd.

But that's just the BC power rate. And we have a situation that goes way back like we had 15 years ago when rates get out of whack. Are you protected or is it a fair...

Q

Dale E. Andres

Senior Vice President-Base Metals, Teck Resources Ltd.

Yeah. It's a long-term negotiated rate under our PPA with the sale agreement to BC Hydro. So, it's a fixed rate that escalates over time with inflation, but that's it.

A

Brian MacArthur

Analyst, Raymond James Ltd.

Great. Thanks. The second question goes back to the call, I'm sorry. Just how many tonnes are actually being moved from Elkview to Coal Mountain? I'm trying to determine. Obviously, overall business is up \$2 a tonne, but obviously those tonnes cost more. And there must be a decision made on A, I guess whether the volume tips the whole market over; or B, just a pure economic change, because I would think at USD 180 coking coal. You would always continue to do that. So, I'm just trying to figure out how many tonnes you're actually moving at those much higher costs.

Q

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Robin?

Robin B. Sheremeta

Senior Vice President-Coal Operations, Teck Resources Ltd.

A

Yeah. Well, we're sort of at the frontend, but we've been doing it for a few months now. We could – I think through the year, we could move as much as 400,000 tonnes from Elkview to Coal Mountain. So, that's roughly the tonnage we're looking at this year. But again, I mean, that's not an ideal situation in the sense that we would prefer to process it closest to the mine and that's why we're advancing the expansion of the Elkview plant. So, ultimately we try from a cost basis certainly to keep the processing as tight to the mine as we can.

Brian MacArthur

Analyst, Raymond James Ltd.

Q

Great. Thanks and maybe one final comment and I don't know – I appreciate it and I think Oscar has asked as well and it's been asked before. So you really can't comment on this Elk Valley situation. But can you even say what the feds are after here? I mean, there's a comment made in here that says talking about since 2014 and I assume that was written carefully. Are they actually disputing what you've done since you put in the new stuff or does this go back to historical? Because I would think there are slightly different issues if they're complaining about what you're doing going forward, all the money and all the new good stuff you're doing is going to be less valuable or can you comment at all on that?

Peter C. Rozee

Senior Vice President-Commercial & Legal Affairs, Teck Resources Ltd.

A

No, I'm sorry. We just can't comment at all.

Brian MacArthur

Analyst, Raymond James Ltd.

Q

Okay. Sorry about that. Thanks.

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

And Brian, just on Waneta, just to be clear, we have like a long term, 15 years stable agreement so totally insulated from volatility and costs and option to renew after that. And the valuation of Waneta reflected about 16 times EBITDA or a bit more, and that's more than quadruple what that stream would have been worth within Teck Resources today. So, there was a very strong logic to doing that transaction.

Brian MacArthur

Analyst, Raymond James Ltd.

Q

No. I totally agree with that. I was just curious when you made the comment that costs went up. And I'm just trying to figure out, make sure there was nothing else in there. But that's very helpful. Thanks, Don.

Operator: Thank you. The next question is from Greg Barnes with TD Securities. Please go ahead.

Greg Barnes

Analyst, TD Securities, Inc.

Q

Thanks. Don, I just want to follow up on QB3, and maybe jumping the gun a bit but would that require to go through that whole permitting process again in Chile, and are we talking – this is a 2030 type of initiative or is that a 2027, 2035? What are you thinking?

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Short answer the first part is yes, but the advantage of course is we've got all the people in place both on our side and the government side that are very experienced in this, very good high quality dialogue so you anticipate that being easier. And remember, we're just talking about twinning what's there and there would be an awful lot less to do on the tailings management facility because it's already done. So QB3 will have significantly less capital required than QB2 so it goes to become very, very capital efficient in terms of CapEx per tonne of capacity and much higher IRR.

It would become the best project in our portfolio in terms of timing because of what we see. And certainly from the feedback from potential partners we have, we're very excited about it. We would be filing the SEIA while we're under construction so that we could start that process as soon as we can and our target would be to be in production by 2026 so.

All of this is just at the scoping or conceptual/scoping stage. But we're clearly going to move this along as fast as we can. Because basically, we're coming to realization that the 4.8 billion tonnes resource that we published isn't anywhere near, what the end resource is going to be.

And given the scope of that, that we should be thinking bigger on what this is. It's in a great geopolitical jurisdiction. It's – got a complete community support. We have 100% of the indigenous community signed now. This is unique. We had a unanimous support in the vote for the permit. So, we should be thinking much bigger on what QB2/QB3 and beyond could look like.

Greg Barnes

Analyst, TD Securities, Inc.

Q

And Don, given great profile, would this – the doubling of capacity, would this mean it's a 500,000, 600,000 tonne a year copper mine, or is it somewhat lower than that as the profile comes down?

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Certainly, we'll be targeting over 500,000 tonnes plus molybdenum on top of that. Yeah. So, it's in that range.

Greg Barnes

Analyst, TD Securities, Inc.

Q

Great. Thank you.

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

And that would be for QB3. Who knows whether we'll end up with QB4 way down the road?

Greg Barnes

Analyst, TD Securities, Inc.

Q

Right.

Operator: Thank you. The next question is from Karl Blunden with Goldman Sachs. Please go ahead.

Karl Blunden

Analyst, Goldman Sachs & Co. LLC

Q

Hi, guys. Thanks a lot for taking the time. Question for you just on the capital allocation decisions you can make. I know we've touched a little bit earlier if you get clarity on QB2 and the partnership funding there that might be enough for the rating agencies to move and give you more freedom.

Could you comment a little bit on whether that you think there are any trade-offs there when you think about the equity returns that you've discussed? Has that been any hold up or is clarity on QB2 really the only thing you really need now?

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

I'm not sure if I fully understood the question.

The first part that we have said that what the rating agencies have told us, they're looking for. I do want to remind people that in terms of our ratios right now and everything that we have done working towards getting that investment grade reinstated, we're already there on all of that. They're just wanting to lock down what their assumptions going forward are on the QB2 side of it, which is fair. I'm not sure what equity component of your question might mean.

Karl Blunden

Analyst, Goldman Sachs & Co. LLC

Q

The question there was that as you increase your equity returns to shareholders, which is fair given the cash flow that you generated, whether that was something that they viewed negatively and a contributing factor to the time they're taking to recognize the improved metrics.

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

... But does your phrase, equity returns refer to returning capital to shareholders?

Karl Blunden

Analyst, Goldman Sachs & Co. LLC

Q

That's right. Yes.

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

A

Okay. Well, I think the rating agency will look at that. We've announced our policy, and we'll be sticking to our policy. Again, we don't know what the quantum is, but it will be consistent and reflective of the very good year we're having. And the fact that we have reduced capital needs going forward. So, I think we'll be in line with what our policy is and they're already aware of our policy.

Karl Blunden

Analyst, Goldman Sachs & Co. LLC

Okay. That's helpful. I think the last piece there is just great. Thanks.

Q

H. Fraser Phillips

Senior Vice President, Investor Relations and Strategic Analysis, Teck Resources Ltd.

Operator, I think we're going to have to call it there. Unfortunately, we're at the end of our time. But let's turn it back to Don for any closing remarks.

A

Donald R. Lindsay

President, Chief Executive Officer & Director, Teck Resources Ltd.

Okay. Well, thank you very much for joining us today, and thank you for your questions. I thought they were a very good list of questions today. We're feeling pretty good about the status of the company and a lot of things happening that are very, very positive for the future. We're seeing strong operating results. While the market will always be volatile, the actual customer demand, the fundamentals of supply and demand that we're seeing are not reflective of the tone of concern that we see in the equity markets. Who knows which way the world will actually go? But for now, these are very strong markets for us and the cash is flowing in. We have tremendous growth opportunities in copper, and to borrow a phrase from a well-known industry associate at Teck, we now have copper growth for as far as the eye can see. Say that with a smile. But anyway, thank you very much and we look forward to speaking to you next quarter.

Operator: Thank you. The conference has now ended. Please disconnect your lines at this time and we thank you for your participation.

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