

# Earnings Call Transcript

## Rockwell Diamonds Inc.

### Quarter 3 Fiscal 2010 Results Call

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#### CORPORATE PARTICIPANTS

**Susie Bell** – Investor Relations

**John Bristow** – President & CEO

**Dave Copeland** – Chairman

**Desmond Morgan** – CFO

**Graham Chamberlain** – Chief Operating Officer

**Glenn Norton** – Mineral Resources Manager

**Jeffrey Brenner** – Manager, Diamond Marketing and Sales

*Note: All dollar figures are expressed in C\$ unless otherwise stated.*

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#### Operator

Good day, ladies and gentlemen, and welcome to Rockwell Diamonds Inc. Third Quarter Fiscal 2010 Results Conference Call. Today's call is being recorded. At this time, all participants are in a listen-only mode. We will conduct a question-and-answer session towards the end of the conference.

I would like to turn the conference over to Susie Bell, Investor Relations.

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#### Susie Bell - Investor Relations

Thanks very much. Good day, everyone, and welcome to the Rockwell Diamonds Third Quarter Fiscal 2010 results conference call. I am Susie Bell with Investor Relations. Today with me on the call we have: John Bristow, President and CEO of Rockwell; Dave Copeland, Chairman; Desmond Morgan, CFO; Graham Chamberlain, Chief Operating Officer; Glenn Norton, Mineral Resources Manager, and Jeffrey Brenner, Manager of Diamond Marketing and Sales.

After the opening remarks with management where we will be reviewing the third quarter business operational results, we will open the phone line to analysts and investors for a question-and-answer session.

I would also like to remind you, our listeners, that our comments and our answers to your questions may contain forward-looking information. This information by its nature is subject to risks and uncertainties and may cause the stated outcome to differ materially from the actual outcome. Please refer to the bottom of our latest news release for more information.

I would like to turn the call over to John now for his remarks.

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#### John Bristow – Rockwell Diamonds – President & CEO

Thank you, Susie, and good morning or afternoon ladies and gentlemen, and welcome to Rockwell's earnings call in which we will report on our results for the previous three and nine month period to November 30, 2009. At this time, I also would like to wish everyone a happy New Year although the New Year has passed and wish you best wishes for 2010.

This presentation will cover highlights for the nine months, our financial results, ongoing initiatives to improve performance of the company, the diamond market, our fund raising, and our plans and outlook for 2010.

It is old news now, but I think we all are well aware that the nine month period in discussion was particularly challenging for Rockwell, and just about every other junior and senior mining company, be they in diamonds or any other commodity for that matter. However, Rockwell's ability to address challenges coupled with an improvement in diamond prices in the latter part of 2009 ensured that the company was able to weather the storm.

In summary, and significantly, robust management of costs, increased production, improved sentiment in the diamond markets in the latter part of 2009 and firming of prices ensured that the company returned to profitability in the third quarter ending November 30.

We remain cautiously optimistic in respect of diamond prices for 2010 and look forward with interest to see how the early 2010 sales will look relative to the end of 2009.

In spite of a difficult and challenging previous year, it is also satisfying to be able to report the following highlights for the company:

- Firstly, obviously, the fact that at the end of our quarter three, Rockwell was able to show a small profit and at the same time was able to settle a large part of our short-term debt.
- Secondly, and particularly satisfying, our cash operating cost remained consistently below the US\$3 per tonne mark for the entire period, the entire nine-month period that is.
- Thirdly, Rockwell was able to resume payment on the lease payment holiday we negotiated with Komatfin or Westbank without incurring any penalty interest.
- Fourthly, diamond prices improved in the latter part of the nine-month period and Rockwell saw its average diamond price return to a better than break-even position of about \$1000 per carat.
- Fifthly, Saxendrift, which we acquired in 2008, had an excellent nine months, both in terms of production ramp-up and regular recovery of large and exceptional stones, with the highlights being the recovery of three stones over 100 carats, the startling pink stone and a number of intense yellow stones in the nine months period we are discussing.

The performance of Saxendrift and the high volume plant we commissioned early in 2009 and the overall contribution of this unique deposit highlights it as a key driver in our company and all the more reason for us to consider and implement the re-commissioning and modernization of Wouterspan across the river on the same type of deposit, and that most importantly, this deposit yields the same diamond population as Saxendrift, and we'll come back to that later in the presentation.

Moving on to our most recent financial results, in the three months to the end of November:

- We recovered 7,963 carats and importantly, just to put that in perspective, in the equivalent previous quarter we did around 6,000 carats from four mines, so the important thing is that in this quarter, we are referring to, we did nearly 8,000 carats of gemstone diamonds from our Holpan/Klipdam and Saxendrift mines and just want to remind everyone that Wouterspan remained on care and maintenance throughout the period.
- 9,409 carats were sold at an average price of US\$1,268.

- Our sales were \$12.8 million and together with other contract sales of nearly \$100,000 we did revenue of \$12.9 million.
- Cost of sales totaled \$7.1 million, amortization totaled \$3.3 million.
- We achieved an operating profit of \$2.5 million for the quarter.
- Our net general and administrative expenses for the quarter were \$1.6 million, interest amounted to \$0.3 million and we had a small tax payment.
- At the end of the day we ended up with a profit of \$0.5 million or \$0.002 per share for the quarter.

By way of comparison in the equivalent quarter of fiscal 2009, the company generated a profit of \$4.5 million. So as I say just to recap, the satisfaction for the company was that in our prior quarter – three months we returned to profitability and importantly saw diamond prices improve substantially compared to the beginning of the year.

For the nine months ended November 30, 2009:

- We mined 19,920 carats compared to 16,558 for the previous equivalent period. And again I should just point out that these nearly 20,000 carats came from three operations, not the four mines that we were running in the previous year.
- 20,646 carats were sold at an average price of US\$969 per carat.
- Sale of diamonds by tender achieved \$21.9 million, while our beneficiation profit share was \$0.5 million and we had other sales of \$0.3 million, thereby resulting when combined, a total revenue of \$22.7 million for the nine month period.
- Cost of sales for the nine months was \$16.7 million, amortization amounted to \$8.3 million and as a result, we had an operating loss of \$2.3 million for the nine month period.
- Net general and administrative expenses amounted to 4.8 million.
- Interest expenses were \$1.1 million and there was an offset and recovery of \$1.6 million in respect of tax.
- Overall, the nine month period thus realized the loss of \$6.1 million, equivalent to \$0.026 per share. Just by way of comparison, in the equivalent nine months period of fiscal 2009, the company achieved a profit of \$1.4 million.

Our diamonds in inventory at November 30, 2009 totaled 2,800 carats; in respect of cash at that point in time the company had a positive cash position of \$2 million.

Moving on from the financials and we are happy to come back and discuss those. The management of costs remains a key focus for the company and our operational, mineral resource, financial and service teams continue to focus daily on managing costs, improving productivity and improving efficiencies at the operations.

Rockwell's Board of Directors and senior management also continue to actively monitor and enhance operating procedures and cost.

As for the previous quarters, we continue to review existing initiatives and introduce new initiatives aimed at sustainable long-term operational improvements, cost reduction and production increases.

In the latest quarter, our initiatives have included amongst others:

- A robust analysis of our geological mapping and characterization of our Holpan and Klipdam gravel resources north of Kimberley. At these two mines we are increasingly mining high volumes of surface deflation or what we term “Rooikoppie” deposits relative to the underlying older paleo-gravels. The Rooikoppie’s are more variable than the underlying gravels in terms of geological and grade character and hence it is important that we are able to establish in advance the nature of our mining blocks, so as to make refinements to our mining and processing procedures.
- We have also implemented a robust review of our earth-moving and mining fleets, aimed at again improvements of efficiencies and long-term rationalization of the fleet, and in particular the budgeting for and replacing of small equipment with larger, more cost-effective units going forward.
- As a third point, we have implemented an assessment of in-pit screening options to reduce the amount of tons we tram from our pits. In light of this we are looking at ways and means to reduce the impact of summer rainfall on our haul roads and mining and screening procedures, particularly at Holpan and Klipdam, which certainly this year have been a lot wetter than the Middle Orange River to the west of Kimberley.
- We have been streamlining our purchasing, procurements and storage procedures.
- We have an ongoing focus on training aimed at productivity enhancements.

Through these initiatives and other changes reported on previous calls, we continue to enhance our operational performance and manage and reduce costs. To-date, we have been able to reduce our cash operating costs on a sustainable basis and in the past nine-month period, we achieved an average cost of US\$2.73 per ton which is well below our target of US\$3 to \$3.50 per ton. Our total costs including rehabilitation, hire purchase payments and royalties were US\$4.44 per ton.

If we move on to the diamond market, we saw encouraging signs of improvements in trades, demand and sales in the later half of 2009 and indications are that 2009 year end, Thanksgiving to Christmas, sales in the U.S. showed an improvement over the previous year; not large, but certainly an improvement.

Importantly, demand for diamond jewelry remains strong in China and India, while the rest of Asia continues to show resilience. Jeffrey Brenner, Diamond Marketing and Sales Manager, has just returned from China, where he included a visit to the Shanghai Diamond Exchange and he can share this recent real-time experience of this important and rapidly expanding diamond venture and country with you later in the call.

Just to get more specific; as noted, diamond prices did improve in the later part of the year and this, importantly, was also in spite of the fact that major diamond producers like De Beers, who cut back production dramatically in the first part of 2009 started to increase their sales of rough diamonds into the market in the later half of the year, without us seeing a negative impact on the market and pricing.

During the later part of 2009, Rockwell saw strong demand and improved prices in the 2 to 10 carat rough range, effectively the bridal range, with greatest increases in prices on the 2 to 5 carat range. Prices of spotty and poorer quality Indian goods also improved slightly in the third quarter as Indian buyers returned to the market. Good quality large goods above 10 carats in size also improved in this quarter, particularly for large white stones.

By our estimates, they show that prices in the 2 to 10 carat range were probably at about 70 to 80% of prior year prices (2008 prices) where plus 10 carat, top quality white stones were showing prices in line with 2007 values. We remain cautiously positive throughout the diamond market and price trends and the fact that sentiment has improved is particularly encouraging.

In respect of corporate matters, we appointed two new directors to the Company following the resignations of two of our previous independent directors, and I would like to add that new directors Richard Linnell and Willem Jacobs have made notable contribution since their appointments and as indicated in our previous earnings call, their close proximity to the management team is particularly useful.

During the period under review, we also strengthened our financial management team by appointing Mr. Johan Oosthuizen who worked previously, amongst other places, at De Beers to run the financial department for our Northern Cape operation. As of November 1, 2009 we also appointed Mr. Graham Chamberlain as our Chief Operating Officer and Mr. Hans Gastrow, also ex De Beers, to manage our processing plants and recovery systems.

Graham and Hans are mining engineers and have already provided important experience and skills to supplement and strengthen our existing operating and management team. They will also play a key role in assisting the Company resume its growth plans and are already actively involved in planning for the modernization and re-commissioning of the Wouterspan mine. We are also well aware that the Company has undertaken a successful private placement and we will also complete a rights offer shortly.

Further to our latest news release, Rockwell has closed its private placements, which was oversubscribed and resulted in the receipt of approximately \$8.6 million in total. These funds were raised through the issue of a total of 132.8 million new shares at a share price of \$0.065.

Due to the success of the private placements and the intervening festive season period, the Company's rights offering was delayed slightly, so that the private placement could close. The Company has now filed the latest draft of the rights offering circular with the Canadian securities regulatory authorities in all of the provinces and territories of Canada and with the Toronto and Johannesburg Stock Exchanges.

As soon as we have final approval of the circular we will provide a timetable for the implementation and closing of the rights offering. And given all things being equal, we would like to get this process going now in the next two weeks or so and it will then run for three weeks or thereabouts to ensure that everyone has adequate time to participate in the rights offering.

Completion of at least \$3.1 million of this rights offering is guaranteed or underwritten by Daboll Consultants, who are associated with the Steinmetz Diamond Group. Assuming that all our shareholders follow their rights, the Company would end up with the combined proceeds of about \$14.7 million from the private placement and the rights offer.

Obviously the Directors and Management of the Company, most of who are shareholders, are well aware that the fund raising has been dilutive to shareholders. The impact of dilution was debated and considered at length, and the prevailing and prudent view, mindful of the events of the past 12 months and also the uncertainty in respect of the diamond and equity markets in the year ahead, we came to the view that the Company should be placed on a firm financial footing and in a position to settle short term debts and resume expansion and growth.

The funds raised from the private placement and rights offer will be applied to the modernization of the Wouterspan plant, which is across the river from Saxendrift, so we will re-modernize that plant and we will also fund some improvements to our existing operations. The prime objective here being to increase Rockwell's diamond production by about 800 to 1,000 carats per month in the short term. This will obviously reflect very positively on our revenue flow, cash flow and profitability.

We will also use funds and have in fact already done so to repay or retire outstanding short-term Komatfin debt or Westbank debt; that was the lease holidays we took. Our overdraft facility will also be settled and debts incurred during the hostile corporate activities we experienced in late 2008, 2009 will also be settled and beyond that we will ensure that we hold our normal two months working capital buffer to manage the company through quiet times in the diamond market.

In respect of our debt situation, it is simply worth reminding ourselves that Rockwell experienced an unplanned outflow of approximately \$2.5 million during the corporate hostilities of 2008, 2009. So we are well positioned to settle all these debts and importantly take the company forward and add significant new carat production to the company.

We have also had discussions with our legal counsel on a consolidation or rollback of our share structure and we will certainly further investigate this once the fund-raising is complete and we are confident about trends in the diamond market. In respect of our fund-raising initiatives, I would like to welcome our new shareholders, in particular Godia Capital out of China, Daboll Consultants, who were affiliated with the Steinmetz Diamond Group and some new additions to our Middle East and investment partners and obviously also our existing shareholders are important in this respect in terms of the future of the company.

In our letter to shareholders distributed to all of you at the time of our AGM in late October 2009, we outlined our plans for the long-term growth and expansion of Rockwell and pointed out that we had identified three groups of shareholders, who had indicated their support for the company's strategy of growth and expansion. We are very pleased to note that the groups that we outlined in our letter committed themselves to the company's private placements and also intend to follow their rights going forward.

As regards our plans for 2010 and I guess in particular fiscal 2011 our long and short-term objectives remain in line with our previously documented plans. By way of short-term priorities, the company will maintain flexibility and resourcefulness to ensure that we can maintain our return to profitability. We will:

- Manage costs, leverage diamond sales and enhance production to maximize revenue at Rockwell's existing operations.
- We will continue to implement ongoing improvements and re-engineering of our processing and recovery plants to overcome bottlenecks and improve efficiencies.
- We will also proceed with the modernization and re-commissioning of the Wouterspan operation which has a history of producing large and exceptional quality gemstones. I should add here that the planning process including engineering, design and costing to benefit from the design benefits and high volume production we have seen at our Saxendrift plant, are well advanced in respect of Wouterspan.

Over the longer-term, the company remains committed to its growth and development plans which will include:

- Increasing the rates of evaluation of our existing defined resources and the assessment of the liability of other diamond projects in our extensive portfolio of mineral rights holdings.
- We also look forward to commissioning the diamond recovery, processing and mining operation at Niewejaarskraal, which is a terrace at the same high grade and diamond quality of Saxendrift and is just down the road from Saxendrift.
- We will also evaluate acquisition opportunities which will add production and improve the company's mix of top quality gemstone diamonds in the medium term.

There are no doubt challenges that lie ahead; there always are in mining. These include:

- increasing oil and fuel process,
- increases in the electricity tariff by Eskom, our State utility provider,
- the persistently strong rand-dollar exchange rate – this impacts on our local revenue stream but we cannot control such factors and hence we continue to manage our dollar- and rand-based costs, and show innovation in running this business,
- there is also obviously still some uncertainty in the prognosis for the diamond markets and volatility in world equity markets, but again these are outside our control and we'll manage them as we face them.

In spite of these sort of challenges, we are confident that as before Rockwell will successfully deal with any new impediments – if we can call it that – put in its way and we will show an improved performance in fiscal 2011.

Thank all of you that have taken time to participate in this call and also extend our thanks to all shareholders, management, employees and the Board of Directors for their commitments and support through the very challenging nine-month period that the company successfully navigated from March 1 to November 30, 2009.

Thanks very much.