

Earnings Call Transcript

Rockwell Diamonds Inc.

Quarter 4 Fiscal 2010 Results Call

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CORPORATE PARTICIPANTS

Susie Bell – Investor Relations

John Bristow – President & CEO

Johann Oosthuizen – Financial Manager Operations

Paul Fouche – Financial Manager

Graham Chamberlain – Chief Operating Officer

Jeffrey Brenner – Manager, Diamond Marketing and Sales

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

Operator

Good day, ladies and gentlemen, and welcome to Rockwell Diamonds Inc. Fourth 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.

Susie Bell - Investor Relations

Thanks very much. Good day, everyone, and welcome to the Rockwell Diamonds Fourth 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; Paul Fouche, Financial Manager, Johann Oosthuizen, Financial Manager Operations, Graham Chamberlain, Chief Operating Officer; and Jeffrey Brenner, Manager of Diamond Marketing and Sales.

After the opening remarks with management where we will be reviewing the fourth 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.

John Bristow – Rockwell Diamonds – President & CEO

Good morning, and afternoon, ladies and gentlemen, and thanks Susie for introduction. We would like to get you practicing on good South African names.

Welcome to Rockwell call, in which we will report our results for the past three months and 12 months to February 28, 2010 with the emphasis on the results for the 12 months period of fiscal 2010. I will be assisted on this call by Jeffrey Brenner, our Diamond Marketing and Sales Manager, Desmond Morgan,

Chief Financial Officer is ill, and Johan Oosthuizen and Paul Fouche will assist with financial matters, Graham Chamberlain, our Chief Operating Officer will also participate in the call.

This presentation will cover the company's performance for the 12-month period. Our financial results for that period, ongoing initiatives to improve the performance of the company, the diamond market, our fund raising completed in March 2010, and our objectives for fiscal 2011 and beyond.

Fiscal 2010 was challenging for the international diamond market, diamond producers in general and obviously Rockwell. Rockwell's rapid response and flexibility in dealing with the credit crunch and economic turmoil that the world faced in late 2008, and early 2009 coupled with an improvement in diamond prices in the latter part of 2009 ensured that the company was, however, able to weather the economic storm.

Robust management of costs, increased production from our three operating mines, improved sentiments in the diamond market as indicated in the latter part of last year, and firming of prices ensured that the company returned to a breakeven position in the latter part of the fiscal year. With the added benefits of a successful fundraise, the company has positioned itself to resume its strategy of being an emerging producer and developer, and our key driver being to achieve critical mass and smooth our revenue flow as we go forward.

Based on the continued good diamond prices and positive market trends in the first quarter of fiscal 2011, we are optimistic, but cautious in respect of the outlook for the diamond market going forward, and we will talk to this later.

As difficult as the past 18 months now been, there were number of highlights for the company that helped us manage the economic crisis, and continue while many of our peers fell by the wayside.

These highlights among several other positives bode well for the company moving forward and include the following:

- The good performance of the Saxendrift mine and the high volume rotary-pan plant that we installed in early 2009 and commissioned in the first quarter of fiscal 2010.
- Another highlight is the overall improvements in operational performance at the company's operating mines with Rockwell's production for fiscal 2010, which increased to 2.9 million cubic meters. That is about 6 million tonnes from three operating mines compared to 2.0 million cubic meters from four operations in fiscal 2009.
- We also achieved and sustained lower cash operating costs, and these were at the lower end of our target range of US\$3 to \$3.50 per tonne and we will come back to that point again.
- We also saw regular recovery of stones greater than 10 carats including some exceptional diamonds greater than 100 carats in size from the Saxendrift operation. I should add that we have seen the same sort of statistical population again this year, and our diamond recoveries are on track as before.
- We also in the previous financial year received approximately US\$1.9 million of profit share from our beneficiation agreement with the Steinmetz Diamond Group and this was in spite of a very depressed diamond market.
- Lastly, we completed the successful private placement and fully subscribed rights offer which allowed the company to strengthen its balance sheet, retire short term debt, and reposition itself for organic growth and the potential acquisition of alluvial diamond assets that will add new production and additional revenue to the balance sheet.

If we look at the summary of the financial performance for the past fiscal year to February 28, 2010:

- The company produced 24,900 carats from its operations at Holpan/Klipdam and Saxendrift. We did also have a very small number of carats from Wouterspan, where we ran our grease recovery plants to audit what we call old tailings that had been mined and processed process previously.
- In the fiscal year, we sold 26,500 carats at an average price of US\$1,010 per carat.
- Tender sales of diamonds achieved revenue of \$26.4 million.
- As noted, we had additional income from our profit share, beneficiation agreement with the Steinmetz Group, which recoups another US\$1.9 million.
- Total revenue from diamond sales will be for \$29.8 million.
- Cost of diamond sales was \$22.9 million, and amortization and depletion was \$9.5 million giving us total operating expenses of \$32.4 million.
- At an operating level, we made a loss of \$2.7 million for the year.
- Our net general and administrative expenses amounted to \$8.7 million, net interest expenses were \$1.5 million offset in total by a net tax recovery of \$2.6 million.
- At a fully consolidated level, the company showed a loss of \$7 million or \$0.03 per share for the period as compared to \$13 million loss than the previous financial year, or \$0.05 per share.

Diamonds in inventory at the end of February 28, 2010 totaled 1,909 carats.

In respect to that cash position, the company had cash in the bank of approximately \$2.5 million at February 28, 2010.

The management of costs remains a key focus for the company, and particularly satisfying fiscal 2010 was in spite of the strong Rand/U.S. dollar exchange rate, the average operating cost for the company's three mines decreased to US\$3.11 per tonne from US\$5.23 per tonne in fiscal 2009 and remained at a consistently low level through the financial year.

In the previous earnings call, we highlighted a number of measures aimed at reducing costs. One of these was to investigate in-pit screening at our various operations to reduce the amount of tonnes we transport from our pits to the plants.

As we speak, we are installing two large in-pit trams and screening trommels at Saxendrift. So that we will have a situation with screening of raw ore takes place within a few hundred meters of the mine faces, and we will then only transport screened ore which can be as much as 40% less by way of volume of the original mass mine. This will have a further positive impact on cost and also reduce long-term wear and tear on our mining fleet. We are also looking at in-pit screening options for our Holpan/Klipdam operations, where we mine more shallow surface Rooikoppie deposits, and if we get that right, we will also benefit from reduced cost.

Allied to in-pit screening, we are also looking at ways and means to reduce the impact of summer rainfall on our mining, screening and process procedures particularly again at Holpan and Klipdam. I should note here that during our recent summer months, that is the period January to April of 2010, we experienced exceptionally heavy rainfall and flooding in the Free State and Northern Cape, in other words, in our mining areas and this has impacted negatively on production. We lost by estimates about 1,800 carats of production in the first four months of this year, which had an impact on the bottom line in the fourth

quarter of 2010 and the first quarter of fiscal 2011. However, our production has recovered back to budget levels, in May 2010, we have achieved 3,000 carats of production.

A further cost benefit to the company in fiscal 2011; in other words, going forward beyond the previous financial year will be the reduction of the State Royalty with – or the Royalty Bill, which has been implemented from 1st of March 2010. Rockwell previously paid a 5% royalty on gross revenue on all diamonds mined and sold by the company. From March of this year, the royalty drops to about 3.7%, which although small certainly will represent a savings for the company.

In respect of diamond production and I mentioned this, Rockwell again produced some exceptional stones during fiscal 2010. We recovered nine +30-carat diamonds during the year, including three excellent gemstones larger than 100 carats. These were a 105.62 carat stone, a 120.45 carat stone and a 122.43 carat stone, all from Saxendrift. The 105 carat stone is an exceptional white and that is being cut, and will end up in a 35.88 carat round vivid and we are expecting a quite strong uplift, or profit share, out of that stone once it has been completed and sold by the Steinmetz Group.

In terms of the diamond markets, and Jeffrey Brenner will add to this later, prices received for the company's diamond production increased progressively through the latter part of fiscal 2010, following a sharp decline at the end of 2008 and into early 2009. Critical was that the diamond prices have recovered from the sharp fall of about 50% in the latter part of 2009. The average price received in the fourth quarter of 2010 was US\$1,154 per carat, a substantial increase from the average price of US\$318 per carat in the fourth quarter of fiscal 2009.

Following the encouraging signs of improvements in diamond trade, diamond demand and sales in the latter half of 2009, this trend has continued into 2010. The U.S. diamond market has shown some improvements in demand and sales, there has been a slight improvement in polish prices and demand for rough diamonds and diamond jewelry remains particularly strong in China and India, while the rest of Asia also continues to show resilience and growth.

We are positive about the diamond market and price trends and the fact that general sentiment has improved further this year, that is 2010, is also encouraging. In respect of corporate matters, the company completed private placements in 2009 which resulted in the receipt of approximately \$8.6 million, and we also had a fully subscribed rights offer, which was closed in the first quarter of fiscal 2011.

Together with proceeds from a standby agreement linked to the rights offer, Rockwell received gross funds of \$16.6 million. We had excellent fundraising from our existing shareholders and new strategic partners and I am grateful for this. A portion of these funds have been utilized to ensure that the company was able to address the impact of the credit crunch and remain on a firm financial footing going forward, unlike several of Rockwell's peers, which were unable to survive the recession.

Funds were utilized to strengthen the company's balance sheet, settle short-term debts, pay fees and costs associated with the fundraising process and make operational improvements at the company's existing operations, particularly Saxendrift. We have also commissioned a low-cost mobile trial mining plant at Klipdam Extension and I should point out that this was done timeously and on budget.

The costs applied, or the money/funds applied to strengthening the balance sheet, settle short-term debt, implementing improvements at existing operations, particularly Saxendrift, and getting the Klipdam extension up and running were about \$8.6 million.

The strengthened financial position of the company has also allowed Rockwell to benefit from potential acquisitions of assets that other financially stressed companies have either had to let go or which these companies can no longer develop, and here I refer to the Etruscan, Tirisano or Blue Gum project, which I will also comeback to towards the end of this presentation.

In our letter to shareholders, distributed in-line with our AGM in late October 2009, we presented our plans for the long-term growth and expansion of Rockwell. These plans are on track and to date we have had excellent support from our previous and existing shareholders as well as from the new strategic partners and look forward to taking the company forward with the support of all of these shareholders.

While noting that the challenges of the economic recession impacted and slowed our overall objectives for the company, our plans nevertheless remain in-line with our previously stated intentions.

By way of short-term priorities, the company will maintain flexibility and resourcefulness to ensure that we return to profitability. To achieve this, we continue to actively:

- Manage costs, leverage diamond sales and enhance production at Rockwell's existing operations.
- We will also continue to implement ongoing improvements and reengineering of processing and recovery plants to improve operating efficiencies and get rid of bottlenecks and lower the operating costs.

In the medium-term, it is critical that Rockwell bulk up production and achieve higher, smoother and more predictable revenue flows. To achieve this, the company plans to:

- Re-commission and modernize high-volume processing plant at Wouterspan. The operation which is again has a history of producing top-quality gemstone and is located across the river from Saxendrift. The planning process including engineering work and costings to conclude the design benefits and improve on the high volume Saxendrift plants are complete for Wouterspan.
- We are also looking and working on the acquisition and development of the Tirisano or Blue Gum Project in the Ventersdorp to the west of Johannesburg in South Africa. This area is well known for its alluvial diamond deposits and again, excellent gemstones. In early 2010, the company entered into an agreement to acquire the Tirisano operation subject to various conditions precedent. The higher grades of these deposits, they are typically about three times or at least twice the grade of the Middle Orange River deposits, which is Saxendrift and Wouterspan. The higher grades, good diamond products will allow Rockwell to achieve a more steady state monthly production, once the Tirisano mine is acquired and fully commissioned. And as noted, this would help smooth our revenue and cash flows. We currently have a small and capable team onsite at Tirisano doing planning and prep work. We have submitted the critical Section 11 application to the Department of Minerals and Resources [DMR] for transfer of the minerals rights. We are working with Etruscan and the DMR to progress these important aspects of the project and to also look at an acceptable contractors agreement whereby we can do certain mine work, mine planning, work on the ground, while we await the granting of the Section 11 and transfer the mineral rights.

Overall, in the longer term, the company is committed to building Rockwell into a unique gemstone and diamond producer. To achieve this:

- We will look to increase the rate of evaluation of our existing defined resources and the assessment of the viability of other diamond projects in our extensive portfolio of mineral rights holdings.
- As an example of this, we look forward to doing some work on the Niewejaarskraal Project in the Middle Orange River area downstream of Saxendrift in the course of this year.
- Overall, our intention is to create a situation where Rockwell can become a 10,000 carat per month or a 120,000 carat per annum gemstone diamond producer.

We are well aware that challenges lie ahead of us. Mining is never easy, and problems always tend to raise their heads when least expected. We are dealing and adjusting our operations to deal with:

- Electricity tariffs increases by Eskom, our State Utility.
- We are also obviously mindful of international economic events, which is the recent European bailouts, which could cause further uncertainty and volatility in international markets and potentially impact on the diamond business.
- Obviously, another challenge for us would be to ensure that we can adequately fund the developments of our new projects and ensure the long-term growth and development of the company.

We believe this can be achieved from both a combination of internal cash flow generation, equity and leverage of our unique diamond products.

We have a plan and we will certainly be discussing it further with our shareholders.

I thank all of you that have taken the time to participate in this call. We at Rockwell certainly appreciate the support that we have had from our shareholders, directors, management and employees during the past 18 months and we look forward to meeting all of you again soon to discuss our plans and to ensure that Rockwell keeps on moving forward. Thank you very much.