

## Statement of Chairman and Chief Executive Officer

### BACKGROUND

Sallies underwent a metamorphosis during F2008. At the close of F2007, the company was underfunded; unprofitable; facing potentially fatal litigation; leaking cash from an acquisition which has cost shareholders R100 million to date; without new order mining rights; abandoned by its auditors; embroiled in adversarial industrial relations and managed by teams who, for many years, had not experienced the thrill of achievement or success. These business challenges were exacerbated by power interruptions, astronomical cost inflation and severe skills shortages.

During F2008, as you will read in the following text, concrete, measurable progress has been delivered. Higher dollar prices for acid grade fluorspar and a weaker rand:dollar exchange rate improved the business environment towards the end of F2008, but the operating teams played a significant role in the transformation.

We are certainly far from where we want to be but have an accurate fix on our destination and much of this particular leg of the journey is behind us.

### SYNOPSIS

The year on year turnaround from an operating loss from mining activities of R21.0 million during F2007, to an operating profit from mining activities of R7.8 million during F2008, is not as stark as the improvement in operating financial performance within the year, from a loss of R9.8 million during H1 F2008 to a profit of R17.6 million during H2 F2008. The "bottom line" loss (loss before taxation), at R42.4 million during F2008 (R47.2 million during F2007) is negatively distorted by the notional value applied to share options granted (R10.5 million) and additional financing costs including interest on debentures (R5.2 million). Both of these result from the parlous state of the company at the end of F2007.

### MARKETING

The market for acid grade fluorspar (+97% Calcium Fluoride or CaF<sub>2</sub>) continued to tighten during F2008 and into F2009. This market is relatively small (about 4.5mtpa) and opaque, with over 70% of the trade being either "captive" or via medium-term contracts, both of these types of trade being privately negotiated. The media reported FOB prices ex China (which supplies over 50% of the overall market) of over USD400 per dry metric tonne (dmt) in August 2008. Some observers believe that the Chinese FOB price is a proxy for South African FOB prices. The sustainability of these prices will be largely determined by Chinese marketing strategy and conditions in commodity markets.

Sales of all grades of fluorspar from Witkop increased by 26% to 124 577 dmt in F2008 (F2007: 98 705 dmt). All local sales of fluorspar from Witkop are now priced at export parity. Sales of acid grade fluorspar from Buffalo increased by 19% to 19 065 dmt in F2008 (F2007: 16 088 dmt). The last contract exports at prices below USD180/dmt were made in June 2008 from Witkop and July 2008 from Buffalo. No contracted shipments were delayed by Sallies during F2008, and no discounts were given due to sub specification deliveries.

The calibre of our marketing agents has historically varied between diligent to totally unsatisfactory. We have rationalised marketing into a single agency which specialises in fluorspar and are eagerly awaiting the results of this decision.

A key issue for management right now is the size and duration of contracts for future delivery.

### OPERATIONS

I am pleased to record that no fatal accidents occurred at either operation during the current review period.

#### Witkop

The last fatal accident at Witkop occurred in November 2001 and as of 30 June 2008, 7 172 fatality free shifts had been accumulated. The DIFR at 3.63 is well above target and receiving appropriate managerial attention.

On 3 June 2008, new order mining rights were notarised for Wintershoek (a conversion from the old order rights) and Buffelshoek (a granting of new rights). Registration of these rights is currently in progress.

Two complete reviews of mineral resources and reserves were completed during the year. A summary of the first, as of 31 December, was published in the audited consolidated results for the six months ended 31 December 2007. Total inferred, indicated and measured resources (the latter including probable and undiluted proven reserves) declined negligibly from 70.3mt at a CaF<sub>2</sub> grade of 14.10% at 31 December 2007, to 69.7mt at a CaF<sub>2</sub> grade of 14.09% at 30 June 2008.

Production of all grades of fluorspar at Witkop improved by 10% to 118 137 wet metric tons (wmt) in F2008 (F2007: 107 865 wmt).

During the year, there have been noticeable improvements to the layouts and condition of the pits and haul roads. This bodes well for future mining efficiencies.

## Statement of Chairman and Chief Executive Officer

*(continued)*

### **Buffalo**

No fatal accidents have occurred at this operation since it re-opened in August 2006 and at year end, 1 854 fatality free shifts had been accumulated. The DIFR at Buffalo for F2008 was 0,82.

On 28 March 2008, Buffalo submitted an application for a prospecting permit covering underground resources, to facilitate evaluation of the remaining ore body. We are also attempting to locate historical records which have been lost. On 6 August 2008, Rooiberg Stone, the holder of the old order tailings rights, submitted an application to convert its rights. This action is a precursor to the separation of Buffalo's new order tailings rights from Rooiberg.

The abortive contract hydro-mining in Mill Hill Pit, which was never contemplated in the Competent Person's Report, was terminated in October 2007 after fluorspar output had collapsed to 769 wet metric tons (wmt) for the month.

Between November 2007 and April 2008, about 2 500 wmt per month was produced from mechanically fed, dry tailings from Mill Hill. This material, which was essential to avoid contractual substitution of Buffalo product with Witkop product, which was already achieving higher prices, was depleted, as expected, during May 2008. Because of uncertainty surrounding the availability of adequate power to source feed from dumps 5 and 6, an attempt to extract the high grade sludge at the bottom of Mill Hill Pit was made during May and June 2008. This proved both unreliable and impractical because of contaminants in these tailings. Since July 2008, small scale, in-house hydro-mining of dumps 1 to 4 has generated plant feed.

Acid grade production for F2008 at 25 720 wmt was 8 795 wmt or 52% higher than for F2007.

### **FINANCE**

The cash component of working capital varies widely as shipments take place and payments are made. As of 30 June 2008, net cash on hand was R20.9 million and a R16.0 million facility was available, of which R5.0 million was reserved against foreign exchange contracts.

The rights offer completed on 2 July 2007 raised almost R75 million (before costs of R2.6 million), and increased the number of issued shares from 506 264 000 to 631 181 000. The rights offer completed on 9 May 2008 raised a further R76 million (before costs of R2.4 million), and added 151 483 440 convertible debentures to the capital structure of the company.

During the year, the market capitalisation of Sallies varied between R254 million and R719 million including the convertible debentures issued in May 2008.

The directors requested an audit of the interim results for the six months ended 31 December 2007, despite the fact that this was not a statutory requirement. The auditors complimented the management team on the improvements to its standards of financial record keeping.

### **HUMAN RESOURCES**

Dr Vincent Msibi, who served on the board since 30 June 2006, tragically lost his life on 12 July 2008. Our condolences were passed on to his family and friends and his contributions will be missed by all. Jürgen Kögl will serve on the Sallies board as the representative of African Renaissance Holdings, our black empowerment partners, in the interim.

Dr FJP (Fred) Roux was appointed as non-executive chairman with effect from 1 July 2008. Stakeholders are fortunate indeed to have a mining sage of this calibre at the helm.

I am pleased to be able to report that capable managers are in place in the general management, geology, mining, processing, engineering, finance, human resource and statutory compliance functions. However, shortages occur in the middle management and skilled labour tiers of the organisation.

Management is focused on creating good industrial relations with the aim of securing the industrial peace so vital to our future success. An early positive indicator from this effort is the 2008 wage agreement at Witkop, which was implemented without strike action for the first time since 2002.

As the company hopefully settles down from turbulent, crisis driven management, we must forcefully address skills shortages through in-house training of high potential employees.

## Statement of Chairman and Chief Executive Officer

*(continued)*

### **HONEYWELL**

Honeywell has submitted an alternative claim of USD4.5 million plus interest and costs to the arbitral tribunal (original claim USD6.9 million plus interest and costs). Sallies is opposing this claim and has submitted a counter claim of USD3.8 million plus interest and costs. The final hearing in the matter took place on 27 October 2008. Final post-hearing briefs are to be filed on 15 December 2008 and statements of costs on 17 December 2008. The Arbitral Tribunal intends to declare the proceedings closed upon receipt of the statements of costs. A final decision could be delivered early in 2009.

### **OUTLOOK**

Acid grade fluorspar is used worldwide to produce hydrofluoric acid. Fifty percent of this acid is used to produce refrigerant gases, for which no practical substitute is on the horizon, and a further thirty percent is converted to aluminium tri-fluoride, a vital ingredient of aluminium production. The twenty percent balance is used in niche markets, including a significant (and growing) volume for uranium enrichment and lithium-ion batteries.

Witkop became profitable for the first time in over five years during the current review period. Witkop fluorspar is highly sought after due to its low levels of impurities but it is a high cost producer due to its relatively low in situ grades. The central challenge for operating management is to improve mining efficiencies to a degree which will maintain its current profitability in less favourable market circumstances.

Buffalo significantly reduced its operating losses during the review period. It is almost one year since I stated the intention to complete a strategic review of the Buffalo operation. The Buffalo product contains high levels of phosphorus due to the composition of the tailings from which it is produced. Our technical advisors have to date been unable to suggest practical means to reduce these. There is a market for Buffalo fluorspar, but it is far smaller than the overall market and thus a significant expansion, even assuming that we can technically negotiate power constraints, would not necessarily benefit shareholders. Due to these facts the board of directors announced on 13 October 2008 that the operations of Buffalo would be placed on care and maintenance.

In pursuit of moving the company down the world production cost curve, we are examining the remaining ore resources at Buffalo; trying to permit a high grade fluorspar deposit in Zambia; evaluating the logistics of fluorspar in Mocambique and reviewing grass roots potential in South Africa.

Much of the limited corporate financial capacity at Sallies was absorbed by the two rights offers completed since 2007; crucially important litigation with Honeywell, SARS and others; and overhauling the management information systems. The bulk of this work is now behind us, and we can now focus on corporate opportunities. We enjoy excellent relations with our BEE partners, African Renaissance Holdings, and look forward to finalising certain details of our agreement with them during F2009.

In conclusion, I wish to thank our shareholders and bankers for their patience and support, my fellow directors and the operating teams led by Casper Badenhorst and Gerrit Bleeker for their hard work, and all our other stakeholders, without whom we cannot succeed.



**TG Dale**

*Chairman (until 30 June 2008) and Chief Executive Officer*

Johannesburg  
14 November 2008