

A transcript of a Proactive Investors interview with Kalimantan Gold CEO Rahman Connelly in May 2008. In addition to an update on the company's main sphere's of activity in gold, coal and copper, the interview contains additional material on mining and Indonesia, the market for coal, land restoration, and the benefits of community involvement for both the community and the business.

Kalimantan Gold – Audio Interview Transcript

So, why focus on Indonesia and Kalimantan?

Harry, Indonesia is certainly regarded as one of the most prospective countries in the world, yet it has received very little in the way of exploration expenditure. Notwithstanding the fact that it already has two of the largest copper mines in the world, it's the largest exporter of thermal coal, and a big producer of gold and tin. So it does have that prospectivity and Kalimantan itself, where we are based, has got several gold mines; it's one of the largest coal producing areas of the world and, of course, has a substantial oil and gas industry.

Rahman, what happened with Kalimantan Gold's copper porphyry joint venture with Oxiana, in Central Kalimantan?

Last year Oxiana spent US\$2.5 million drilling 6,000 metres over 16 holes and withdrew, on the basis of their work, as they believed there was not a shallow copper porphyry deposit there.

So what are Kalimantan Gold's plans in Central Kalimantan, now?

First thing we did following Oxiana's departure - as you would expect, we bought in an independent consultant in the form of Dr Peter Pollard, one of the world's leading authorities on copper porphyry deposits; he's worked in just about every major copper project in the world. He came in for ten days, to look at both Kalimantan Gold's own work and Oxiana's programme, and his conclusion is that Oxiana left behind considerable untested potential. In other words, there were some very obvious targets and they were, in fact, not drilled by Oxiana. So, that leaves us in the position now of needing to look for a new partner but, in this case, what we are looking for is a partner that will do a thorough programme that will thoroughly test the prospects - and the view of Dr Peter Pollard is, someone's going to have to spend about US\$10 million to do that. So, it's really getting in a partner with a commitment to do the work to fully test the prospects, Harry. We have been in discussion with a number companies and those discussions are ongoing.

So Rahman, what's happening with the Jelai gold prospect in East Kalimantan?

Harry, as you probably know, that area is originally drilled by Ivanhoe Mines in the late-to-mid 1990s, when they spent some US\$3.5 million. The crown jewel of their work, according to their own people, was the Jelai area. They drilled 4,000 metres over some 26 holes and got some very high intersections. We acquired that area in the middle of last year and have continued drilling where they left off. We've drilled some 3,000 metres and we have been able to replicate their results; for example, we are getting a lot of intersections of 5 and 6 grams of gold, over 5 to 10 metres, and some higher intersections than that. So far, last year, we just had one scout drill rig at work but as of now, we've got three drill rigs going, we've got two scout rigs which are there to identify veins, or shallow mineralisation, and the vector us towards deeper drilling. And so, as of a couple of weeks ago, we started drilling with a 300 metre capable rig and we expect, at depths, to find the bonanza grades we are looking for in an epithermal system such as Jelai. We know from Ivanhoe's work that the veins tend to widen out at depths. So, that's the current programme, and these rigs are working 24 hours a day, seven days a week. Our objective with Jelai is to bring to the market, within 6 months, a JORC inferred resource for gold.

So Rahman, what attracted Kalimantan Gold to coal?

Harry, we had already been working in East Kalimantan, in the Jelai area; we couldn't help but observe all the coal barges coming down the river, stacked with coal, and people started offering concessions, to us. We thought about it for quite some time and then eventually decided, late last year, that coal was something that offered the potential to produce cash flow, in the short-term, because the exploration process is relatively simple compared with copper and gold, and it's something you can be in production with, within 12 to 18 months. So, that was the prime attraction of coal.

Do you want to say anything about the joint venture arrangements with the Mesra Group?

Yeah, another point just before I deal with those, is to say that East Kalimantan produces 60 per cent of Indonesia's thermal coal, and Indonesia is now the largest exporter in the world, for thermal coal. So the areas in which we've picked up these coal areas, are really some of the world's 'hotspots', or epicentres, for coal.

We were very lucky, I think, to link up with the Mesra Group. There are a lot of brokers and owners of coal concessions, out and about in East Kalimantan, and these are not easy people to deal with. But in the Mesra Group we found a company that was already successful with coal, they had already, in the last year, done substantial deals with Korean, Indian and Middle Eastern companies. So we knew they had the expertise to identify and secure coal areas, and we were

are able to attract them to the table by showing them that they can, in fact, make a lot more money if they retain their interests in the coal areas, by way of a share market listing, either in London or in Australia. So, initially, we have a joint venture arrangement which covers five coal concessions and the idea is that, in the future with Mesra, any further areas that they identify will come into our strategic arrangement. So, the arrangement we have with Mesra is that Kalimantan Gold, itself, will retain a 70 per cent interest. GMT Indonesia, who are the contract explorers for Churchill Mining, we are providing with a 5 per cent incentive share arrangement, and Mesra will end up with 25 per cent of the initial issue of shares. But what's particularly attractive about the joint arrangement we've entered into, is that there is no cash payment up front and there are no royalties. One of the problems in East Kalimantan today is because it's a seller's market, people are out there, everybody's combing East Kalimantan looking for coal, so proprietors are asking for substantial sums of up front cash and royalties; and royalties may be okay in today's environment where there are very high margins, but I think some of these arrangements will come apart, once there's a squeeze on coal margins. So, very fortunately, we've avoided that and what Mesra end up with is a 25 per cent interest, and we are also paying them a bonus payment when we make a decision to mine; i.e. we have a JORC resource and arranged finance - when we've decided to mine, we will pay them 25 cents per tonne of JORC resource. So, it's a very attractive deal. It's something that is robust, in the longer term.

Kalimantan Gold has a very strong commitment to social license and, in particular, to capacity building and developing governance with local communities. Is this part of the Kalimantan Gold business model?

Well, absolutely. Firstly it reflects the philosophy of the directors, but it is also something which is entirely pragmatic, simply because this work builds relationships with local people and anywhere where you are mining, but particularly Indonesia, relationships are of the up most importance if you want to be able to take your ore body away. And I might say that there's another aspect of community development which is, that it also opens doors for us. In fact, even obtaining the recent coal joint venture, the fact that we have a commitment to insuring that the local people benefited from the development was, in itself, a big attraction to our local partner. So, it's the philosophy of the directors but it's also something very pragmatic.

What can investors expect from Kalimantan Gold over the next 6 months?

Well Harry, with our Jelai gold, as I said to you earlier we will be bringing in an estimated and inferred resource to the market, within 6 months from now, and we'll be endeavouring to do the same with coal because, as I said, it's a lot simpler process, in terms of exploration. So all our efforts, at the moment, are going into those two projects and we expect to have resources for both of those, within six months. On the copper side, we are in discussions with a number of

companies and during the course of this year we hope to be able to enter into a joint venture arrangement. But importantly, we are continuing to review other areas, to acquire other prospects.

Where do you hope Kalimantan Gold will be in five years time?

Harry, we will be hoping to be a major producer of gold in East Kalimantan, at our Jelai prospect. Also, a large producer of coal and, as I've said to you before, we certainly have a partner that has the potential, on an ongoing basis, to secure excellent areas for coal. In regard to copper, I would like to see an active joint venture partner there, moving towards bankable feasibility. Most importantly, to note that Kalimantan has an active programme of reviewing new areas and we hope to secure a number of those.

So while you are on the line, Rahman, I would like to ask you a few extra questions. Have you any observations about Indonesia in general, what are your thoughts on Indonesia?

Well Harry, Indonesia has been a very difficult place to work, in recent years. Firstly, there's been a lack of a mining law for new projects and there's a lot of conflict between forestry and mining policy - in fact, we've had a forestry led mining policy. The government is addressing both of those issues, we are expecting a new mining law to emerge from parliament in the coming months, and the government has recently announced a package of measures which will enable mining companies to operate in forested areas, subject to compensation. But notwithstanding that, we are already seeing a substantial drift back to Indonesia. People like Churchill Mining that are doing very nicely, thank you; there's Finders Resources ...looking at the larger companies, Oxiana have committed to spend over US\$300 million to develop the Martabe gold project, in Northern Sumatra, and Vale (formerly CRVD), a big Brazilian company has just committed US\$1 billion to a new nickel plant. I just noted yesterday, that Rio has finally come to an agreement with the government on tax arrangements, with regard to a very large nickel project, which will result in the investment of some US\$2 billion. So, there is a drift back to Indonesia, Harry, and I think that's good news.

So, what kind of coal are you prospecting for, and what market is it suitable for?

Harry, we're prospecting for thermal coal and, as you might know, coal power generation is taking over from oil and gas. If you look at the big countries of India and China, 80 per cent of their future power generation is expected to be coal-based. Indonesia, itself, is fast-tracking the development of thermal coal power stations, and even Italy - when I was in Europe recently, I noted that they are expecting their coal power generation to go from 13 per cent, to 33 per cent. So coal, for the foreseeable future, is going to be a large generator of electricity.

Now, if we look at Indonesia, Indonesia is now the largest exporter in the world of thermal coal and East Kalimantan, the area in which we have obtained our five concessions, produces 60 per cent of that, some 80 million tonnes a year. So, it is for thermal electricity, it's medium quality coal, and the demand is as far as your eye can see.

So, what will be your obligations to restore land, after open pit coal mining in Kalimantan?

Yes Harry, all companies are obliged to restore land after open pit mining but in East Kalimantan, it is true to say that a lot of the smaller companies have mined and just walked away. Being a public company, obviously, Kalimantan will comply with the law and I think we will do more than comply with the law. We will reclaim the land and make sure, to the greatest possible extent, that that land is arable. In other words, we may need to add components to that so it can be used for agriculture.

How have local people benefited from Kalimantan Gold's presence?

Firstly to say that, as an explorer, it is pretty unique for an exploration company to actually undertake community development programmes. This usually happens more where the company has moved into, or is about to move into, production. Kalimantan Gold works in 38 villages, both in East and Central Kalimantan - in other words, in proximity to our gold, coal and copper prospects. Our whole focus with community development is capacity building; working with local villages for them to identify their own needs and then assisting them in "how to" fulfill those needs. So, we call it a "hands up" approach, rather than a "handout". In other words we don't do specific projects, we simply help these people to plan for their own needs; and if they can identify their needs and document their needs, then they can relate to the next level of government, then they can relate to other donor agencies. So, that is our approach and, I might say, it's brought the company a lot of kudos and, as I mentioned earlier, opened a lot of doors for us.

Does Kalimantan Gold, plan to role out its social programme in conjunction with each new project?

Yes, absolutely, I mean it's already doing it in relation to copper - in Central Kalimantan we have a full time community development manager, and staff in East Kalimantan that are working with villages in proximity to Jelai - and, of course, we will do the same thing when we identify which of the coal concessions we will be working on, through the mining.

I sometimes get the impression that investors don't give a stuff about social commitment - do you find that to be the case?

Yes, some investors think it's a waste of money but, as I said earlier on, it's both a philosophy of the directors and entirely pragmatic. I mean, you have cases all around the world where mines are shut down because proprietors have failed to engage with local people. A little investment up front can create the social license by which you operate and that social license, in many ways, is as valuable as the ore in the ground. But, in today's world, having a proper programme for local people is also a very important part of getting finance. There are some financial institutions now, that will not provide finance unless you have those programmes in place. And thirdly, in our experience, it opens up opportunities; for example, obtaining our coal areas with the local partner. I think, one of things that attracted the local partner to us, as opposed to anyone else, was that we had a commitment to local people - and bear in mind, he is a local person. So, it's very pragmatic and I think that it delivers far more value than you spend on it