LUCAPA
DIAMOND COMPANY

ASX Announcement 27 May 2019

# 2019 AGM - CHAIRMAN'S ADDRESS

Good afternoon Ladies and Gentlemen.

My name is Miles Kennedy and I am the Non-Executive Chairman of Lucapa Diamond Company Ltd. I welcome you to the 2019 Annual General Meeting and thank you for attending.

With me are my fellow Directors; our CEO Mr Stephen Wetherall, our Chief Operating Officer Mr Nick Selby and Mr Ross Stanley, who is today attending his first Lucapa AGM as both a Director and the Company's major shareholder. Also present is Mr Mark Clements, our Company Secretary.

The formal business of today's meeting is to place before you as shareholders the Company's Annual Financial Report for 2018 along with seven resolutions which I shall deal with in greater detail when we come to each of those resolutions.

Before we consider the formal business, I would ask to take up some of your time to provide an overview of Lucapa's achievements since our last AGM and what 2019 holds in store. In doing so, I would also like to address the frustrating disconnect between those achievements and our share price.

Put simply, Lucapa's goal is to grow as a producer. We want to produce high-value diamonds on a sustainable and profitable basis from our two African diamond mines – Lulo in Angola and our new Mothae mine in the mountainous diamond-rich Kingdom of Lesotho. And while it is yet to be recognised in our share price, we have put in place the foundations to achieve that goal.

As I will outline, we have also put in place plans to accelerate the repayment of loans from our Lulo alluvial mining operations.

And while we have curtailed our exploration efforts at Brooking and Orapa to focus on maximising cash generation from our producing assets, I will also explain why your Board remains convinced that the cost of exploring for the kimberlite mother lode at Lulo remains justified.

Let me briefly run through Lucapa's three main operations and workstreams, starting with Mothae.

Since our last AGM, the Lucapa management team has successfully built, commissioned and commenced commercial production at our new 1.1Mtpa Mothae kimberlite mine. We delivered that at a total cost of circa US$38m, including the original US$9m purchase price for our 70% interest and the pre-production bulk sampling program.

To give that US$38m investment some context in the diamond space:
- It is a fraction of the ~US$250m development cost considered by the project's previous owner, Canada's Lucara Diamond Corp.
- It is also around one-fifth of the US$187m cost borne by global diamond giant Alrosa to develop the Zarya pipe in Russia, which at 1.25Mtpa is a similar sized plant to Mothae.

Despite being in commercial production for less than five months, Mothae has already proven itself to be one of a select few global mines producing large and high-quality diamonds. It has produced what we expected - regular Specials, rare Type IIa whites and fancy coloured gems. Mothae diamonds achieved stunning individual prices of up to US$36,000 per carat in the February commercial tender in Antwerp.

In fact, when I started drafting this address, the only thing missing from Mothae was a "trophy" +100 carat diamond. This duly arrived before the ink dried in the form of a gem-quality 126 carat diamond, recovered last week from one of the supposed lower-margin zones of the kimberlite pipe.

The 126 carat diamond arrived after the production cut-off for the next Mothae tender of circa 7,000 carats, which is scheduled to be concluded in Antwerp within days.

For Mothae to produce such results so early in its mine life is tremendously encouraging considering ore to date has been predominantly sourced from the previously considered lower-margin zones of the Mothae kimberlite pipe.

Let me explain why that has been the case. Under our original mine plan, we had intended to dewater the main southern pit at Mothae in H1 to begin accessing more ore from the higher-margin kimberlite zones that we have been unable to get to because of the water, but which produced the best diamonds during the previous trial mining phases conducted by Lucara. Lucara's trial mining recoveries from these zones included several large Type IIa whites, including a 56 carat gem which sold for US$2.1m, along with a broken 254 carat boart stone.

Due to the better-than-expected efficiency of the new Mothae plant we alluded to in Q1, the management team brought forward plant modifications to increase diamond production.

Because increases in plant throughput require a commensurate increase in water consumption, a decision was taken to preserve the water required in the southern pit until the completion of the main 500,000$m^3$ Dam 4 wall in H2.

Had we not taken this decision regarding the dewatering of the southern pit, at the expanded capacity, we would have increased the risk of running low on water at Mothae later this year, and possibly being forced to either shut or slow down the mine until the rains returned. It is an example of where Lucapa has avoided the temptation of a short-term sugar fix to ensure the Company's production growth strategy is not compromised.

The higher-margin diamond zones that lie beneath the water in the southern pit, which will be accessed in H2, constitute about 77% of the total ore currently planned to be mined from the open pit. As such, Lucapa will wait until mining has transitioned to these zones properly in Q3 before updating its operational guidance and mine plan for Mothae.

I turn now to our flagship Lulo diamond mine in Angola, where I will touch on a similar theme.

Unlike Mothae, in which Lucapa has a controlling 70% stake, Lucapa has a 40% interest in the Lulo alluvial diamond mining company *Sociedade Mineira Do Lulo* ("SML"). As such, SML is treated as an associate under International Financial Reporting Standards and not consolidated into Lucapa's accounts.

Thus, when Lulo diamonds are sold this represents revenue for the associate mining company SML - not its 40% owner Lucapa. Those diamond sales fund the operating and alluvial exploration costs of a mine which now employs close to 400 staff and contractors – and pays taxes on its profits under Angolan law.

This accounting treatment has caused some confusion among Lucapa shareholders regarding SML's cash position. And in particular, how the free cash generated by SML – over and above its operating costs and taxes - is utilised.

To date, SML has declared US$17m of its free cash to Lucapa in the form of pro-rata distributions and repayments on the loans advanced by Lucapa over the past decade to explore for alluvials and establish the mining operations. Lucapa has repatriated the bulk of those returns, and used the balance to fund the Lulo kimberlite exploration program, which I will go into in detail further on.

Like Mothae, Lulo is currently preparing another run of mine diamond sale which is expected to leave SML in a very strong cash position. And like the upcoming Mothae tender, the Lulo sale will exclude some high-value diamonds held in inventory that missed the diamond export cut-off dates, including the 130 carat gem-quality diamond recovered earlier this month.

For Lucapa, one option would have been to repatriate as much of SML's free cash flow as possible to head office. Afterall, Lucapa is contractually entitled to 70% of the free cash returned to the Lulo partners in the form of loan repayments and pro-rata distributions.

Let me explain why we chose not to do so.

As we foreshadowed earlier this year, SML is expanding production and alluvial exploration at Lulo to recover and sell even more of the world's highest US$ per carat alluvial diamonds.

This expansion will comprise additional mining fleet and a third operating shift on the 1.1Mtpa Lulo plant, which will then operate on a 24/7 basis.

It will cost circa US$12m, inclusive of the usual fleet replacement, which will be self-funded by SML. Thus, all the Lulo partners will contribute to this expansion.

SML achieved plant throughput of 285,000 bulk cubic metres (bcm) in 2018, an annual record. The additional investment will enable SML to increase that throughput to approximately 450,000 bcm on an annualised basis in 2020. That is an increase of more than 50%.

The rationale for Lucapa in supporting the self-funded expansion of Lulo is simple: increased diamond production will generate more free cash for SML, resulting in higher and earlier returns to Lucapa and its Lulo partners.

Your Board believes this represents the best way to accelerate the repayment to Lucapa of the remaining ~US$30 million in investment loans outstanding from SML. In the interests of providing perspective, that outstanding loan balance is well in excess of the corporate borrowings taken on by Lucapa to build Mothae.

Two other factors reinforced our confidence in expanding diamond production at Lulo.

Firstly, in March, we announced a 90% increase in Lulo JORC resource carats, at a higher average value per carat of US$1,420. We expect to continue to grow this resource.

Secondly, the landmark diamond sector reforms introduced in Angola since our last AGM provide further justification. As you are aware, these reforms resulted in Lulo diamonds being the first Angolan production sold via international tender in Luanda earlier this year. The exceptional prices achieved in that historic tender provide proof that the new international sales channels will enable SML to generate even higher prices for its Lulo production.

Expanding diamond production at Lulo will also assist our efforts to move along the diamond-value chain into the cutting and polishing of select Special diamonds. While the absence of any firm announcements on this strategy may well create the impression we have not made any progress, the reality is we are well advanced and on track to deliver this strategy this year.

I would now like to touch on our third major asset and workstream, the Lulo kimberlite exploration program.

Since our last AGM, we have secured an extension to our Lulo kimberlite exploration licence through to April 2023. This was courtesy of a new Mineral Investment Contract, the issuance of which is further evidence of the positive changes taking place in Angola's diamond sector.

Under the terms of the kimberlite licence, Lucapa is obliged to continue funding the Lulo kimberlite exploration workstreams, with that funding treated as an investment loan which is repayable to Lucapa when and if a kimberlite mine is discovered and developed. Very much the same as the alluvial structure with SML.

As I touched on earlier in my address, Lucapa draws on its alluvial mining returns from SML as a source of funding for this kimberlite exploration work.

Of the most recent US$5.6 million in returns declared to Lucapa from SML's 2017 earnings, we have repatriated US$2.1m to Australia. We have allocated the balance to the kimberlite exploration program.

Such a funding arrangement does not sit comfortably with all of our 6,000 Lucapa shareholders. Understandably, there are some who believe we should stick to our two high-value diamond mines and reconsider the kimberlite exploration.

Indeed, some shareholders are of the view that despite spending many years and many millions of dollars on our kimberlite exploration program, we are no closer to finding the mother lode at Lulo.

We hear that, loud and clear. But as someone who has spent decades in the diamond industry, I am firmly of the belief that we should continue our kimberlite exploration for the duration of the licence we have been granted.

To me, the main game in Angola for many years has been to find the kimberlite diamond pipe or pipes which, about 100 million years ago, erupted within our Lulo concession, and in doing so shed the world's most valuable alluvial diamonds down into the terraces we mine today.

And while kimberlite exploration can by nature be painstakingly slow, I am equally of the view that we are closer than ever to finding the mother lode at Lulo.

Let me explain what my confidence is based on:

- We already know we have the diamonds at Lulo – the most valuable alluvial diamonds in the world no less.
- We already know we have the kimberlites at Lulo – we confirmed the existence of more than 70 kimberlites in our 2018 drilling program alone.
- We know our kimberlites at Lulo are diamond-bearing – we have already identified several diamondiferous kimberlites.

And just as importantly, I believe we have the plan to find the mother lode. As we have alluded to, we recently conducted a detailed technical review of all our kimberlite results and data. Along with our own geological team, this review, conducted in Cape Town over a period of three days, included input from external experts - some of the world's most knowledgeable and independent diamond consultants.

As we speak, we are finalising with our Lulo partners the follow-up kimberlite exploration program based on our results and the outcomes of that Cape Town review. Some of the main workstreams involve bulk sampling priority kimberlites as well as gravel from tributaries that feed from high priority zones and into our main high-value alluvial mining blocks. We too are frustrated with the laboratory turn-around times, which is why we are also participating in the development of new technologies which have the potential to detect the diamond pathfinders we are looking for much earlier than conventional mineral chemistry analysis.

It is also important not to lose sight of the size of the prize we are chasing here.

The alluvial diamonds we have recovered to date at Lulo have sold for an average of around US$2,000 per carat.

In comparison, the Catoca kimberlite mine operated by Russian giant Alrosa just 150km from Lulo in Angola generates annual sales of something like US$600m from diamonds with an average price per carat of just US$100-115.

There are no silver bullets in the kimberlite exploration game either. But the patient and methodical approach adopted by our exploration team is narrowing down and confining the search areas of our quest. It may take us another couple of years, but I am more confident than ever that we can indeed find the diamond source at Lulo. And for the reasons I have outlined, that has the potential to be a discovery of huge wealth.

We can certainly look at funding alternatives for this program, but now is not the time to deviate from that path or to give up.

By my calculation, our share price represents a discount of some 20% to our net asset value, despite the unique position we have forged for ourselves in the global diamond sector.

Which is why one of the questions most frequently asked of me as Lucapa's Chairman is: What is wrong? The answer is that nothing is wrong.

There are two well-known stock market adages. One is: *"The market always gets it right."*

The other, which has shades of our recent Federal election, is: *"When the market gets it wrong, it gets it horribly wrong."*

With the greatest respect, I would suggest that in the case of Lucapa, the latter adage is applicable.
I am about to end, but lastly, I want to thank our teams and partners – all of them - here in Perth, in Angola and Lesotho, who continue to work tirelessly to deliver on our growth strategy. Thank you also to our loyal shareholders, including those of you who have supported us for many years. We are grateful for your patience and your continued support.

As I hope I have explained, there is no let-up in our desire, drive and determination to deliver results to our shareholders. Please stay the course.

I now move to the business of the day.

**MILES KENNEDY**
**CHAIRMAN**

**Competent Person's Statement**

Information included in this announcement that relates to exploration results and resource estimates is based on and fairly represents information and supporting documentation prepared and compiled by Richard Price MAusIMM who is a Member of the Australasian Institute of Mining and Metallurgy. Mr Price is an employee of Lucapa Diamond Company Limited. Mr Price has sufficient experience which is relevant to the style of mineralisation and type of deposit under consideration and to the activity which he is undertaking to qualify as a Competent Person as defined in the 2012 Edition of the Australasian Code for Reporting Exploration Results, Mineral Resources and Ore Reserves. Mr Price consents to the inclusion in the announcement of the matters based on this information in the form and context in which it appears.

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