



## PROJECT REPORT

### Appendix 5B for September 2008 Quarter

#### The New Force in Iron Ore

#### Current Project Highlights:

- Cash at end September was A\$624 million – an increase of A\$432 million on the previous quarter - with funds flowing from a number of sources being a A\$140 million preference share issue, A\$302 million equivalent in sales prepayments (assumed converted to AUD on receipt), A\$201 million from leasing and sales receipts of A\$645 million.
- As at end September Fortescue had loaded 8.536 million tonnes of product onto 52 ships dispatched from Fortescue’s Herb Elliott port facility.
- Fortescue exploration and operations teams completed a new Reserve Estimate for Cloudbreak and Christmas Creek with an increase of 54% to 1.625 billion tonnes.
- Rail network in full operation with ballast “superlift” completed enabling ore wagons to run at full 160 tonnes (gross) loads and the train speeds to achieve scheduled rates of up to 90kms per hour.
- Herb Elliott Port now fully commissioned for 45 million tonnes per annum “Mta” run rate with the in-load and out-load systems operating well and work on optimisation out to 55 Mta near completion.
- The mine operations with 5 pits now working and additional contractors assisting with overburden removal during the quarter. All but one of the 14 surface miners have been commissioned and are in full operations with the final machine soon to be operational.
- High Court of Australia rejected an appeal by BHPB regarding Trade Practice barriers to third party access to rail infrastructure. Costs were awarded in Fortescue’s favour.



## CORPORATE

**Cash at end of  
Quarter was  
A\$624 million**

**- an Increase of  
A\$432 million  
from the June  
quarter**

**Preference  
Share Issue  
raises A\$140  
million**

**Prepayment  
Receipts raise  
US\$245 million  
with balance of  
US\$25 million  
expected over  
coming months.**

The September quarter covers a three month period of operations with the company in gradual ramp up mode. It is likely to be the last quarter that Fortescue will lodge with the ASX as an Exploration / Development entity. Going forward, Fortescue will make application to ASX Limited to be recognised as a Mine Production company.

Cash at the end of the September quarter was A\$624 million. The key contributors of cash inflow for the period were;

1. total sales revenue of A\$645 million, comprising A\$488 million of product sales and A\$157 million of gross shipping revenue, includes gross product receipts of c.A\$90 per tonne that were converted from USD to AUD at average \$0.87. The cash statement shows actual cash received during the quarter, however revenue from some shipments towards the end of September will be recorded under debtors as cash has not yet been received from confirmed bank letters of credit;
2. the issue of a A\$140 million preference share tranche following the EGM approval for a change in constitution to allow for such issues;
3. the receipt of US\$245 million in sales prepayments from Chinese customers as part of a total contracted sum of US\$270 million with the balance of funds expected over the next quarter (note for accounting purposes the cash statement assumes prepayments are converted to AUD at time of receipt however the majority of these proceeds are still held in USD); and
4. leasing receipts of A\$201 million were received during the period as Fortescue continued its operating lease program.

The receipt of the above funding is part of the financing for the expansion of the current infrastructure platform from the optimised 55 million tonne per annum "Mta" capacity to the next targeted stage of 80 Mta. The balance of expansion funds will come from internal cash flow with the works project scheduled to be completed by end calendar 2009.

In addition to the cash at bank, there was also \$91 million held as security backed deposits to support bank guarantees for certain suppliers and service providers.



***Depreciation of AUD to bring benefits to the bottom line.***

It should be noted that Fortescue does not have any hedging over its USD sales receipts so it has benefited strongly from the recent fall in the Australian dollar. Fortescue receives all its product sales and shipping sales revenue in USD so the AUD fall of c.25% over the past few months has added significantly to the company's bottom line.

To put this in context, whilst all revenue is contracted in USD, only some 65% of operating expenses are paid in AUD and under the expansion program, approximately 75% of the scheduled capex will be made in AUD.

The expansion project to 80 million tonnes per annum is the first stage under the Heng Shan project that will ultimately see the infrastructure platform move to 160 Mta over future years as the market conditions warrant.

## OPERATIONS

The main production statistics for the operation are summarised below. It is important to note that the operation is still in ramp up mode as the first stage run rate of 45 Mta is expected to be achieved from late 2008. The run rate is then expected to step up to 55Mta as from April 2009 onwards as the optimised product handling system is completed.

### Mining

The mining team have been active over the quarter with a number of key achievements being:

***Mining Team now in Five Pits***

- A fifth mining area "Brampton Pit" was opened up during the quarter with its higher grade material being an important part of the blending operation at Cloudbreak;

***Two contractors now assisting with Overburden Removal***

- Additional contractors have been deployed to assist in overburden removal with Brierty Contractors commencing in August and more recently NRW Contractors are also providing services. Over the quarter c.7.8 million bcm's ("bulk cubic metres") of overburden material was removed;



***Mine Village  
expanded to  
take over 1,300  
Personnel***

- Fortescue's complement of mining operators is now over 600 people. Together with maintenance and service personnel and direct administration staff, the total number of employees in the mining team now exceeds 950;
- The village at Cloudbreak has been expanded to accommodate over 1,300 personnel which provides a base for both operations and some members of the construction teams;
- Fortescue has also taken delivery of all of its mobile mining fleet to provide for the 45 Mta scale operations; and
- On the ore mining side, 13 surface miners have now been commissioned with the last machine close to final commissioning stage. Over the quarter c.6.9 million tonnes of ore was mined.

**Rail**

The rail team of 95 people is now fully operational with 429 journeys made to date and several key milestones achieved during the quarter:

***429 Rail  
journeys to date***

- The ballast "superlift" has now been completed which allows for the full loading of each ore wagon to 160 tonnes (gross) capacity and train speed to be unimpeded up to 90 km per hour;
- The cycle time for each train journey is now at 18.5 hrs which is the targeted rate for operations. An additional 160 ore wagons from the same manufacturer have been ordered and will arrive on site this quarter to enable the train size to be optimised at 240 wagons per consist;
- Ultrasonic testing by an independent party of the entire rail line was completed during the period with no defects found. The steel for the Cloudbreak to Christmas Creek line has been ordered from the same manufacturer; and
- Regular testing of the rail wagons covering both performance criteria and material fatigue continues to highlight the superior performance of the rolling stock.

***Rail track  
"Superlift"  
completed with  
trains now able  
to run at Full  
Load Capacity  
and Full Speed***



## **Port & Shipping**

The port team has achieved a number of important outcomes during the quarter being:

### ***52 Vessels loaded and dispatched from Port as at end Sept 2008***

- 52 shipments of product have departed the Herb Elliott port as at the end of September carrying a total of 8,536,837 tonnes of ore;
- The shipments have been spread across a range of customers covering some 28 mills in China;
- Under Fortescue's sales terms, it receives 95% of the contracted cargo value and 100% of the shipping value (if Fortescue has organised the vessel) via a Bank letter of credit "LC". The LC is confirmed and opened prior to loading the vessel. The LC is then drawn after the presentation of the Bill of Lading following the vessel's departure and 95% of the cargo value and 100% of the shipping value is paid within a maximum of 14 days. The balance of 5% of the cargo value is received after the product has been received at the destination port and certified within specification;

### ***Port Optimisation to 55Mta nearing Completion***

- The wharf optimisation work is nearing completion with the marine structures for the second berth now in place and the prefabricated decking being laid along the length of the wharf. There will be a short wharf shut down in the near future as the ship loader track is extended along the second berth to enable a fully traversing loading system; and
- The port team of some 70 people is now at its targeted size with all employees now residential within the Hedland area and strongly engaged in community programs such as various emergency response groups and the recent Blackrock Stakes fund raising event.

## **MARKETING**

All shipments delivered to customers have been accepted and there have been no unfilled available loading slots at the Herb Elliott Port. In regards to the marketing strategy of the company there are several points that should be noted in the context of the market in China.



***Fortescue  
Marketing  
strategy based  
on technical  
benefits and  
“value in use”  
advantages***

- Fortescue has deliberately targeted the top and mid tier mills in China based on a strategy of dealing directly with the customer rather than through commodity traders;
- Fortescue has conducted extensive technical work with its customers to ensure the product shows clear benefits including cost advantages through the steel making process;
- Fortescue has not been producing lump product to date which is seen as a positive thing in the current tighter market given the premium that lump is currently priced at under the benchmark system. Conversely, Fortescue fines are very efficient in the production process which is appealing to many of our customers who are looking to optimise the “value in use” of their raw material feed stock; and
- The Chinese market’s motivation to encourage the emergence of Fortescue as a strong new alternative seaborne supplier of iron ore has gained further momentum in the last quarter. A recent attempt by one of the major seaborne suppliers to increase benchmark prices mid season, and ongoing concerns within the Chinese market over the proposed merger of BHPB and Rio have caused many of our customers to reconfirm to us the commitment of the Chinese market to the ongoing emergence of a fourth major seaborne supplier.

## **METALLURGY**

***Product  
deliveries at  
Targeted  
Specifications***

The key activity of the metallurgy team over the period was to ensure that the product quality from mine to customer was meeting contract specifications. As at end September, over 8.5 million tonnes of product had been exported and the average Fe grade was on specification. To date Fortescue has only sold fines as the lump circuit at the mine site will not be operational until the end of 2008.

The desands plant at the mine site is also expected to be completed at the end of this current quarter which will then enable further pits areas to be opened up as those sites with higher alumina require the ultra fines to be washed through the desand plant to bring the Al<sub>2</sub>O<sub>3</sub> contaminant level down to the targeted < 2%.



## TENEMENT PORTFOLIO

**Total Tenement Portfolio now at over 105,800 km<sup>2</sup>**

### **West Australian tenure footprint**

Fortescue's Western Australia tenure footprint (including joint venture arrangements and tenements subject to agreements) currently stands at about 69,000 km<sup>2</sup>, an increase of about 11,700 km<sup>2</sup> from that last reported. These holdings are comprised of pending and granted exploration licences being principally for the purpose of iron ore exploration in the Pilbara region. The great majority of the tenements and applications are 100% owned by Fortescue.

During September, Fortescue's subsidiary The Pilbara Infrastructure Pty Ltd applied for three miscellaneous licences to facilitate some preliminary investigation into port infrastructure options along the Pilbara coast line.

### **New offshore exploration licence applications**

During the reporting period, Fortescue applied for a suite of exploration licences off the northern Pilbara coast. The licence applications cover an area of approximately 11,200 km<sup>2</sup> and are for the purposes of exploration for offshore accumulations of detrital iron mineralisation.

### **New Zealand**

Since the last reporting period, Fortescue has made a number of new tenure applications in New Zealand. To date Fortescue has applied for approximately 25,600 km<sup>2</sup> of exploration and prospecting permits in New Zealand principally for iron sands exploration.

## EXPLORATION AND METALLURGY

**Major Increase in Reserve Estimate to 1.625 billion tonnes.**

### **Cloudbreak & Christmas Creek**

During the quarter the team produced a new Reserve Estimate for the Cloudbreak and Christmas Creek deposits. The result was a major increase of 54% to a new Reserve estimate of 1.625 billion tonnes. The detail of the Reserve study was released to the market on 19 September 2008 detailing the split between probable and proved reserve as 1,482 million tonnes and 143 million tonnes respectively.



***Reserve Study  
draws on mining  
experience and  
revised pit  
modelling***

The study has been concluded following the review of further drilling and assay results, more detailed pit modelling and additional metallurgical testwork. The additional information brought about an increase of approximately 474 Mt in the Measured and Indicated Resource to a combined total of 1,855 Mt for Cloudbreak and Christmas Creek (Feb 2006 Christmas Creek and March 2006 Cloudbreak Resource models).

Fortescue was also been able to incorporate into the study a greater understanding of its mining methodology, given it has been operating for over 6 months. A number of variables used in the previous (2006) mine study have been better defined given the experience of actual operations, where over 8.5 Mt of product had been shipped as at end September 08.

**Solomon (100% Fortescue)**

***Continuing  
Exploration at  
Solomon  
Tenements.***

The main Exploration focus continues to be on the Solomon area with 4 RC drilling rigs and 2 diamond drilling rigs working on the site throughout the quarter. Infill drilling to a 200 x 50 m grid has been completed at the Valley of the Kings and Valley of the Queens sections of the CID deposit. It is expected that this spacing will be sufficient to support estimation of Indicated Resources. This will be confirmed when all assays are available and appropriate geostatistics and validation are completed. Part of the Valley of the Kings area is being drilled out to a spacing which is expected to support an estimation of Measured Resources.

During the quarter the Brockman Formation-hosted mineralisation at the Firetail prospect was drilled out on a nominal 200 x 100 m grid. It is expected that this will support an estimate of Inferred Resources which is expected to be completed during the coming quarter.

As the infill programs draw to a close, the rigs are being re-allocated to testing of other targets in the Solomon area and targets further afield. Several targets for CID, DID and BID have been identified and are ready to be tested.



***Boasteel JV  
focuses on the  
2<sup>nd</sup> stage drilling  
campaign for  
Glacier Valley***

**Glacier Valley (Boasteel earning up to a 50% interest).**

Phase One of the drill testing of this magnetite project was completed in late January. Drilling on the Darby prospect has intersected strongly magnetic BIF up to 400m thick and open at depths of greater than 300m. Davis Tube Testing has given very positive results producing a magnetite concentrate of 67 to 69% Fe comparable to or better than other major Australian magnetite projects.

Phase Two is a more intensive RC drilling program intended to lead to an estimate of Inferred Resources. It commenced in June and is now complete with 9,187 metres drilled. Assays from this drilling are being received and appear to be in line with results from Phase One. Diamond drilling commenced early in August. We are presently drilling the third hole in a four hole - 1320 metre program, which is expected to be completed in the second half of November.

**FORTESCUE  
METALS GROUP  
LTD**



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# Appendix 5B

## Mining exploration entity quarterly report

Introduced 1/7/96. Origin: Appendix 8. Amended 1/7/97, 1/7/98, 30/9/2001.

Name of entity

**FORTESCUE METALS GROUP LTD**

ABN

**57 002 594 872**

Quarter ended

**30 September 2008**

### Consolidated statement of cash flows

Cash flows related to operating activities	Current quarter \$A000	Year to date (3 months) \$A000
<b>1.1</b> Receipts from product sales and related debtors	488,203	488,203
Receipts from shipping	157,710	157,710
<b>1.2</b> Payments for		
(a) exploration and evaluation	(5,285)	(5,285)
(b) development	(423,235)	(423,235)
(c) production	(184,829)	(184,829)
(d) administration	(7,135)	(7,135)
(f) Shipping	(132,953)	(132,953)
(g) Government royalty	(6,581)	(6,581)
<b>1.3</b> Dividends received		
<b>1.4</b> Interest and other items of a similar nature received	4,718	4,718
<b>1.5</b> Interest and other costs of finance paid	(118,150)	(118,150)
<b>1.6</b> Income taxes paid		
<b>1.7</b> Other		
<b>Net Operating Cash Flows</b>	<b>(227,537)</b>	<b>(227,537)</b>
<b>Cash flows related to investing activities</b>		
<b>1.8</b> Payment for purchases of:		
(a) prospects		
(b) equity investments		
(c) other fixed assets		
<b>1.9</b> Proceeds from sale of:		
(a) prospects		
(b) equity investments		
(c) other fixed assets	201,580	201,580
<b>1.11</b> Loan repaid by other entities		
<b>1.12</b> Other		
<b>Net investing cash flows</b>	<b>201,580</b>	<b>201,580</b>
<b>1.13</b> Total operating and investing cash flows (carried forward)	<b>(25,957)</b>	<b>(25,957)</b>

**Appendix 5B**  
**Mining exploration entity quarterly report**

1.13	Total operating and investing cash flows (brought forward)	<b>(25,957)</b>	<b>(25,957)</b>
	<b>Cash flows related to financing activities</b>		
1.14	Proceeds from issues of ordinary shares, options, etc	940	940
1.15	Proceeds from issue of preference shares	140,000	140,000
1.16	Proceeds from borrowings		
1.17	Repayment of borrowings		
1.18	Other: Transaction Costs		
1.19	Other: Deposits Received	302,838	302,838
	<b>Net financing cash flows</b>	<b>443,778</b>	<b>443,778</b>
	<b>Net increase (decrease) in cash held</b>	<b>417,821</b>	<b>417,821</b>
1.20	Cash at beginning of quarter/year to date	<b>192,237</b>	<b>192,237</b>
1.21	Exchange rate adjustments to item 1.20	14,018	14,018
1.22	<b>Cash at end of quarter</b>	<b>624,076</b>	<b>624,076</b>

**Payments to directors of the entity and associates of the directors**

**Payments to related entities of the entity and associates of the related entities**

		Current quarter \$A000
1.23	Aggregate amount of payments to the parties included in item 1.2	513
1.24	Aggregate amount of loans to the parties included in item 1.10	-

1.25 Explanation necessary for an understanding of the transactions

**Non-cash financing and investing activities**

2.1 Details of financing and investing transactions which have had a material effect on consolidated assets and liabilities but did not involve cash flows

N/A

2.2 Details of outlays made by other entities to establish or increase their share in projects in which the reporting entity has an interest

N/A

**Financing facilities available**

*Add notes as necessary for an understanding of the position.*

		Amount available \$A	Amount used \$A
3.1	Loan facilities	-	-
3.2	Credit standby arrangements	-	-

**Appendix 5B**  
**Mining exploration entity quarterly report**

**Estimated cash outflows for next quarter**

		\$A000
4.1	Exploration and evaluation	3,000
4.2	Development	298,000
<b>Total</b>		<b>301,000</b>

**Reconciliation of cash**

Reconciliation of cash at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts is as follows.	Current quarter \$A000	Previous quarter \$A000
5.1 Cash on hand and at bank	<b>624,076</b>	<b>192,237</b>
5.2 Deposits at call	-	-
5.3 Bank overdraft	-	-
5.4 Bill	-	-
<b>Total: cash at end of quarter (item 1.22)</b>	<b>624,076</b>	<b>192,237</b>

**Changes in interests in mining tenements**

	Tenement reference	Nature of interest	Interest at beginning of quarter	Interest at end of quarter
6.1	Interests in mining tenements relinquished, reduced or lapsed			
6.2	Interests in mining tenements acquired or increased	E 47/1532 E 08/1831	Nil Nil	100% 100%

**Issued and quoted securities at end of current quarter**

*Description includes rate of interest and any redemption or conversion rights together with prices and dates.*

		Total number	Number quoted	Issue price per security	Amount paid up per security
7.1	<b>Preference securities</b> <i>(description)</i>	1,400	1,400	\$100,000	\$100,000
7.2	Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions	1,400	1,400	\$100,000	\$100,000
7.3	<b>*Ordinary securities</b>	2,806,857,510	2,806,857,510	N/A	N/A
7.4	Changes during quarter (a) Increases Options exercised Options exercised Options exercised  (b) Decreases through returns of capital, buy-backs	268,750 2,200,000 25,000  -	268,750 2,200,000 25,000  -	703 cents 267 cents 569 cents  -	703 cents 267 cents 569 cents  -
7.5	<b>*Convertible debt securities</b>				
7.6	Changes during quarter (a) Increases through issues (b) Decreases through securities matured, converted				
7.7	<b>Options</b>  FMGAW	8,243,380 2,656,250 3,767,030	Nil Nil Nil	<i>Exercise price</i> 26.7 cents 56.9 cents 70.3 cents	<i>Expiry date</i> 31 Dec 2009 25 Jan 2011 01 Jun 2011
7.8	Issued during quarter				
7.9	Exercised during quarter	268,750 2,200,000 25,000	268,750 2,200,000 25,000	703 cents 267 cents 569 cents	703 cents 267 cents 569 cents
7.10	Expired during quarter				
7.11	<b>Debentures</b> <i>(totals only)</i>	N/A	N/A		
7.12	<b>Unsecured notes</b> <i>(totals only)</i>	N/A	N/A		

## **Compliance statement**

- 1 This statement has been prepared under accounting policies which comply with accounting standards as defined in the Corporations Act or other standards acceptable to ASX (see note 4).
- 2 This statement does give a true and fair view of the matters disclosed.

Sign here: ..... Date: XX October 2008  
Print name: **CHRISTOPHER J CATLOW**  
(Chief Financial Officer)

## **Notes**

- 1 The quarterly report provides a basis for informing the market how the entity's activities have been financed for the past quarter and the effect on its cash position. An entity wanting to disclose additional information is encouraged to do so, in a note or notes attached to this report.
- 2 The "Nature of interest" (items 6.1 and 6.2) includes options in respect of interests in mining tenements acquired, exercised or lapsed during the reporting period. If the entity is involved in a joint venture agreement and there are conditions precedent which will change its percentage interest in a mining tenement, it should disclose the change of percentage interest and conditions precedent in the list required for items 6.1 and 6.2.
- 3 **Issued and quoted securities** The issue price and amount paid up is not required in items 7.1 and 7.3 for fully paid securities.
- 4 The definitions in, and provisions of, *AASB 1022: Accounting for Extractive Industries* and *AASB 1026: Statement of Cash Flows* apply to this report.
- 5 **Accounting Standards** ASX will accept, for example, the use of International Accounting Standards for foreign entities. If the standards used do not address a topic, the Australian standard on that topic (if any) must be complied with.

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