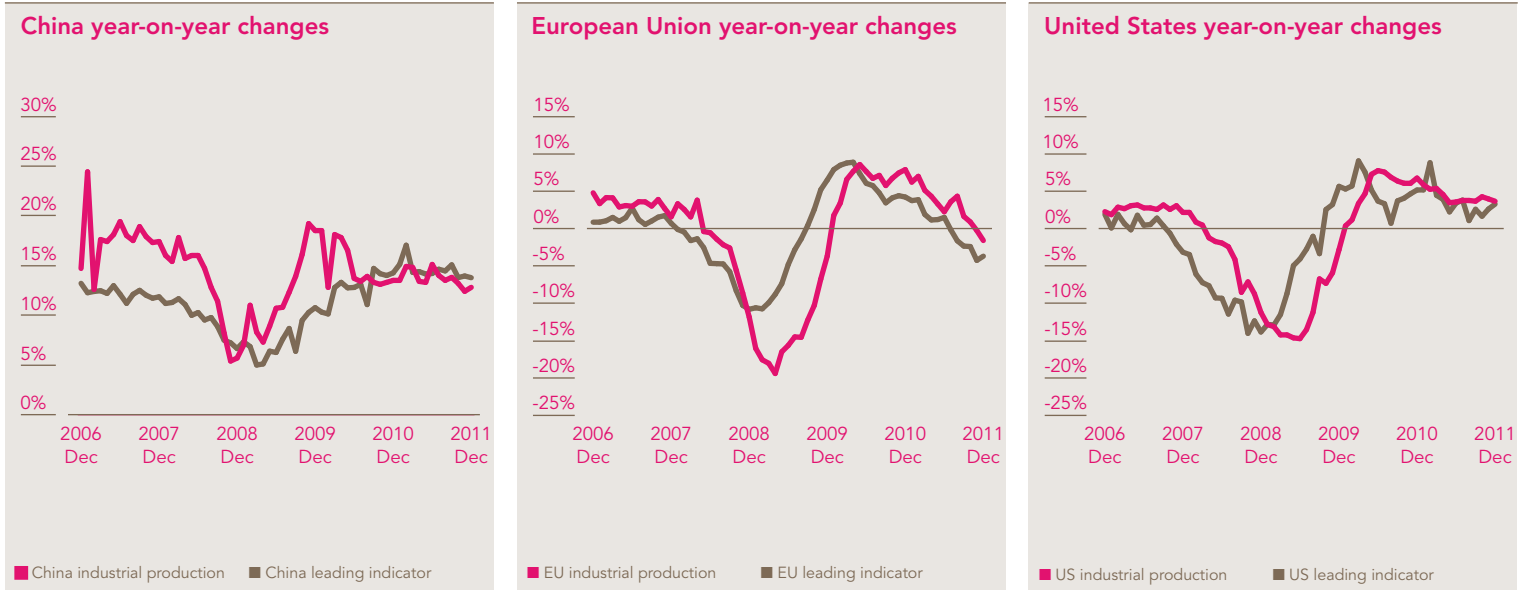


Market outlook



Markets

Global demand for commodities remained strong during 2011 and is continuing to grow into 2012, despite mixed economic growth across the major markets. Demand for commodities is closely correlated with global economic growth and in particular, industrial production.

Fast-growing economies, including China and India, experienced high inflation due to the combination of elevated commodity prices and domestic constraints such as tightening labour markets or insufficient physical infrastructure. Growth in these markets is tempered by government actions in response to inflationary pressures, but rates of economic growth and demand for commodities are expected to remain robust. Overall the outlook for the global economy presents a picture of moderate growth for the coming year.

In 2011, Chinese industrial production maintained its strong growth trajectory, despite fears of a drop in export demand. The People's Bank of China began to ease monetary policy as inflation receded and economic growth receded from the 10% average annual growth rate of the last few years. Government initiatives and continued domestic demand will mitigate the slowdown being witnessed in the high-end Chinese property market.

For many European countries, public austerity measures undermined domestic demand and reduced confidence in 2011. Large-scale monetary stimulus to the banking system at the end of 2011 and in early 2012 has eased fears of an imminent implosion of the Eurozone. However, the region's problems of high debt, low growth and uneven competitiveness will take many years to address and low growth is likely to continue, even if the currency union can be preserved. Germany is the major exception, benefitting from a relatively weak euro and strong competitiveness due to the fact that it undertook its own reforms at a time of buoyant external demand.

In the US, employment is rising and economic growth has become more robust and self-sustaining following the deepest and longest labour market slump in post-war US history. The US property market continues to restructure in response to the huge number of foreclosed properties and its construction sector is only likely to recover once this has been accomplished.

Average commodity price



Revenues and earnings for mining companies depend to a large extent on the commodities produced. As these commodities are traded globally, we do not, in common with our competitors, control the prices we receive for our commodities. Commodity prices are significantly affected by global economic conditions and, in particular, industrial production, which drives global demand for metals and energy.

Outlook

Significant short to medium-term uncertainty remains, despite signs that the global economy has managed to avoid another recession. The massive monetary stimulus provided by Western central banks has supported financial markets and banking systems, in turn stabilising growth. Major emerging markets are slowing from very high growth rates to more sustainable levels and, despite the Eurozone sovereign debt crisis remaining unresolved, economic indicators suggest a moderately robust outlook for global growth.

Our proprietary early-warning tracking shows real economy and industrial production indicators pointing towards stable growth for the two largest economies, the US and China. This, along with rising prosperity in Southeast Asian and African countries, will underpin demand for commodities. In contrast, the Eurozone faces a deteriorating outlook as the southern periphery drifts into recession.

High energy prices could undermine demand in advanced economies and further limit output growth in emerging markets. The long-term solvency of major economies such as Spain and Italy will depend on their ability to reform labour markets and raise their growth potential. This slow and difficult process may yet falter, possibly leading to a public debt default with major implications for the global banking system.

The longer-term prospects for the world economy are positive and global demand for commodities remains high and looks set to continue. The increasing number of middle class consumers and heavy investment in emerging markets' physical infrastructure are important long-term drivers. These should persist regardless of recent developments in emerging markets as government measures to control inflation temper growth rates. In addition, rising living standards mean that large numbers of households are joining the middle class in developing countries. This trend will support a substantial increase in the consumption of basic materials via demand for consumer goods and for more modern residential and commercial buildings.

The Chairman's statement (pages 4 to 7) and Chief Executive Officer's strategic review (pages 10 to 19) include commentary on the outlook for Xstrata's markets. More detailed commentary on each of Xstrata's key commodities is included in the Operating review (pages 46 to 77).

