Letter from the CEO

Donald R. Lindsay
President and Chief Executive Officer

To the Shareholders

The year 2016 was one of extremes. After entering the year with commodity prices at historic lows during one of the longest and deepest downturns in our industry's history, we saw unprecedented rallies, particularly in steelmaking coal, in the second half of the year. Today, it's abundantly clear that the steps we took over the last five years to reduce costs, increase efficiency and improve productivity positioned us well to create real benefits for our shareholders as the markets improved.

At the beginning of the downturn, we set out a company-wide strategy focused on five key objectives that we believed would allow us to emerge stronger from those difficult times — and we have delivered against each of them:

- We did not sell any core operating assets;
- We did not issue equity;
- We continued with our investment in Fort Hills;
- We maintained strong liquidity; and,
- We reduced debt.

We knew that if we remained focused on these objectives, our company would be better positioned than our competitors when commodity markets improved. As a result, we are emerging from this cycle with all of our operating assets intact, in a stronger financial position, and poised to deliver increased production per share.

While the market rally at the end of the year is fresh in our minds, the volatility we witnessed in 2016 was reflected in the significant shifts in prices for our key commodities over short periods of time. In steelmaking coal, spot prices ranged from historically low levels of US$74 per tonne in February to over US$300 per tonne in November. Our annual average realized price rose by 24% to US$115 per tonne, compared to 2015. The increase was largely due to a number of supply-side factors, and, as current coal prices have since come down from that peak, we still face a volatile price environment. In copper, prices ranged from a low of US$1.96 per pound in January to a high of US$2.69 per pound in November. Average prices fell by 11% to US$2.21 per pound, compared to last year. In zinc, prices again ranged from US$0.66 per pound in January to US$1.32 per pound in November as the global zinc deficit finally took hold in the market. Average prices rose by 9% to US$0.95 per pound, compared to 2015.

These significant price swings demonstrate the kind of volatility that is becoming the "new normal" for our industry, with commodity cycles that have the potential to be faster moving and more extreme. This makes it more important than ever that we build resilience into our business to weather the dramatic lows in the commodity price cycle, while remaining ready to capitalize on high prices when they occur.

The tenet that has guided us through the downturn has been "controlling the controllable": ensuring safety, remaining focused on sustainability, driving down costs, controlling capital spending and maintaining strong production. In that respect, our operations continued to perform well in 2016, with 11 of our 13 operations increasing production while decreasing unit costs compared with a year ago. We also set a number of quarterly and year-to-date sales and production records. This included achieving record annual production and sales of steelmaking coal of 27.6 million tonnes and 27.0 million tonnes, respectively, as well as record annual production of refined zinc and lead at Trail Operations.

We generated significant free cash flow in 2016, particularly from our steelmaking coal and zinc operations. Our gross profit before depreciation and amortization in 2016 was $3.8 billion, compared with $2.6 billion in 2015, with the increase due mainly to higher commodity prices. One of our key objectives has been to reduce debt, and we are delivering on that by applying some of the additional free cash flow from higher commodity prices to strengthen our balance sheet. In just over 12 months, we reduced our debt by approximately US$1.1 billion, bringing our total debt down to $8.3 billion at year-end. Our financial position and liquidity remain strong. At December 31, 2016, we had CAD$1.4 billion of cash and US$3.0 billion (CAD$4.0 billion) of unused lines of credit, providing us with CAD$5.4 billion of liquidity. We will continue to consider opportunities to opportunistically reduce debt.

We are close to adding a fourth major commodity to our business, with construction of the Fort Hills oil sands project now surpassing 76% completion. Project execution is now effectively site-based, as the module program has been completed and all remaining construction components are now substantially on-site. While the project has seen some modest capital cost escalation, it remains on schedule to produce first oil in late 2017. The project's economics are robust, and significant free cash flow is expected over its 44-year mine life.

We remain focused on our core value of safety across every aspect of our business. In 2016, we reduced Total Reportable Injury Frequency by approximately 13% compared with 2015, and we had zero fatalities. Lost-Time Injury Frequency fell by 11% and High-Potential Incidents by 12%. We continue to be vigilant in pursuing our vision of everyone going home safe and healthy every day. This past year, we rolled out the fourth phase of our Courageous Safety Leadership program, and we continue our focus on reducing High-Potential Incidents — those incidents that have the greatest potential to seriously injure someone.

Our 2016 progress in sustainability was recognized by a number of prominent international ranking institutes. We were named to the Dow Jones Sustainability World Index (DJSI) for the seventh consecutive year, and ranked as one of the Best 50 Corporate Citizens in Canada by media and investment research firm Corporate Knights. Following the successful completion of our first set of short-term goals in our Sustainability Strategy in 2015, we are now pursuing our next set of short-term goals that will guide our progress through to 2020, with added focus on air quality and climate change.

Looking ahead, we will continue to stay focused on delivering on our production and cost targets for each of our steelmaking coal and base metals business units in 2017. We will also continue to focus on improving operating excellence and increasing our margins to take advantage of the current positive price environment — particularly in steelmaking coal.

In addition, following project optimization work in 2016, we will continue to advance permitting in light of the updated feasibility study for our Quebrada Blanca Phase 2 project in 2017. We will also advance the NuevaUnión joint-venture project in Chile with an emphasis on technical and exploration drilling, completion of a prefeasibility study, and community relations. We will also continue to contribute to the successful completion of the Fort Hills oil sands project.

As previously announced, we had a number of senior executives retire in 2016, and I am pleased to say that the transition to our new realigned organizational structure has been a smooth one. As part of these changes, Dale Andres, Senior Vice President, Copper assumed responsibility for our zinc business, becoming Senior Vice President, Base Metals; Alex Christopher was promoted to Senior Vice President, Exploration, Projects and Technical Services; and Robin Sheremeta was promoted to Senior Vice President, Coal. The tremendous experience Dale, Alex and Robin bring to their new roles has already proven beneficial as we navigated through a volatile 2016.

We have come a long way this year. Thanks to the hard work of our employees, we have come through some of the most challenging market conditions in recent history and emerged stronger. By maintaining our focus every day on the factors within our control — safety, sustainability, costs, productivity and efficiency — I know our team is ready to take advantage of any opportunities and tackle any challenges that come our way in 2017.

Donald R. Lindsay
President and Chief Executive Officer
Vancouver, B.C., Canada
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