

DIRECT EMPLOYEE ENGAGEMENT : The Business Benefit

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14 November, 2006

1. Introduction

What do we mean when we talk about employee engagement?
Why is it so important?

I will address both these questions, in the context of our experience in BlueScope Steel. My perspective is set against the background of a large industrial manufacturing company, spun out of BHP Billiton a little over 4 years ago, with a clear mission to create it's own new foundations for the future.

Direct employee engagement is a fundamental principle that under pins our global HR strategy, but it is in the Australian operating environment where the contrast between BlueScope Steel's past, and future is stark. Accordingly, it is also the region where the examples of the business benefits are abundantly clear. So forgive me in advance for the Australia centric focus of this presentation, as I illustrate the benefits of what is a global BlueScope Steel approach. Unfortunately, the HR strategy of any major industrial manufacturing company in Australia involves a significant amount of industrial relations management, and I will also refer to our IR episodes during the implementation of direct employee engagement programmes.

2. What is Employee Engagement?

In BlueScope Steel, it means the direct, positive behavioural alliance that our Company seeks to have with our employees. For us, employee engagement is not simply an aspirational statement of a belief, but a systematic programme delivered through front line leaders. There are five main elements:

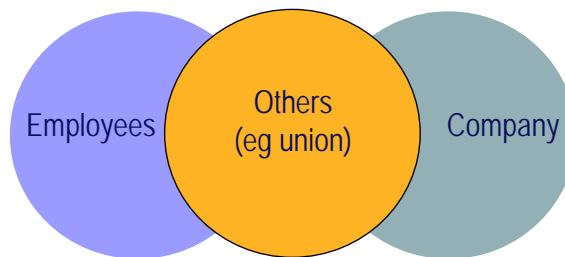
- Safety,
- Employee Share Ownership,
- Front Line Leadership,
- Confident Employees, and
- Management Resolve.

I will briefly deal with each element. First, let me illustrate the shift involved in adopting a strategy of direct employee engagement, between the old BHP Steel and the new BlueScope Steel. It can be argued that a number of the 5 elements above existed to varying degrees in BHP Steel, and in many other major industrial companies – so what's the big deal?

The first part of "the big deal" is that the employee engagement model in BlueScope Steel is direct, not indirect as existed previously, as illustrated below:

Employee engagement

BHP Steel

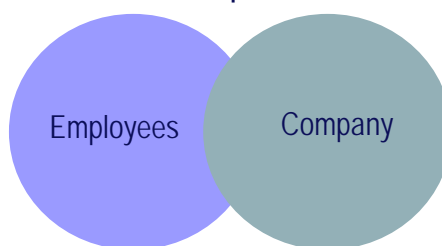


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Whereas the approach in BlueScope Steel looks like this:

Employee engagement

BlueScope Steel



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The second part of the “so what’s the big deal?” is the “Fifth Element” – Management Resolve. In BlueScope Steel, this forged a more binding strategic linkage and purpose across the four other elements. Previously, these tended to operate as separate, unconnected initiatives.

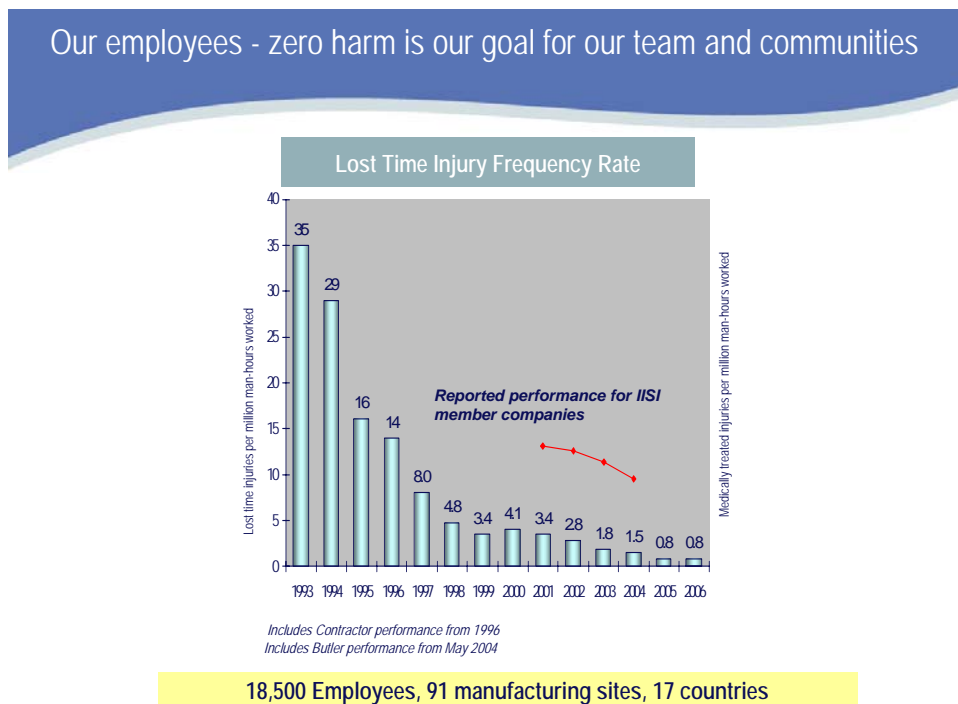
Let’s briefly look at each element, along with some related business results.

3. Five Elements

i. Safety

This is the most fundamentally important demonstration of a behavioural alliance across BlueScope Steel. Our shared commitment to the goal of zero harm had been adopted in BHP Steel well before the demerger from BHP Billiton. Since demerger our safety performance has benefited from programmes aimed at broad active direct engagement.

This is what our safety record looks like:



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For those who are more familiar with the US OSHA measures, which calculates injuries per 200,000 work hours (vs 1 million hours in Australia) divide these results by 5, ie: BlueScope Steel's LTI rate for comparison with US companies is 0.16

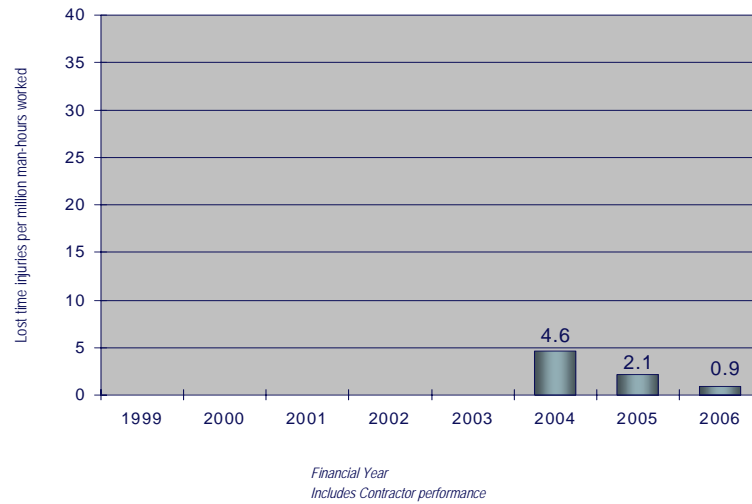
Line managers and lawyers in the audience will intuitively appreciate the business benefits of excellent safety. Aside from the personal distress, the effect on productivity and reduced time involved in post injury management is significant. In Australia our annual incurred cost under our workers compensation self-insurance arrangements is presently tracking at around 1 per cent of payroll cost.

The effect of the Fifth Element – Management Resolve – on safety is possibly best illustrated by the results being achieved in our US businesses which we acquired in 2004, and in our Asia portfolio.

This graph shows the performance of our 4,000 US employees in our Butler Pre-Engineered Buildings, and our Vistawall businesses since acquisition by BlueScope Steel. The data uses the Australian standard of injuries per 1 million hours.

Safety performance

North America Lost Time Injury Frequency Rate

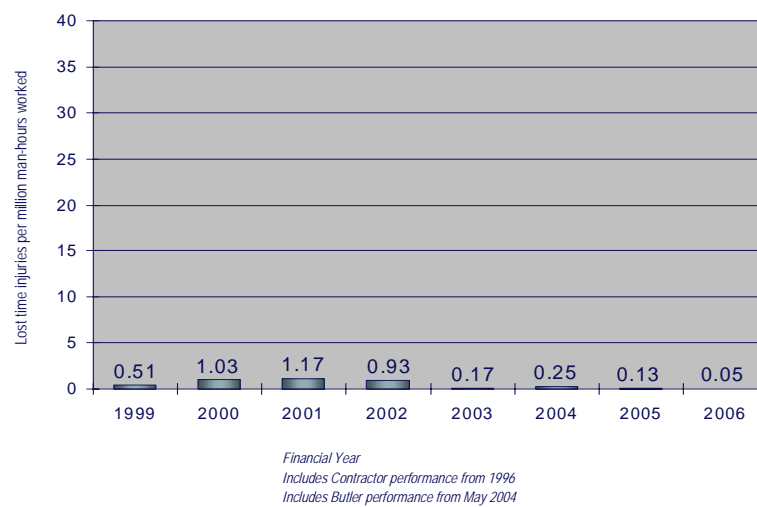


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BlueScope Steel Asia includes China, Thailand, Malaysia, Indonesia and Vietnam. In contrast to the community industrial standards in these countries, our Asia portfolio, where employee numbers have grown 200% to 4,500 today, leads our Company in safety.

Safety performance

Asia Lost Time Injury Frequency Rate



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This performance is outstanding, BUT the single LTI in China in the '06 financial year was in fact a fatal fall of a contractor on our Suzhou construction site. No one in BlueScope Steel is relaxed or comfortable with our safety performance!

ii. Employee Share Ownership

Different companies have different views on the contribution an employee share plan makes to the employee engagement objective. BlueScope Steel has a strong belief in the importance of share plans, as a means of aligning the common interest of shareholders and employees, on a global basis.

However, the way we approach the design of our share offers may differ from some others.

First, our share plan does not form part of the expected conditions of employment. The terms are not negotiated with anyone, and it is not used as a substitute for any other reward or entitlement.

Secondly, its principle purpose is to provide a basis for line management communication and education about the strategy and performance of the Company, from a shareholder's perspective. As our shareholders would know, our 2005/2006 results were disappointingly below our expectation. Accordingly, the employee share plan was deferred this year, pending a return to expected financial performance.

Thirdly, entry to the share plan is by personal referral from a line manager in respect of a new employee in their team, after the required qualifying period. It is not a gift that mysteriously appears in the corporate mail.

Fourthly, in developed, higher wage countries, we now require employees to invest their own money to qualify for their invitation.

99% of BlueScope Steel employees are shareholders. We introduced the requirement for employees to invest their own money after the industrial disputes in Australia in 2004 and 2005. We took the view that it was simply unacceptable that some employees take a gift of shares with one hand, while raising the other to support their union's campaign against BlueScope Steel. Accordingly, we decided that employees who want to see the Company succeed should be willing to invest themselves. 95% did just that, which in light of the industrial disputes less than a year earlier, was an encouraging surprise.

Notwithstanding the high employee participation rate, and in light of the Australian industrial disputes, you may be wondering why I am convinced about the merits of a general employee share plan, which costs BlueScope Steel about \$14m each time.

- During the industrial disputes the high participation rate enabled the lines of communication between management and the workforce to remain constantly open – not as manager to union member, but as shareholder to shareholder.
- Employees reached agreements on a site by site basis, not the single BlueScope Steel Australia agreement sought by unions.

Our encouragement by the 95% participation rate in the employee investor plan in Australia was recently strengthened. Our first employee share offer in 2003 recently vested after the statutory 3 year period, 93% of our 8,500 Australian employees chose to retain their shares.

iii. Front Line Leadership

The internet facilitates a “mass media” approach to communicating important information and Company-wide programmes to employees. But this medium by-passes the most effective form of communication and motivation available. Front Line Leadership, face to face discussion.

In BlueScope Steel, the Front Line Leader is our HR “channel to market”. With the exception of market sensitive information, we have formal processes to ensure that Front Line Leaders are equipped to not only personally communicate messages to work teams ahead of media, or intranet announcements, but to also discuss and debate the issues involved.

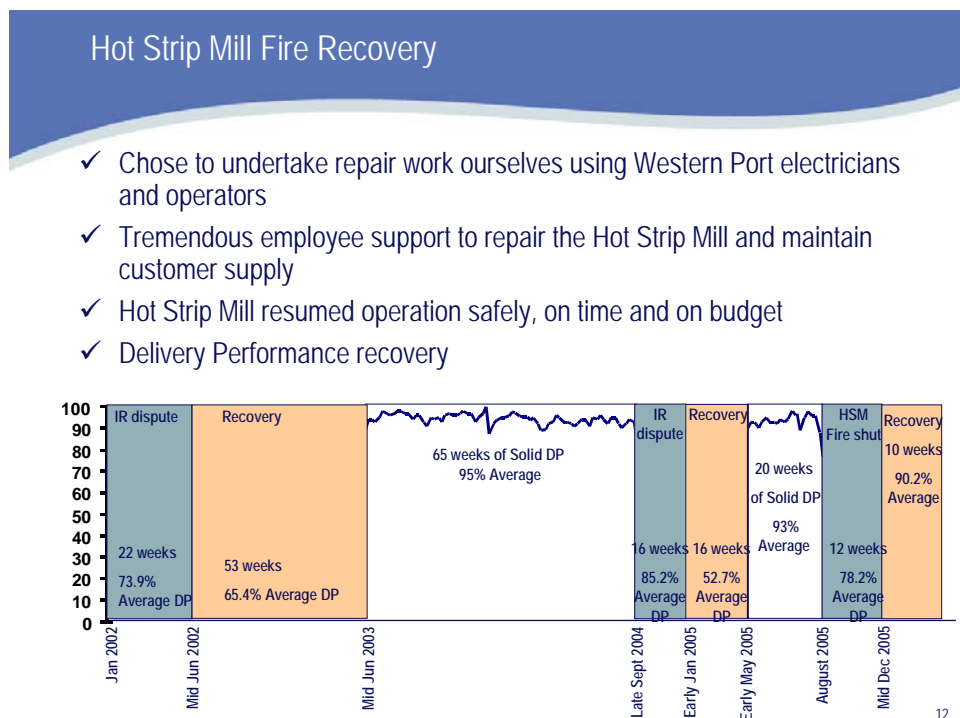
A good example which illustrates the benefit of this approach can be found in our experience with the ACTU national protest days against the Federal Government's WorkChoices legislation. When the first day of protest was scheduled for July last year, some of our Australian site managers strongly felt that an active programme of information and discussion would only serve to heighten awareness of, and participation in, the day of action. Others strongly felt such a programme would reduce the potential for business interruption. On the day, when about one thousand BlueScope Steel employees walked off the job to attend, it was clear from our site participation analysis that our active communicators were right. When the second day of action was announced for November last year, we mandated an active information programme to equip line managers with the ability to hold meetings and engage in debate on the issues raised in the media. About 400 employees attended the second protest. Employee absences across our 8,500 Australian employees for the third event in June this year was 86 – two thirds of whom applied for, and were approved, leave to attend the protest in their own time.

This demonstrates what consultant's studies have been consistently telling us for years – that the front line leader is the most dominant influence on the level of discretionary energy of an employee – the difference between what we have to do, and what we want to do.

In BlueScope Steel, Front Line Leaders are the key to our employee engagement strategy. However, it is this element where we are, frankly, in “catch-up” mode. Providing the information and communication workshop, is one aspect we are now pretty good at but we cannot expect Front Line Leaders to be fully capable in this pivotal role without focussed training and personal development. We are only now beginning to address this with the launch of our Front Line Leader Essentials programme on a global basis.

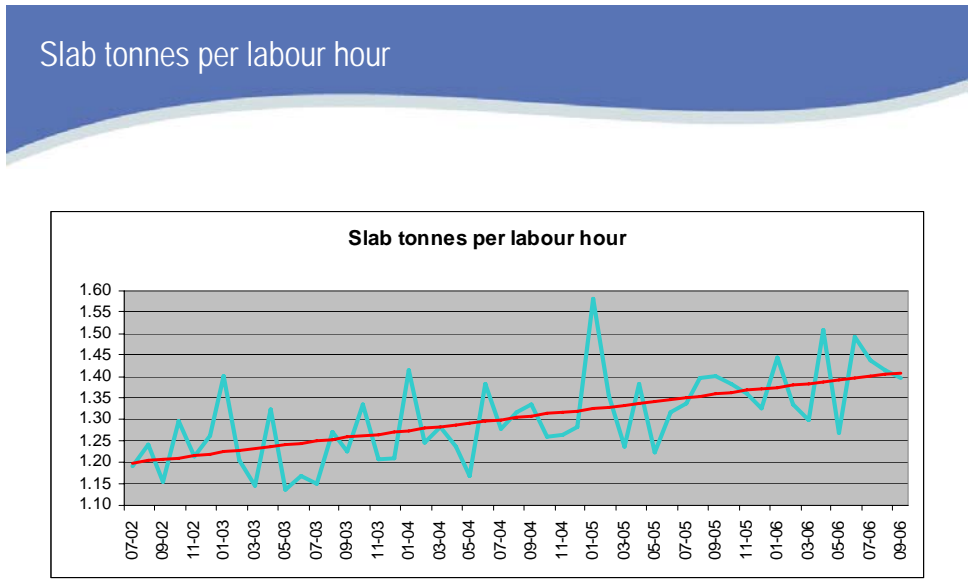
iv. Confident Employees

It is difficult to separate the preceding element of Front Line Leadership, from the importance of employee self-confidence. There is no doubt that BHP had done an excellent job in skills training over many decades, and this is a critical piece in the self-confidence puzzle. However, in the years preceding our demerger, BHP Steel was run for cash, with its status in the BHP Billiton fold publicly “short-term”. Overlay the uncertainty of going it alone as a newly listed company. Against this background, it is not surprising that our Australian workforce was further challenged by the shift from the three party paradigm, to the direct employee engagement model. Clearly, Australian unions were challenged by it, because it represented a clear threat to the special – almost unique – position of leverage they had developed over decades in BHP Steel. However, the position we are in today is very encouraging. The combination of effective Front Line Leadership, and employee confidence, is best illustrated by the following data from our Western Port site in Victoria.



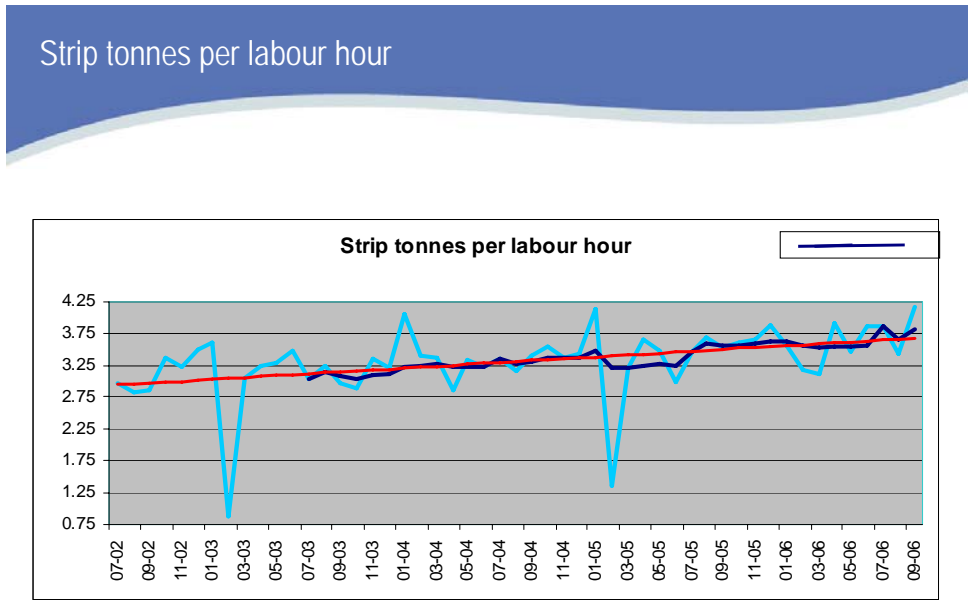
You can see the effect on delivery performance of a major industrial dispute with maintenance unions in the six months preceding demerger. It took a full year to recover the previous delivery performance after that dispute was settled. The next dispute with both production and maintenance unions occurred during the enterprise bargaining round in late 2004. You can see that recovery took 16 weeks. The next major disruption was caused by an electrical fire which knocked out the Western Port Hot Strip Mill. When agreement could not be reached between the Victorian Branch of the Electrical Trades Union and contractors on the employment terms for the re-build and replacement of the destroyed plant, our own unionised electricians, along with the unionised production workforce, our supervisors, engineers, managers, procurement, sales, etc, etc, kept the business going and re-built the plant themselves – ahead of time and under budget! The recovery time shortened to 10 weeks. Today, Western Port is setting new production records.

And talking about records, this is the data from our steel making operations at Port Kembla since our demerger from BHP Billiton.



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And another from our Hot Strip Mill at Port Kembla.



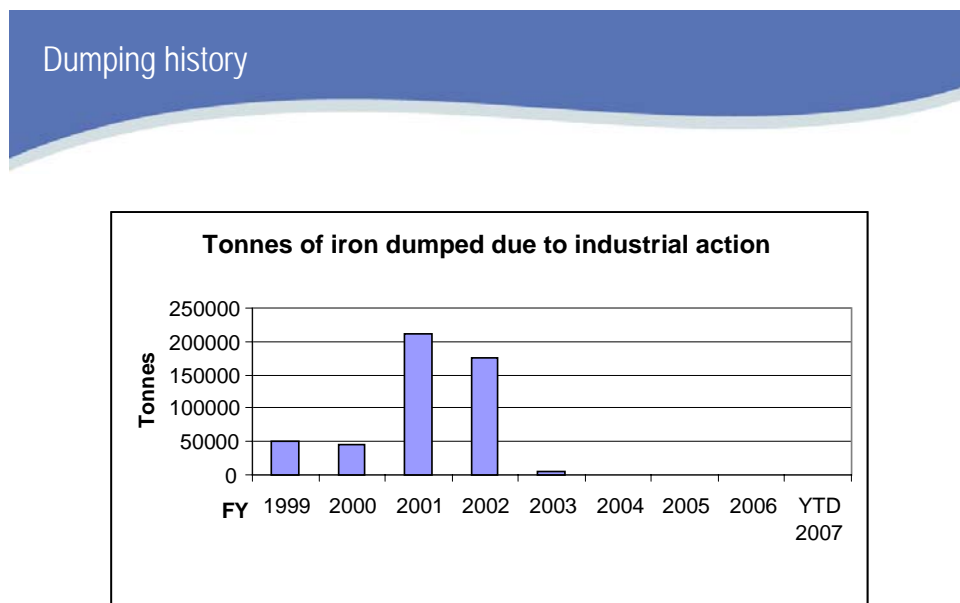
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The two big dips are planned maintenance shuts.

- v. Management Resolve
Now to “the Fifth Element” – management resolve.

Earlier I touched on the effect on the business model of unions of the move from the three party paradigm to direct employee engagement. Australian unions strongly reacted against BlueScope Steel in defence of their previous status as “broker” in the relationship between the Company and their members. The conflict was costly, but absolutely necessary to re-set our foundations for our future as an independent company.

The graph below shows the amount of iron dumped at our Port Kembla steelworks due to industrial disputes.



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The iron dumping fell to nil from 2003 onwards and reflects a decision by the State Industrial Relations Commission of NSW which prohibited any further industrial action at Port Kembla causing iron to be dumped, or industrial action that interrupted continuity of critical customer supplies.

Nevertheless, unions continued to fight BlueScope Steel on a national front. In the last 6 months of 2004 BlueScope Steel in Australia endured 200 separate stoppages! (And not a minute of industrial lost time in our BlueScope Steel history in any other country.) One of these disputes, involving a small number of electricians at Western Port in Victoria, threatened to shut most of Australia's metals manufacturing industry, causing the Federal Industrial Relations Commission to issue rare Orders prohibiting further industrial action.

Today's picture is, thankfully, very different.

- After defying their union and playing the pivotal role in rebuilding plant at Western Port after the disastrous electrical fire a year ago, our electricians finally reached a wage settlement with their own non-union collective agreement.
- At a time when the Federal system only allowed a maximum of three years, a leading edge four year collective agreement covering operators at Western Port was reached with the AWU. Our next negotiation is in late 2008.
- Agreements reached with unions at Port Kembla are in place through to March 2009, bringing an unprecedented opportunity for management and the workforce to invest their energy on more productive pursuits. The "no iron dumping" and "continuity of supply" provisions remain in force.
- All of our remaining 50 Australian manufacturing sites have their own site specific industrial arrangements, ranging from union collective agreements, to non-union collective agreements, to individual staff employment contracts.

There is no doubt that resolute our shift towards the direct employee engagement model confronted the industrial relations world of BHP Steel unions. But, notwithstanding the I.R. battle during the first two and a half years after demerger, the operating performance of the business continued to improve during this period. Clear evidence that we were not "at war" with our employees.

The confrontation with Australian unions is, I believe, behind us. BlueScope Steel has a new, but frankly natural, employee relations platform in place.

4. Conclusion

To conclude, when BlueScope Steel was spun out of BHP Billiton on 1st July 2002, direct employee engagement was the foundation stone in the company's objective to deliver superior future organisational performance.

The strategy conflicted head-on with the role of Australian unions in the old BHP Steel. At the time of demerger, BlueScope Steel had around 11,500 employees, 72% of whom were in Australia. Today we have 18,500 employees, with 45% in Australia. The industrial relations struggle to achieve what should be a normal, natural relationship between a company and its employees is, I believe, behind us. We are now able to concentrate our efforts on fully unlocking the potential benefits of direct employee engagement.

I have covered 5 elements of our programme:

- Safety, where our people have created operating environments in their industrial workplaces that are amongst the safest in the world.
- Employee share ownership, where BlueScope Steel employees have already demonstrated their confidence in the company by committing their own money, and by retaining vested shares.
- Front Line Leaders, who we believe are key to superior workforce performance.
- Confident employees, who have endured uncertainty in the periods pre and post demerger, had their confidence shaken by union campaigns, but have returned to deliver operating records, and
- Management Resolve – some things are just not negotiable.

Finally, the competition to attract and retain skilled employees is at the forefront of business concerns, particularly in Australia and in Asia. In BlueScope Steel our direct employee engagement strategy contributes to our high rate of employee retention where voluntary turnover is about half industry rates in both regions.

If there are BlueScope Steel shareholders in the audience, I look forward to seeing you at our AGM in Sydney tomorrow.

Thank you.