Tracking the trends in mining

Key issues impacting the mining industry in 2016 and beyond

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Quick introduction

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- Based in London
- Extractives clients in gold, copper, diamonds, iron ore, rutile, coal, oil & gas
- Client operations in Australia, South Africa, Canada, Chile, Egypt, Russia, Ukraine, Kazakhstan, United States, Congo, Botswana, Sierra Leone
- Client corporate headquarters in London, Jersey, Johannesburg, Brisbane, Adelaide, Hong Kong, Santiago, Denver
- Piano player
Global context

Key influences:

- Oil staying “lower for longer”
- Iron ore majors decision to maintain output
- China growth slowing
- Middle East/North Africa tensions
- Russia/Ukraine tensions
- Eurozone continues to be mixed
- US market generally good
- Seaborne freight rates dropped
- Equity markets strong
62% Iron Ore
Copper

Price - USD/MT


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Coffee

Price - COP/KG

Key themes:

We are in a time of low commodity prices. In response, miners need to seek continual improvement, through operational excellence, innovation and energy efficiency.

The slowdown in China, increased difficulties in stakeholder management, imminent changes in the global taxation environment and ongoing financing difficulties all make this a tough time for mining companies.

Safety is, as always, a number one priority.

Despite the current difficulties, the cycle will turn – what goes down must come up, and now may be time to start considering acquisitions.
1. Going lean
Operational excellence remains front and centre

- Miners cannot become complacent about cost control
- Leading miners are leveraging best practices from other industries
- Difficult issues are now being faced, for example labour relations
- Other areas of focus include:
  - energy efficiency
  - lean practices
  - innovation (refer trend #2)
  - supply chain optimisation
  - data integration
  - back office restructuring
  - collaboration
- Whilst improving efficiency and sustainably removing costs is key, miners need to make sure they don’t remove the ability to respond to the upturn when it comes!
2. Innovation: the next generation
Preparation for exponential change

- Innovation was initially focused on cost-cutting
- But innovation can also assist with managing talent shortages
- Collaboration is key
- Knowledge sharing adds to the effectiveness of innovation
- Innovation can also add to mine safety
- Miners can learn from complementary industries
- Go beyond technological and process innovation, to include community and government engagement, process management and procurement
- Leadership is essential if innovation is to succeed
3. China’s painful transition
Looking for the silver lining

- China’s significant impact on world markets means miners need to understand China, its economy and its market trends, particularly at a time of transition in the Chinese economy.
- Issues of note for miners include:
  - More interventionist government policies
  - The anti-corruption drive
  - Property oversupply and slowdown
  - Stock market wobbles
  - Currency issues
  - China’s domestic commodity supply
- China will continue to be very important to mining – China consumes approximately 50% of the world’s refined copper (source – ICSG World Copper Fact Book 2015)
4. Adjusting to the new normal
What goes down must come up

- Although commodity demand is down, production has not fallen at the same pace.
- Some producers (e.g., the Australian iron ore producers) have ramped up production to consolidate market share, reduce marginal cost, or seek to “ride out” the downturn and avoid the costs of closing mines.
- However, there has been a significant decline in exploration and project pipelines across multiple commodities (including copper).
- This will ultimately lead to supply shortages.
- Urbanisation is ongoing, industrialisation and infrastructure development will all contribute to growth in global demand.
- This demand combined with inevitable supply shortages will ultimately send prices back up again.
- Miners need to consider how they can respond to this whilst avoiding the “all or nothing” response from last time the cycle turned upwards.
5. The shifting global energy mix
Preparing for inevitable change

- China’s thermal coal consumption fell in 2014 and 2015 despite an increase in electricity generation
- Natural gas continues to grow as a fuel for electricity consumption and is expected to surpass coal by 2040
- Installed capacity of nuclear power generation expected to grow by 60% in the next 25 years
- Renewables generation continues to grow, with the intermittency issues being addressed through technological progress in generation and in battery storage
- Thermal coal producers need to think about the long term, although there is still significant demand across the world, particularly in the Pacific rim
- Diversification is important (e.g., lithium and other metals used in battery storage should see ongoing, significant demand growth)
- Miners should consider their own energy mix
6. Engagement party
Changing the nature of stakeholder dialogues

- Stakeholder expectations continue to rise (regardless of the state of the mining industry)
- It is getting harder for miners to reconcile the often competing needs of governments, local communities, NGOs, employees, regulators and shareholders
- Miners need to be very sophisticated in how they work with stakeholders, including being able to measure accurately and communicate effectively their achievements in benefiting the communities in which they operate.
7. The capital crisis
Starved of finance, miners struggle to survive

- Attracting capital is harder than ever
- Companies seeking alternative forms of financing (eg streaming)
- Miners getting creative (eg equipment & construction financing)
8. A taxing time for miners

A global tax reset challenges yesterday’s tax management

- OECD and G20 seeking to curb inappropriate tax management
- BEPS has significant tax implications for global miners
- Regulatory change will be effective from 31 December 2016
- Miners need to plan for these changes and engage with tax authorities as appropriate
9. The M&A paradox
To buy or not to buy; that is the question

- Most deal flow stems from divestments or as a consequence of distress
- This makes it a good time for miners with strong balance sheets to make acquisitions
- May be time for miners to think “counter-cyclically”
- Think carefully before divesting
10. Safe, secure and healthy
An expanded view of corporate and personal welfare

- Miners continue to refine safety programmes, focussing on achieving zero fatalities
- The culture of safety continues to expand and now includes mental health
- Miners need to be prepared to tackle new risks, including the mounting threat of cyber attacks and their consequences
- Strengthened policies, risk management and security protocols will assist
In summary

Times continue to be challenging for miners, including copper miners. However by focussing on the key trends and responding to them, miners can maximise their returns through this difficult period.

The cycle will turn, be ready to reap the benefits!