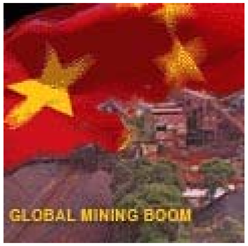
Chinese dragon flames global mining boom



Globally, 2004 was a boom year for the mining industry on the back of Chinese demand for a broad range of commodities.

South Africa, however, did not fair as well as its global counterparts.

A survey of the mining sector, 'mine - enter the dragon' released yesterday by PricewaterhouseCoopers indicated that 2004 was a 'spectacular' year for the mining industry - globally.

The survey takes into account 40 of the world's top mining companies, which together make up 80% of market capitalisation.

All the information used is publicly available, explains partner and leader of the global mining division Hugh Cameron.

Of the companies, only two are not publicly listed.

Industry market capitalisation is up by 19% to $184-billion and, for the second year running, profits doubled.

The net profit margin went up five per cent from ten per cent and return on equity (ROE) moved by 8,7% up to 18,9%.

Net debt equity is down 14,3% to 25,4%.

Yet none of these glowing figures can be extrapolated to the South African situation, described by Cameron as bleak.

Local companies market capitalisation was down nine per cent and, while revenue increased by 44% in dollar terms, the increase in rand terms was only three per cent.

Cameron explains that cost terms in rand went up significantly and when non-dollar costs are converted at strong rand rates the effect means a higher dollar base.

ROE halved from the 2003 period, down to 9,7%.

Harmony Gold's failed takeover bid for Gold Fields also influenced these figures, says Cameron, as the industry saw some high-value destruction.

Overall, the mining industry out performed the Dow Jones and S&P 500 indexes, thanks to the high demand and resultant high prices in commodities.

Looking at market capitalisation, this is dominated by BHPBilliton, Rio Tinto, Anglo American and Companhia Vale do Rio Doce (CVRD).

Cameron made the point that if the BHPBilliton take over of WMC goes ahead; the resultant company will have 90% of the total market capitalisation in the gold industry.

Mining companies are sitting on vast war chests; cash reserves are up 58% to $22-billion.

Huge reserves will cause investors to start asking questions and money will either have to be invested in capital expenditure, growth or be returned to shareholders.

Cameron says that the time is ripe for new greenfields discoveries.

New discoveries by juniors may see them absorbed into larger companies.

Acquisitions are set to continue, although not at the same rate as last year, which saw three large failed acquisition attempts.

Commodity prices have steadily increased in dollar terms over the last three years with the exception of nickel.

By contrast, prices in rand terms have decreased in the last three years - highlighting the link between a loss in revenue and a strong rand.

The key to good margins is to continuously cost-cut, even in good times, says Cameron.

He hopes to see improved management of costs in boom times and not just slow periods.

Last year saw global revenue increase 39% but operating costs went up 30%; a phenomenon he ascribes to only moderate increases in production, increased freight costs as capacity to China was limited and increased energy costs.

Mines have not seen the end of the effect of these costs - Cameron warned that they are lagged costs and the full effect will only be felt in the coming year.

Problematic too are high steel costs and catch-up maintenance costs.

Despite this, 2005 globally will be an even better year.

The dragon

Much of the boom globally is ascribed to China's push towards doubling its economy by 2020.

In the last 25 years, the country has grown its economy six fold.

In 2003 it imported $102-billion in minerals - and imports continue to surge as it attempts to balance growth.

China makes up four per cent of global gross domestic product and uses 30% of the world's coal, 30% of global steel and some 3% of electricity.

Currently its mining efforts are largely inefficient and fragmented, despite appearances of a mining boom in the country.

Cameron says that legislation is opening up to allow operations, but only if your company is Chinese.

Added to this, the government continues to push Chinese firms out of the country in a bid to secure supply chains.

Chinese investment out of the country now stands at $1,9-billion, $0,9-billion of this made last year, compared with investment into China of $336-million.