

Iron ore party not over yet

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Stephen Bell



AUSTRALIA'S swelling band of would-be iron ore producers looks a trifle rusty after the recent bloodbath on world commodity markets. But if you believe one of the big hitters of iron ore, it is not all doom and gloom for those shell-shocked rock kickers.

Sam Walsh, Rio Tinto's iron ore chief, was the bearer of reassuring news last week when he told journalists in Perth that he expects "continuing strong demand for iron ore from China for a few years yet".

Speaking after an Australian Institute of Management breakfast, Walsh was also crystal clear in his response to China's tardiness in signing up to the 19% iron ore price hike agreed to last month by European, Japanese and South Korean steelmakers.

"The benchmark is in place," he said, adding that Rio – along with its competitors BHP Billiton and Brazil's CVRD – are now just waiting for China to "come to the party".

CVRD head of iron ore Jose Carlos Martins said pretty much the same thing after his speech to Melbourne's Mining Club on Thursday.

The *Metal Detective* interprets the comments from both iron ore giants as a pointed message to China: "Drag your heels as long as you like. But the market is still tight. If you want your iron ore, pay up."

Rio's Walsh, like any good chief executive, was talking his book.

But it was certainly a welcome reiteration of iron ore's bullish fundamentals amid the recent savaging dished out to LME-traded metals.

As any investor knows, the share market works mostly on sentiment.

At the moment, people are nervous about interest rate rises and a potential slowdown in the US economy.

So the recent 19% price hike did not prevent a rout among the junior iron ore stocks caught up in last week's market downturn.

At the close of trade Friday, shares in Fortescue Metals Group were down 30% from their recent peak. Gindalbie was off 38% from its high, Territory Iron was down 30%, Midwest was 34% lower while Murchison Metals and Grange Resources fell 12% and 22%, respectively.

The extent of the retreat is a tad unfair, given that iron ore prices – under the traditional annual benchmark system – are relatively immune from the rampant speculation that has tainted the LME-traded markets.

Walsh believes that the benchmark system is alive and well, despite China's painfully drawn-out stalling tactics this year.

"This system has worked for the past 30 years," he said. "People find it very comfortable because once the price is settled, it gives us stability and reliability."

The International Iron and Steel Institute had debated whether it wanted to move to an LME-based mechanism for steel prices. "But they made the decision that it wasn't right for them," Walsh said. "Likewise, to me, that would indicate that LME isn't right for iron ore either."

Commenting on demand, Walsh said 80% of the growth in iron ore stems from China.

Therefore, any worries over a sharp pullback in the Chinese economy would have dire consequences for Australia's expanding iron ore sector.

As yet, however, there were no signs of that occurring.

"Some people are saying that they expect (Chinese) GDP growth to be in excess of 7% for the next 10 years," he said.

That expansion will continue to drive healthy demand for iron ore, Walsh believes, though longer term, the market will come into balance as new supplies are brought online.

Just how fast those supplies will arrive is the billion dollar question, of course.

Rio, BHPB and CVRD are spending billions on building new mines as fast as they can.

Macquarie Bank has calculated that there are \$US15.4 billion (\$A20.7 billion) worth of committed iron ore projects, globally, due to come on-stream in the next few years, with another \$21 billion of "likely and possible" projects.

Australia also boasts a host of proposed start-up ventures, many of them in partnership with Chinese companies.

Of the \$6.4 billion worth of committed Australian projects (totalling 124.5 million tonnes per annum), around \$525 million are from "small" companies, including Gindalbie, Territory Iron, Portman, Midwest, Murchison Metals, OneSteel and Aztec Resources.

The likely and possible ventures, meanwhile, include 12 Australian projects, such as BHPB's RGP 4 and FMG's Pilbara Iron.

The difficulty for these proponents, however, is that labour and materials are becoming much more expensive, while government and environmental approvals are taking much longer.

If you look at an iron ore hopeful "starting from scratch", it could be in the "vicinity of five years from when they have the twinkle in their eye until the project is actually putting iron ore into the ship", notes Walsh.

"The timings are considerable," he said.

That is partly why Rio thinks that there are a few years left in the iron ore boom – many of the projects being talked about have "lots of distance to travel".

No names were mentioned, of course, but Walsh could easily have been referring to projects such as FMG's Pilbara venture.

He is not alone in thinking that FMG's aim of starting production by late next year looks optimistic, given the current pressures on the industry.

In a funny sort of way, though, that may not be such a bad thing for FMG or the other start-up companies.

After all, any further project delays will help keep the iron ore market tight – and increase the prospects for another price rise in 2007.



Aspermont Limited
Street Address 613-619 Wellington Street, Perth WA Australia 6000
Postal Address PO Box 78, Leederville, WA Australia 6902
Head Office Tel +61 8 6263 9100 Head Office Fax +61 8 6263 9148
e-mail contact@aspermont.com website www.aspermont.com ABN 66 000 375 048