Mine 2019

Resourcing the future

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Shifting expectations

Welcome to our annual review of global trends in the mining industry, as represented by the Top 40 mining companies by market capitalisation.

Judged by traditional metrics, things are looking good for the world's top miners. In 2018, the world's 40 largest miners consolidated the stellar performance of 2017. As a group, they increased production, boosted cash flow, paid down debt, and provided returns to shareholders at near record highs. And there was still cash left to increase capital expenditure for the first time in five years. All while delivering significant value to stakeholders like employees, governments and communities, as well as supplying the raw materials underpinning global economic growth. The benefits of mining have flowed far and wide.

Yet investors seemed unimpressed, at least judging by market returns and valuations. What accounts for this discrepancy? Stock markets are famously futures markets, not present markets. And when investors and other stakeholders look at the future of the mining industry, it is clear they have concerns about the industry's perception on vital issues such as safety, the environment, technology and consumer engagement.

In spite of the strong operating performance, both investors and consumers seem to be down on the brand of mining. They question whether the industry can responsibly create sustainable value for all stakeholders. Discrete events, such as safety or environmental incidents, have contributed to these challenges.

'Big questions' to address

But far-reaching structural changes in the environment – and in the operating environment – are also raising questions about the industry's future. Foremost among them is the impact of climate change, highlighted by the rising frequency of extreme weather events. As the finder and provider of carbon-based raw materials in the form of coal and a substantial creator of CO^2 emissions via mining and metals processing, the mining industry is firmly involved in the climate change debate. The Top 40 response is varied: some have adopted a climate change strategy and others are seemingly indifferent.

Copper and battery metals, which stand to gain as the energy mix moves away from combustion engines to electricity including renewable energy, are receiving the bulk of capital investment. (However, as coal contributes 38% to global electricity generation, it remains an important part of the basket and continues to receive substantial capital investment and transaction focus.)

Mining companies are also streamlining their operating portfolio by disposing of non-core assets and optimising project portfolios in line with long-term strategies. In 2018 and early 2019, a key focus of merger activity among the Top 40 was consolidation in the gold sector. It remains critical that potential acquirers evaluate their strategic options before taking action, but we may see further transactions to drive efficiencies and improve productivity.

Can mining change fast enough?

While they appreciate the efforts to improve operations and engineer superior results, it is clear that investors and other stakeholders are concerned that the industry is lagging when it comes to several factors that have not been a traditional focus of the mining industry. These include dealing with emissions, investing in differentiating technology and digitisation, engaging more proactively with consumers and building brand.

Looking ahead to the rest of 2019 and beyond, we see a continuation of the strong operating performances, and pockets of progress in these contemporary factors. But we don't see any signs of a quantum shift in priorities that will allow the industry as a collective to keep pace with changes delivered in other sectors. Without such a shift, we expect the growing awareness gap between the brand of mining and the benefits of mining to continue to widen.

The mining industry will have a window of opportunity over the next few years, created by strong operating fundamentals, to adapt to the growing and changing expectations of stakeholders. By utilising technology to operate safely and more efficiently, addressing global concerns, and maintaining a disciplined strategy to create ongoing value for its stakeholders, the industry can forge a better future for all beneficiaries of mining – industry, consumers, communities and other stakeholders.

Responsibly creating value for all stakeholders on a sustainable basis

Top 40 mining companies performance snapshot

Financial capital

Revenue
$683bn up $51bn (8%)

Record dividends paid to shareholders $43bn

EBITDA
of $165bn up $7bn (4%)

Market cap
as at 31 December 2018 $757bn (down by 18%), as at 30 April 2019 $849bn

M&A activity up to $30bn

Manufactured capital

Costs up by 8.6% driven largely by commodity-based input costs

Capex up for first time in five years by 12% to $57bn

Modest growth in production

Human capital

Safety focused, but fatalities remain an issue

21% of new Board member appointments were female

Social and environment capital

Reported Scope 1 and Scope 2 emissions show a CAGR reduction of 5.2% from 2016 to 2018

Value distributed to government and employees - 43%

All figures are US dollars
Source: Annual reports, PwC analysis

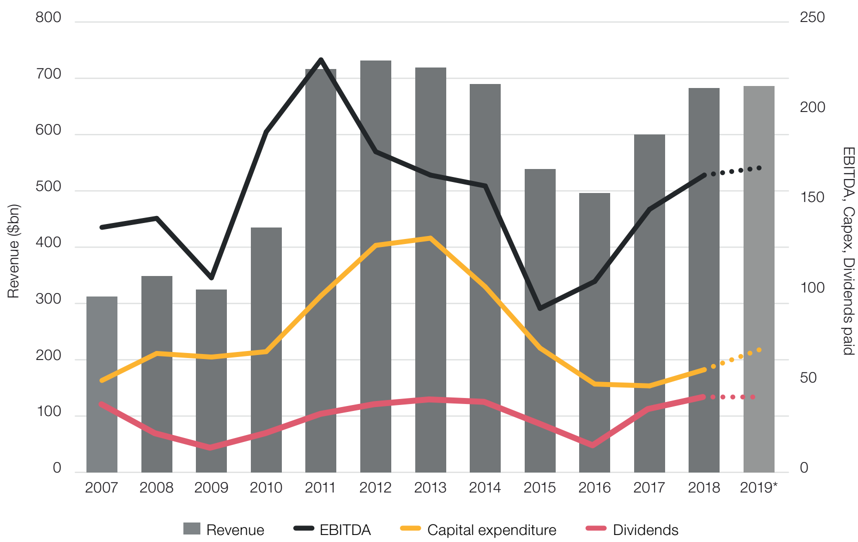
Industry overview

Steady but the heat is on

The Top 40 continued to see steady growth in revenue and profitability, as predicted in our forecast last year. Dividends to shareholders are at an all-time high and balance sheets are strong. Capital expenditure showed an increase for the first time in five years, albeit still below 2008 pre-boom levels.

Trade wars, geopolitical crises and climate change continue to create industry volatility. This uncertainty was particularly evident at the end of December 2018, when commodity prices and emerging economy exchange rates decreased substantially.

Figure 1: Top 40 mining companies performance trends ($bn)



**2019 outlook*

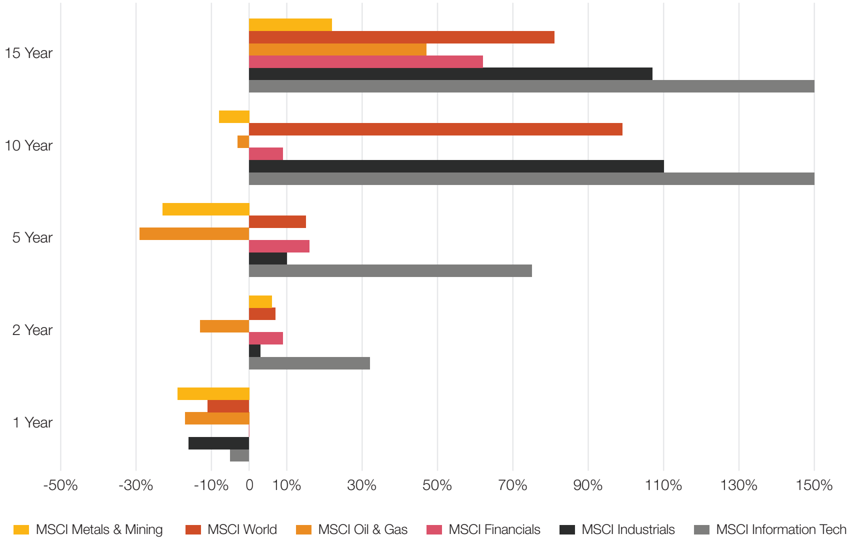
Source: Annual reports, PwC analysis

In the broader market context, mining continues to struggle for favour

Despite the industry's impressive financial performance over the last two years, the mining index has barely held its own against global market indices. Notwithstanding multi-year high profitability levels supported by strong financial positions, investors are seemingly not willing to invest at historic price and dividend yield levels, hence existing investors have not been rewarded with an equivalent market price performance.

Moreover, our long term analysis points to only marginal market capitalisation growth by the mining industry over a 15 year period. In this period, its performance has lagged that of the market as a whole, new technologies and comparable industries, such as oil and gas.

Figure 2: Relative sector total shareholders return* performance



Annual capital growth (31-Dec over 1-Jan) plus dividend yield

Source: S&P Capital IQ

Mining companies do not measure their success based solely on their share price performance. Nevertheless, the share price movement relative to the rest of the market is an indication of the market's view of the industry's attractiveness. Mining dividend yields have increased to above 3% since 2011 and are well in line with those of other sectors (e.g. oil and gas between 3–5%, technology between 1–2%). There has been a significant increase in dividends paid in the last two years. Despite the strong financial position and recent track record, investors seem concerned about mining's negative publicity, the future of certain commodities and the industry's ability to manage stakeholder expectations. Additionally, the fact that only three mining companies are in the 2018 Global 500 brand index (none in the top 100), compared with 22 oil and gas companies, indicates an unfavourable or indifferent perception of 'brand mining'.

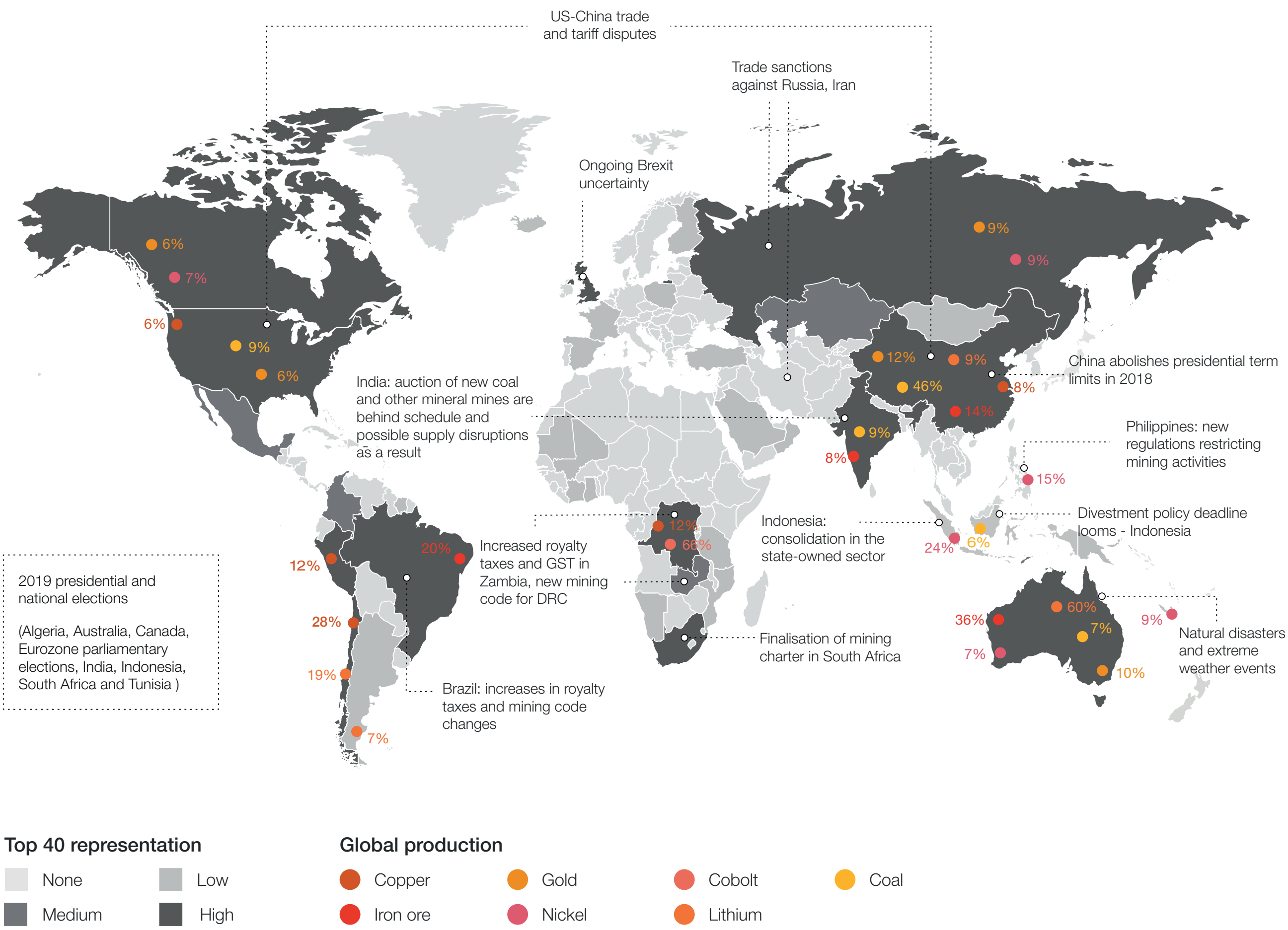
One thing is clear – mining requires far more than good financial performance to continue to create and realise value in a sustainable manner.

We believe the under-performance is connected with the risk and uncertainties of a changing world and the market perception about the mining industry's ability to respond. The future success of the mining industry will not only depend on its ability to adapt but also its ability and willingness to sell its brand as the primary provider of raw materials to many essential industries and products that humans rely on everyday, whether it be the ten metals and minerals - including gold, silver, aluminium and nickel - that can be found in their cell phone, the lithium in the battery of their electric vehicle, the steel from iron ore in their cooking pot or the coal fuelling their electric lights.

A changing world with risks and uncertainties

Mine 2018:Tempting times, highlighted a number of regulatory and political challenges. This year is proving no different. Against the backdrop of US–China trade disputes and upheaval in the Eurozone, all spheres of business including taxation, environment, politics, investment and labour are marked by volatility and uncertainty. This places further pressure on the mining industry to create sustainable value into the future.

Figure 3: Top 40 reach and external market drivers



Source: USGS, PwC analysis