The mining sector faces some serious challenges, but companies have options that could help position them for the future, according to Deloitte Mining sector leader, Rick Carr.

After a steep fall in gold and silver prices in 2013, iron ore, coal, and copper followed suit in 2014. Fundamentals such as growing supply from new low-cost projects, a stronger US dollar, weak global demand, and credit restrictions in China have pushed prices of these commodities into a “technical graveyard.” Copper, for example, is trading close to its technical support level of $3 per pound, while iron ore prices are at a five-year low of $75 per ton.

Weakening prices and a sluggish outlook for demand growth have turned investors away from the mining sector. The S&P/TSX Global Mining Index fell by about 10 percent through the end of November 2014, while the S&P 500 rose by 11 percent. Given these market conditions, investors question the sector’s ability to address a decade-long productivity decline, improve capital efficiency, revive sinking shareholder returns, and service mounting debt and interest obligations.

Waiting for a market upswing or adopting traditional cost containment measures will not likely suffice to turn the sector around. Mining companies should consider pursuing innovation for sustainable cost reduction and margin improvement, embracing autonomous mining solutions by working closely with vendors, and leveraging data analytics to increase productivity, according to Deloitte’s Rick Carr.

Q: What would it take for a mining company to navigate the current environment and position itself for the future?

Rick Carr: It’s hard for many mining companies to avoid resorting to standard financial levers—reducing headcount, adjusting cash outflow to inflow ratio, limiting funding approvals to only the highest quality projects, and regulating discretionary spending—to navigate the current environment. However, these measures rarely stick; spending creeps back up to historical rates when the cycle swings upward, driving the company into a continuous cycle of cost cuts and cost creep. Positioning for success will require adoption of an alternative strategy.

One cost-effective opportunity would be to use this time, when demand is off its peaks, to focus on productivity and hone operational processes and procedures in readiness for efficient, scalable increases in output. Mining companies should institute a long-term cost management and operational improvement culture across the supply chain, from pit to port, by investing in technology. This encompasses a cost and value focused culture that is not cyclical, but deeply ingrained in the mindset of executives and employees. Rather than layer incremental technologies over existing operating models, the industry could work with equipment makers to design autonomous solutions, collaborate with technology firms to develop sensor-driven production visibility tools, and embrace mobile and modular solutions for bulk mining operations.

For example, at Glencore’s Ulan West mine in Australia, an
underground flexible conveyor system—the second of its kind in the country—is being installed to drive improved operations, increase safety, and lower total operating costs.

Increasing investment in innovation might seem countercyclical with today's weaker commodity prices, but these investments would separate profitable, growth-oriented companies from the pack and equip them with a sustainable competitive advantage, while the rest of the industry uses traditional measures to respond to the latest down cycle.

Q: What should the industry be mindful of as it develops strategies for 2015?

Rick Carr: The worldwide political, social, and economic equation is changing rapidly. Top mining nations that are reeling under low growth—Brazil, South Africa, Indonesia, and India—recently completed their general elections. Ruling establishments in these nations were either voted out by a record margin or returned with reduced majorities. Governments and social activists are increasingly leveraging social media to discuss social matters and environmental responsibility, including mining-related issues. So for mining companies to rebuild and broaden their relationships with new governments, they must embrace social media, both for public outreach and to preempt reactions from stakeholders.

Mining companies should also be mindful of their suppliers and contractors, whose situation is equally precarious. Rather than pressuring suppliers further by demanding deeper price discounts, mining companies can adopt several non-pricing mechanisms such as flexible contracting, inventory management, preventive inspections, and mobile maintenance programs. By working with key suppliers on how to take cost out of the solution versus simply trying to cut into supplier margins, companies can not only lower costs but also drive sustained improvements. This approach is designed to encourage valued suppliers and contractors to maintain the critical services mines rely on while teeming to improve total cost elements on both the operator and supplier side.

Q: What is the next big thing in the sector? Where are the opportunities amidst all the challenges?

Rick Carr: With the exception of a few large miners, much of the mining industry has not yet leveraged big data to the degree that other capital-intensive sectors have such as defense, nuclear power, and the oil and gas industry. The mining industry generates a million terabytes of data every minute—Rio Tinto’s iron ore operations in Western Australia’s Pilbara region, for example, alone produce 2.4 terabytes of data a minute—but much of that is only used for reporting purposes. Real-time analysis of data from connected machines, fleets, and people can open new chapters in increasing mine safety and productivity.

Although an acquisition may sound “adventurous” in today’s uncertain market climate, well-positioned mining companies may look to purchase mining operations that are cash constrained but have good long-term prospects. Rather than traditional corporate buyouts, mining companies can benefit from today’s buyer’s market by making joint bids, taking minority stakes, and partnering in late-stage development projects in the right commodities and regions.

Endnotes

2. FactSet. Returns are for the period January 01 to November 28, 2014.

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