The Global Economic Crisis – Worldwide Impact on Mining Companies[1]

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The current economic crisis has negatively impacted virtually every industry. Demand is down for almost all goods and services. This has hurt commodity prices for base metals such as copper, aluminum, nickel and zinc, which are driven by industrial demand. Precious metal prices, such as gold and silver, have generally held up better than base (industrial) metals, however, day-to-day prices, particularly for gold (which is viewed as a hedge against economic uncertainty), are extremely volatile.

The economic crisis: where are we today?

The mining industry has enjoyed a long bull market, driven by the boom in the so-called "BRIC" countries – Brazil, Russia, India and China. Starting at the bottom of the cycle in October 2001, commodity prices peaked sharply in July 2008 before the plunge. However, commodity prices are still well above historical norms, and are currently experiencing an upward trend:

	Current Price	**Cyclical Low**	**Cyclical High**
Base Metals			
Copper	US$1.97/lb	US$0.60/lb in 2001	US$4.10/lb in 2008
Aluminum	US$0.64/lb	US$0.55/lb in 2001	US$1.48/lb in 2008
Nickel	US$4.88/lb	US$2.50/lb in 2001	US$24.80/lb in 2007
Zinc	US$0.61/lb	US$0.30/lb in 2001	US$2.10/lb in 2007
Precious Metals			
Gold	US$882/oz	US$265/oz in 2001	US$1000/oz in 2008
Silver	US$12.14/oz	US$4.25/oz in 2001	US$22/oz in 2008

[1] This article is based on the presentation by Janne Duncan and David Knight, "The Global Economic Crisis – Impact on Mining Companies (and Mining Engineers)" given in Kingston to the Queen's Engineering Department on April 1, 2009, and on the presentation by Janne Duncan and Brian Levett at Mine Africa's "Surviving the Global Mining Crisis" given in Toronto on January 13, 2009 and again on February 28, 2009. See http://www.mineafrica.com/specializedseminars/survivingseminar-feb282009.htm for more information.

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"Cash is King" – cash flow is critical
Mining companies need cash in order to survive. There are 3 traditional sources of capital, however, these traditional sources are generally not available:

- Internal cash flow from operations: low commodity prices have had a negative impact on the ability of producing companies to generate revenue;

- Borrowing (issuing debt): credit is unavailable, as banks are afraid to lend (even to each other); and

- Equity (issuing shares): with stock prices down, companies issuing new shares to the public at low prices risk substantial dilution.

Any mining company that has access to any of these financial resources is encouraged to take advantage of them, wherever (and whenever) available. But, since these resources are generally not available, where does this leave mining companies today?

Exploration, development and production
In order to understand current markets, we need to distinguish between exploration, development and production companies (some companies undertake all 3 phases):

- Exploration companies - these companies look for (and hopefully discover) new deposits that can be developed into mines;

- Development companies - these companies develop the discoveries (upgrade resources to reserves, conduct feasibility studies and arrange project financing); and

- Production companies - these companies produce the minerals for sale.

Bringing a mine from exploration to production normally takes from 7 to 9 years.

Exploration and development
Exploration and development are very risky and highly speculative undertakings. Very few exploration companies actually find commercial deposits. Also, exploration and development companies generate no cash to fund operations or service debt. They are almost entirely dependent on risk equity which is very hard to find in the current environment.

As a result, many exploration companies are now hanging on for dear life. Some are looking to producers or other exploration companies with cash to buy them. Joint venture arrangements and sales of future production or royalty interests are other options.

However, unfortunately, many exploration companies will not survive. If they were able to raise money before the stock markets crashed, they may be able to last until market sentiment turns – but nobody really knows when that might be.

Production companies
Production companies may be enjoying the cash they generated over the last several years because of high prices driven by significant demand from the BRIC and other developing

countries. These companies need to continuously replenish their reserves as their existing reserves are mined out. They can do this either by buying reserves through acquisition of other companies, or through discovery and development of new mines.

Mergers & Acquisitions (M&A)
We anticipate continued consolidation in the mining industry, but the mergers will be different than during the "bull-run" period.

During the "bull-run", it was felt that larger companies could attract investors and undertake bigger projects. From 2005 to 2008, the number of mining deals world-wide roughly doubled, from 653 deals in 2005, to 1,300 deals in 2008. The number of deals over US$1-billion surged from 8 in 2005 to 25 in 2007.[3] Of note was Rio Tinto's acquisition of Alcan - the largest mining deal ever valued at US$43-billion.

Today, there are more friendly deals between junior and mid-tier companies that need strategic mergers in order to survive, and more "hostile" take-over attempts because of perceived gaps in value between what the selling shareholder thinks the target company is worth, and the company's current trading price which the bidder hopes to pay (usually a depressed market price, with some notional "control" premium).

Forecasts
Exploration companies are definitely at risk in the short and medium term because they are having great difficulty gaining access to capital. But production companies that are flush with cash from the high prices that have lasted for several years should be able to weather the storm – with prices still high by historical standards.

Canada is Still the World's Leading Mining Finance Market
The Toronto Stock Exchange (which lists mid-tier and senior companies) and the TSX Venture Exchange (which lists junior companies) are host to the most natural resource companies in the world, by number and by market capitalization. These stock exchanges offer the following advantages to international mining companies, wherever located, that wish to tap into the public capital markets:

- Sophisticated securities regulation - Canada's capital markets operate within a highly developed legal framework, and are well-regulated by the Canadian securities administrators (CSA) and Canadian stock exchanges.
    - National Instrument 43-101 - *Standards of Disclosure for Mineral Projects*, which is the guideline on how public companies can disclose scientific and technical information about mineral projects, is supervised by the CSA and is considered by many mining professionals to be the "gold" standard of disclosure of mineral resources and reserves.

[3] Source: KPMG LLP

- Sophisticated market players – Canada has highly experienced investment bankers, analysts, lawyers, engineers and other professionals in the mining industry.

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