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BHP Splits the Difference

No one wants to end up on the wrong side of a split personality -- something BHP Billiton investors should ponder.

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The Anglo-Australian miner is leaning toward spinning off a collection of assets to focus on its four core commodities. The ones to be shed are expected to include its nickel, manganese and aluminum assets and potentially thermal **coal**.

BHP, which reports full-year earnings on Tuesday, hasn't said how it would structure any such deal, an issue complicated by the **company**'s dual listing and the need to treat different sets of shareholders equitably.

One suggested option would be to spin off the assets to Australian shareholders, while offering compensation to holders of the London-listed stock. BHP did this in the 2002 spinoff of BHP Steel, now BlueScope Steel.

An idea floated in the Australian media is that the quid pro quo for shareholders of the London-listed shares would be a buyback of that stock. That wouldn't wash; buybacks of one line of BHP's stock benefit all its shareholders, because the boost to earnings per share is spread across the entire **equity** base.

In the case of BHP Steel, London investors instead received a bonus issue of PLC shares, equivalent to the value of the spun **company** being distributed to holders of BHP Billiton Ltd., the Australian **company**.

However any split is handled, it would create two very different **mining** companies.

The spun-off **company** would be a ragbag of generally unloved assets in commodities that have, until recently, been out of favor. BHP's aluminum, manganese and nickel assets generated $4.2 **billion** in revenue in its fiscal first half ended in December, but only $148 **million** of operating profit. Thermal **coal** prices, already depressed, have fallen further this year.

So the newly created miner would appear an old-school bet on commodities prices. Aluminum prices have ticked up recently on hopes of more demand, particularly from the automotive sector -- though the perennial problem of excess capacity still lurks out there. Meanwhile, nickel, despite recent falls, is up more than 30% this year on hopes that an Indonesian ban on exporting unprocessed metal ores would squeeze supply. There is more than a whiff of opportunism around the timing of this split if it goes ahead.

The remaining BHP, on the other hand, would be a more streamlined miner finally putting to rest its supercycle thinking of very broad diversification. It would be focused on **iron ore**, **copper**, metallurgical **coal** and **oil**. The spin would underscore its commitment to the new **mining** orthodoxy of efficiency, investment discipline and returning funds to shareholders.

In that sense, a split would be the most striking manifestation yet of the schism between the old face of **mining** and the new.

-- Helen Thomas

Coke Tames the

Monster Price

Coca-Cola is getting another jolt of caffeine. Its **purchase** of a 16.7% **stake** in **energy**-drink maker Monster Beverage for $2.15 **billion** in cash and some swapped assets is the latest bet on a category growing much faster than soft drinks overall. That should give Coke a boost, but also serves to emphasize the challenges in its core **business**.

Monster's stock jumped 30%, likely on hopes Coke will eventually **buy** the whole **firm**. Even absent that, Monster could nearly double its sales with full access to Coke's distribution network, according to Sanford C. Bernstein. Coke, meanwhile, buys another option on the world's changing drinking habits.

And Coke needs options. Analysts see sales falling slightly in 2014, the second consecutive year of declines. This partly reflects a shift in some markets toward ditching soda in favor of drinks seen as healthier.

Bets on faster-growing categories are one way to revive growth. Coke said in February it would pay $1.25 **billion** for a 10% **stake** in Green Mountain Coffee Roasters and partner with it to develop a single-serve system for cold drinks. Coke also has made significant investments in juice and tea. Sports and flavored **dairy** drinks might be areas of interest for future deals.

While mature companies seeking the elixir of growth often overpay for young upstarts, Coke's deal looks reasonable. Assuming the asset swap is a wash, the deal values Monster at $12 **billion**, net of cash on its balance sheet. That is 14.7 times 2015 earnings before interest, taxes, depreciation and amortization.

That is only slightly above Coke's multiple, and that is before any synergies are factored in. As down payments on the future go, this one looks easy enough to swallow.

-- Miriam Gottfried

Kazakhmys's Tightrope Routine

Kazakhmys is getting a fresh start as KAZ Minerals. That doesn't make it a **copper**-bottomed bet.

Investors voted Friday to approve a drastic restructuring of the London-listed **copper** miner, shedding its highest-cost production into a private vehicle owned by 36% shareholder Vladimir Kim. Given the challenges involved in such a plan, getting this far is no mean feat; Kazakhmys also negotiated a lower-than-expected cash payment of $150 **million** to the new entity as part of the deal.

Kazakhmys shares are up 45% this year in part because the restructuring addresses a central issue: that its better mines were destined to keep subsidizing money-losing assets that, politically, it couldn't close. Getting rid of its cash sinkhole, low-grade, labor-intensive **operations** in Kazakhstan's Zhezkazgan and central region, makes KAZ look investible again. But, even by the standards of emerging-market resources companies, it remains a risky bet.

After shedding about 70% of its production, KAZ will be a wager on the **company**'s ability to deliver its large-growth projects on time and on budget -- an area in which the **mining** industry has hardly covered itself in glory.

KAZ's 80,000 metric tons of annual **copper** output will be low-cost and needs relatively little investment. But that is dwarfed by Bozshakol and Aktogay, which together could produce more than 200,000 metric tons of **copper** a year at their peak.

Bozshakol is slated to start production toward the end of next year, which gives KAZ a high-growth outlook; J.P. Morgan Chase puts its annual **copper** growth rate at 28% from 2013 to 2018, versus 23% for First Quantum, or just 3% for Antofagasta.

But KAZ recently lowered its peak production guidance for the projects and increased its outlook for unit costs. The **company** already has upped the budget for Bozshakol to $2.3 **billion**, adding a second contractor to try to keep the mine on schedule. Spending at Aktogay is also under review.

The developments will also add to KAZ's borrowing. Net debt to earnings before interest, taxes, depreciation and amortization could approach 10 times at its peak before falling quickly, reckons J.P. Morgan. That is alarmingly high for a miner, but in this case may not be an issue. Most of KAZ's debt is from the **China** Development Bank, with covenants tied to asset values rather than Ebitda; it has the ability to repay other facilities if needed.

But KAZ will be extremely sensitive to copper prices, making for a volatile ride. Every 10% change in the copper price means a 55% change to 2016 earnings per share, notes Barclays, and an 84% change to the net present value of KAZ's cash flows.

Even for ardent fans of the orange metal, buying KAZ will require nerves of steel.

-- Helen Thomas

Gas Bulls

Sweat Out

A Cooler

Summer

Can you hear that? It's the deafening silence of New Yorkers not switching on their air conditioning units.

Easier to hear are muffled sobs from natural-gas traders. Having started 2014 with cheers as the polar vortex revived the price of their favorite commodity, they now see the same weather dynamic flooding the eastern U.S. with cooler air when the region should be stifling. That cuts demand for air conditioning, electricity and gas. Front-month futures, which poked above $6 per million British thermal units in February, are now below $3.80.

Even worse, unless winter is ferocious for the second year running, 2015 is shaping up to be another washout.

Natural-gas stocks were depleted by last winter, leading many to conclude that the need to rebuild them heralded a turn in the market's fortunes. By late March, inventories were 55% below their five-year average. But stocks have been catching up. In the week ending Aug. 8, they rose by 78 billion cubic feet. This caused a flurry of optimism as it was below estimates, but it was still way above what is normal at this time of year.

Besides cool conditions curbing demand, higher supply explains about half the unusually high injections into storage, says Tudor, Pickering, Holt & Co. The Energy Department expects inventories to finish October -- when injections usually end -- at just under 3.5 trillion cubic feet, about 10% below the average.

The risk for gas bulls is that injections into storage carry on for longer than usual this year, according to Teri Viswanath, an analyst at BNP Paribas. That is because of new pipeline capacity due to start up in the northeastern U.S., enabling more gas from the Marcellus and Utica shale basins to enter the broader market.

The current bottleneck can be seen in discounts regional producers offer; gas trades on the Leidy hub at under $2. They will take anything higher than that when pipes start up.

Output this winter could be 3.5 billion cubic feet a day higher than a year before, Ms. Viswanath estimates. That is equivalent to government estimates for growth in total U.S. gas demand for the entire period of 2013 through 2015.

Winter may be a few months away, but gas bulls should be feeling chills already.

-- Liam Denning

Overheard

Investors have put much faith in Applied Materials' pending merger with Tokyo Electron. And faith can be easily shaken.

Worries over the deal sent Applied's shares down nearly 8% in the three weeks leading up to its quarterly report last Thursday.

It regained about half that ground Friday on the back of good results.

Another positive: Executives said Applied is "engaged in dialogues with regulators around the world consistent with our goal of closing the merger before the end of the calendar year."

This despite the fact the firm had to refile a notification with Chinese regulators reportedly leaning against the deal.

Not so fast, said Pacific Crest. It noted that Applied's language had changed slightly from prior expectations for the deal to close this year. "We may just be paranoid," the brokerage noted, but this holds out the prospect of a delay to 2015.

Even so, Pacific is taking a glass-half-full view, arguing the stock's current level is warranted even if the deal fails.

Now that's a show of faith.

CO bhpstl : Bluescope Steel Ltd | bkhlp : BHP Billiton Ltd | bltplc : BHP Billiton PLC

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