



HD Moody's: Negative effect of weak **iron ore** prices on certain Australian issuers

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Moody's Investors Service says that the currently weak **iron ore** price will exert a direct negative impact on its rated Australian producers over the next 6-12 months with second-order effects on a host of other sectors.

"Lower prices -- combined with the general softness in prices across the whole commodities spectrum -- is exercising a flow-on negative effect on several issuers and sectors across the rated portfolio, including **mining** services, construction, and airlines," says Matthew Moore, a Moody's Vice President and Senior Analyst.

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Moore was speaking on the release of a Moody's special comment, titled "Impact on Australian Corporates of Decline in **Iron Ore** Price".

The report notes that **iron ore** prices, currently around \$84 per metric tonne (mt), are down considerably from the average for the six months to 30 June 2014 of around \$110 per mt, which is down from an average of around \$135 per mt in FY13. This is largely because of a significant rise in production capacity in Australia and, to a lesser extent, Brazil, as well as slowing demand in the key export market of **China**.

"To preserve margins, we expect the miners to reduce their scope of work and renegotiate contracts with the providers of **mining** services, which will in turn further reduce earnings and cash flows at the latter," says Moore.

Atlas **Iron** Limited's (B2 stable) credit profile will be the most affected, reflecting its position as a single-commodity producer with moderate cash costs. Atlas will be further impacted by widening price discounts for its **iron ore**, which is generally of lower quality than that from the major producers.

Of the major **iron ore** miners, Fortescue Metals Group (Ba1 stable) is the most affected as, unlike its peers, it is a single-commodity producer.

By contrast, the earnings and credit metrics for BHP Billiton (A1 stable) and Rio Tinto (A3 stable), while also experiencing pressure, are better positioned, given their lower cost profiles, improvements in debt levels, and benefits from product diversity.

Moreover, as part of initiatives to counter the weak price environment, the majors have been reducing their labor forces, meaning reductions in fly-in fly-out passengers. This trend is negatively impacting the airlines and airports, such as Qantas Airways (Ba1 negative) and Perth Airport (Baa2 stable).

A potential further reduction in capital expenditures for development would negatively impact the construction and engineering sectors, as companies, such as Leighton Holdings (Baa3 stable), face reduced project work.

Subscribers can access the full report at
http://www.moodys.com/viewresearchdoc.aspx?docid=PBC_175517.

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