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HD **BHP Billiton prepares to bury mining merger of century**

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The natural resources colossus is mulling what to do with unwanted assets, which may lead to it leaving London, reports Danny Fortson

A FEW DAYS after Paul Anderson unveiled the largest merger in the history of the mining industry, the American boss of BHP went on a Sunday talk show in Sydney to put politicians' minds at rest. They were concerned that BHP, the 116-year-old national champion known as "the Big Australian", was about to be lost to London.

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Anderson and Brian Gilbertson, head of smaller rival Billiton, had just announced their $28bn tie-up that would create a new natural resources goliath.

Billiton was already listed in London. BHP, meanwhile, ran its giant oil operation out of London. A relocation of the group headquarters from Melbourne seemed a distinct possibility. After all, the combined group would stretch across five continents and produce everything from diamonds and oil to nickel and iron. Why not run it from Europe's financial capital? The fears, Anderson assured, were misplaced. He said the merger was "a win-win". There would be housekeeping to be done but a headquarters move would not be part of it. "I'm sure there will be two or three things in the portfolio that we will want to sell off ... once we put the companies together," he said.

A few things indeed.

Thirteen years on, Andrew Mackenzie, the saxophoneplaying former BP executive who took over at the helm of BHPa year ago, wants to undo the deal. The Scot is considering a radical plan to spin off most of Billiton into a separate entity.

Goldman Sachs has been working on the initiative, called Project River, for more than a year. Mackenzie expects to decide by the end of the year whether to create a new, listed company stuffed with the group's unwanted assets or to sell them off piecemeal. These make up most of the former Billiton, including the aluminium, manganese and nickel operations.

Industry sources claim the move could lead ultimately to BHP pulling out of London, delisting its shares and closing its office in the capital to leave it with its original Australianlisted stock and headquarters in Melbourne. BHPhas poured cold water on the latter.

Finance director Graham Kerr said in February the company's dual listing "has worked and continues to serve shareholders well".

Yet Mackenzie's demerger and investor enthusiasm for it — analysts have universally praised the move — lead to a simple question. Was mining's defining deal a bust? First, some context. In the last decade alone, BHP Billiton has showered investors with $62bn in dividends. During that time only one big company's shares were a better investment than BHP Billiton's, which generated a 400% total shareholder return. That company? Apple.

Part of this is luck. Nobody knew that China was about to boom and send the prices of iron ore, copper and oil through the roof. The deal's timing was serendipitous. Indeed, in the 40-page presentation the companies put together to sell the deal to investors, China didn't get a single mention.

What the merger did, the company argues, was to equip it for the boom when it came, giving it the financial heft and access to London's capital markets to fund a giant investment programme. Since 2001, it has spent more than $120bn to expand its mines or buy new ones.

Some of this was badly invested. Indeed, Mackenzie was swept into the top job amid a clearout of chief executives in the industry after tens of billions were written off on over-budget mines and bad deals. BHP was no exception.

The company said:"The BHP-Billiton merger gave the combined company the structure, scale and capability needed to take advantage of the substantial growth in commodity demand created by China's urbanisation and industrialisation."

That may be. The question, however, is whether BHP investors would have done even better if Gilbertson had never convinced Anderson to scoop up Billiton, a ragbag of lesser assets centred on a core of aluminium mines and South African coal.

Analysts have valued the Project River assets at $15bn-$20bn — or about a tenth of the combined group's $184bn market value. BHP has cherry-picked a few Billiton projects, such as its Antamina copper-zinc mine in the Peruvian Andes, but the River assets trace back almost exclusively to Billiton.

It is worth remembering the circumstances that brought the companies together. It all started with a threatened takeover bid for Billiton from Anglo American.

In 2000, the South African tycoon Johann Rupert split up the Rembrandt Group, a sprawling empire that spanned Cartier diamonds, cigarettes and technology, founded by his father, Anton. Under the restructuring, he swapped the 7.1% stake held by one of the new companies he created, Remgro, to Anglo American in exchange for its shares in FirstRand, a bank. Anglo pledged not to make a bid for the company for a year, but the arrival of Billiton's much larger rival, as Anglo was then, on the shareholder register left Gilbertson with no illusions. His company's days were numbered.

He tested the appetite of rivals, including Rio Tinto, for a takeover, but no one was interested — except for Anderson. The pair announced a merger four months later.

An industry source said:"It was an absolutely incredible deal. What Gilbertson got for his shareholders was unbelievable."

The deal also provided an elegant exit for Anderson, who for personal reasons would soon have to leave Australia. When they unveiled it in March 2001, Anderson said he would make way by the end of 2002 for the chief executive in waiting, Gilbertson. In the event the latter lasted only six months in the top job before a clash led to his exit.

Three chief executives and more than a decade later, BHP is returning to its roots. Iron ore is one of the four pillars of the slimmed-down BHPthat Mackenzie has zeroed in on, with oil, copper and coal.

It is too simplistic to say the company is excising Billiton cleanly. The deal allowed it to sell its steel arm and bulk up in key commodities such as copper, yet the new commodities Billiton brought — aluminium, manganese and nickel — last year accounted for less than 1%of earnings.

The core of the old BHP, meanwhile, has exploded. Last year the company churned out 217m tonnes of iron ore from its giant operations in Western Australia and Brazil — nearly four times what the division produced in 2001.

Oil, accounting for a third of earnings before the deal, now makes up about a quarter. Today, though, it comes from the mammoth operations in the deep water of the Gulf of Mexico and American shale fields rather than Liverpool Bay, the Irish Sea reservoir that was once the unit's main profit centre. By the time BHP sold it in April it accounted for less than 2% of production.

Meanwhile, BHP's centre of gravity has gradually shifted away from the London corporate office that is another Billiton vestige. Last year it announced plans to build a 30-storey tower in downtown Houston to house its global oil headquarters. Much of the space at its London building, a stone's throw from Victoria station, is empty.

There is one other factor that could ease the separation. When the companies opted to keep the dual London and Sydney listings in 2001, they also kept alive the separate corporate entities.

On paper, the London entity remains the owner of the Billiton assets, while the Australian **company** houses BHP'sassets. It has the makings of an elegant exit.

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