

HD Cliffs Plans to Write Down \$6 Billion in Assets -- Update

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Cliffs Natural Resources Inc. is taking a \$6 billion write-down, mostly related to the ill-timed purchase of a Canadian iron ore mine intended to supply the then-booming Chinese steel market.

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The hefty write-off by Cleveland-based iron ore and coal miner, announced Friday, is the latest blow to a sector reeling from a 40% drop in iron ore prices from a year earlier due largely to oversupply and slumping demand in China. Iron ore is the main ingredient in the making of steel.

As prices fall, midsize players like Cliffs are getting squeezed by major miners BHP Billiton and Rio Tinto Ltd. in Australia, and Vale SA of Brazil, which produce more than 60% of iron-ore exports globally and continue to push production. The big three control massive mines, ports, and railroads, allowing them to produce iron ore at costs of \$50 per ton and below.

By comparison, Cliffs's costs at its Eastern Canadian operations were \$87.50 per ton in the second quarter. That division lost \$88.2 million in the first six months of 2014, after losing \$30.3 million over the same period in 2013.

Cliffs expanded in Canada in 2011 when it bought Consolidated Thompson Iron Mines Ltd. and its Bloom Lake mine in Quebec province for \$4.9 billion. "We have one problem child, and that problem child is Bloom Lake," Chief Executive Lourenco Goncalves said in an interview Friday. "[Cliffs] paid too much, and we are correcting what needs to be corrected."

At the time, Cliffs officials said they hoped to diversify from their traditional business of mining iron ore in Michigan and Minnesota and selling it to Midwestern steelmakers. Specifically, they wanted to ship ore from Canada to China, which produces around half of the world's steel and imports around two-thirds of all the iron ore traded on global markets.

But markets have been rocked this year as the big three miners have expanded production while Chinese steel production has eased up, prompting a drop in imports and iron ore prices. The price of iron ore imports into China have fallen 40% from year-ago levels to around \$80 per ton, from \$134 per ton. Prices for metallurgical coal, the other key ingredient in steelmaking, have also fallen.

The price decline has especially hurt iron ore companies with operations far from China. In the first eight months of 2014, iron ore exports to China from Canada were down 19% at 7.4 million tons. From Australia, exports to China rose 34% to 353.9 million tons.

In 2011, Cliffs "over-paid and over-invested based on high iron ore price," said John Tumazos, an investor and analyst at Very Independent Research LLC. "The write-off is not a business decision, it's simply acknowledging what is the status quo."

In an earlier interview, Mr. Goncalves said the big three producers "can have" the Chinese market, "I don't want to be a part of it."

Cliffs is seeking partners for its Canadian **operations**, and its Australian **iron ore** mines, which are still profitable but have trouble competing with the major miners. It is also seeking buyers for a chromite project in Canada, and its U.S. **coal operations**. Mr. Goncalves took office in August after a board coup orchestrated by activist shareholder fund Casablanca Capital LP.

Cliffs's strategy now is to re-center its business on the five mines in Minnesota and Michigan that supply **iron ore** to automotive-focused steel mills with **operations** in the Midwest, such as ArcelorMittal. With the auto industry prospering, those mines have been profitable.

Cliffs's stock fell 8% to \$8.74 on Friday. In the second quarter, the **company** swung to a net loss of \$1.9 **million**, from a year-earlier profit of \$133.1 **million**. Last week, S&P lowered the miner's credit rating to BB- from BBB- with a negative outlook, citing falling **iron ore** prices.

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