HD BEWARE THE “SHADOW BANKS” AS CHINA INVESTMENT CHANGES

WC 832 words

PD 28 May 2014

SN Mining Business Media

SC MIBMED

LA English

LP

Sydney, May 28

There will not be any significant immediate term funds coming out of China for magnetite iron projects in Australia or internationally, according to advisory firm, PCF Capital, as it warns of pending swings in global competition for exploration funds.

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The market changes also raise the spectre of “shadow bank” operations becoming a temporary force in mine project funding, but at much higher risk than conventional bank based debt.

Perth, Western Australia-based PCF Capital M/D Liam Twigger has told the Paydirt 2014 Latin America Downunder conference that current market dynamics point to China not expected to back any new magnetite iron projects for at least 5 years.

“China has 2 magnetite projects in Australia that it is struggling to get fully commissioned amid cost blowouts and other challenges – Citic’s Cape Preston Project and the Karara J/V, with a third being the development of Sino Iron’s Extension Hill. Until these projects (all in Western Australia) actually get up and deliver, there will be no more Chinese backing for magnetite projects either in Australia or overseas.”

However, Twigger says the good news is that the market now knows a lot more about magnetite operations and the detail required in feasibility studies.

”The only ones with any chance of success in attracting capital will be those with a measureable pathway to production and some relativity between the sponsor’s market cap and the amount of capital needing to be raised.”

He says this prevailing mood swing comes at a time Australia is trying to get a number of long mooted magnetite projects off the ground and into mining and export.

“Equity markets are now on the cusp of a turning point and magnetite aside, Australia should continue to present compelling value within the mood shift. The top tier investment sentiment will swing heavily and dominantly behind gold, copper and nickel.”

Twigger warns, however, that a collapse in market appetite for capital raisings via predominantly placements and rights issues, and to a much lesser extent IPOs, is seeing a material increase in companies seeking debt and increasingly accessing this from non-conventional sources allowing the emergence of “shadow banks.”

“For ASX investment, the value of placements and IPOs is down from around $A107B in 2009 to barely $14B or so in the first half of 2014, few of which have been mining plays. Equity has become hard to come by and entities are borrowing more to minimise shareholder dilution.

“On a global basis, this same capital starved trend has seen equity and debt raisings for gold and base metals fall from around $US23.6B in 2010 to barely $8.5B in 2013. The mix of capital access has also changed in this time from 70% equity and 30% debt, to now around 50:50 equity and debt.

“Within this, we have seen shadow banks emerge – basically metal trading and offtake parties as well as metal streamers -- which don’t have to operate within the regulatory and prudential constraints of traditional banks.

"They operate quickly and can provide large chunks of cash in return for offtake and marketing rights. The big unknown, however, is how these trading houses will act when things get tough – as they increasingly are – and that should worry project owners going down that route or considering such a credit line possibility."

Twigger points to Latin America's sustained investment appeal and **mining** performance over this period – and he expects it to continue to be so.

"At a time the global exploration spend is down 60%, compared to its all-time high in 2010, Latin America on a regional basis, will continue to dominate the global exploration spend and be at the forefront of new investment rallies, particularly as it presents a premium pricing for **gold** projects.

"On a one year average, the market is now paying up to 4 times to buy into a Latin American **gold** project – somewhere around $US86 an ounce – compared to only $22oz on a global basis. Even on a 3-year average, the **gold** premium is more than double for Latin America at $70oz compared to $37oz globally."

He points to new data showing Latin America remains at the forefront of global exploration appeal, accounting for 27% of last year's $14.4B spend – with **gold** dominating that activity – some 46% of budgets.

"In short, Latin America has retained the mantle as being the number-1 region for exploration expenditure for the past 20 years and this trend should continue."

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AN Document MIBMED0020140529ea5s00007

