

HD Baosteel plays to the power

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Technically, Baosteel's \$1.4 billion bid for control of Perth-based Aquila Resources is an iron ore deal; but looked at slightly differently and it's also a gold deal, because the Chinese steel giant is reminding the world of the golden rule of business that 'he who owns the gold makes the rules'.

There is no doubt that Baosteel, and its ultimate masters in the Chinese government, have the financial firepower to buy whatever they like at whatever price they're prepared to pay.

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But after acknowledging that China is sitting on the world's biggest pile of spare cash, there are questions left unanswered; not that Aquila chairman Tony Poli is hanging around waiting for an answer.

Mr Poli, who has a track record of knowing when it is best to sell, will trouser around \$400 million for his 29 per cent stake in Aquila.

Not a bad result for a few years' hard work.

Whether he could have got more and reclaimed his billionaire status is unlikely, because Baosteel's bid of \$3.40 for each Aquila share is generous given the weakened state of the iron ore market.

And that's when it becomes interesting to connect the dots in the Baosteel raid on Aquila and to wonder whether there is a connection between the two matters - Aquila's share price and the price of iron ore - and the degree to which the latter (at least) has been influenced by decisions in China.

And while it might offend Baosteel to suggest it has been anything other than the fortunate beneficiary of such good fortune, the company has enjoyed a remarkable run of luck - with the sharp fall in the iron ore price in recent months coinciding beautifully with the bid for Aquila.

Back on May 5, when Baosteel first made its offer for Aquila, the iron price had already started to fall. From as high as \$120 a tonne earlier in the year, the price had retreated close to \$105/t.

That fall should have been more than enough to convince Aquila shareholders that \$3.40 was a very attractive price, given that their shares had been trading at \$2.45 immediately before the bid and that the iron ore price was falling - because Chinese steel mills had cut back on their orders.

The biggest of those Chinese steel mills buying less Australian iron ore is Baosteel; and that's where the interesting question lies. Baosteel is buying less iron ore while also busy launching a takeover bid for an emerging Australian iron ore producer.

Obviously Baosteel has an optimistic view on the future for iron ore or it would not be trying to buy its own Australian iron ore mine.

Equally obviously, it views \$3.40 as a fair price for Aquila, and can demonstrate that by pointing to the current iron ore price of around \$90/t.

And then there is a third factor - Chinese determination not to pay over the odds for another Australian iron ore asset in the same way it overpaid spectacularly for the ill-conceived and poorly designed Sino Iron project near Karratha.

For Baosteel, the timing is right for its Aquila bid - and Aquila shareholders understand that \$3.40 is the best they can hope for in a falling market for **iron ore**.

In theory, that makes everyone a winner; and while we will never know why the **iron ore** price started falling just before the Baosteel bid in early May, and kept falling over the past six weeks, it will restore some of **China's** lost credibility in the WA **iron ore** industry.

Sino **Iron**, which was supposed to cost \$2.5 **billion** but has already cost \$8 **billion** and is yet to hit nameplate capacity, taught **China** a painful lesson about doing business in Australia and on the importance of choosing the right local partner.

With Aquila, the deal seems likely to be wrapped up at the price first offered - which is unusual in a takeover these days - and a rock-solid partner in Aurizon has been chosen to work alongside the Baosteel team in developing Aquila's West Pilbara project.

Would that have been possible if the **iron ore** price had not fallen in such a timely manner?

That a question to which we will never know the answer. It's also one not many people will ask, because everyone involved is getting ready to walk away with a smile from a deal that has produced a surprising number of winners.

CO aqres : Aquila Resources Ltd. | baois : Shanghai Baosteel Group Corp

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