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HD **Roy Hill looks a winner to its lenders**  
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**Iron ore** price weakness means different things for different producers and prospective producers, as the \$US7 **billion**-plus debt financing package for Gina Rinehart's \$US10 **billion** Roy Hill **iron ore** project underlines.

Export credit agencies in Korea Japan and the US, and a consortium of 19 banks including Australia's big four have agreed to provide \$US7.2 **billion** of debt funding for the project, which is owned 70 per cent by Rinehart's Hancock Prospecting, 15 per cent by Marubeni Corporation of Japan, 12.5 per cent by the Korean steel maker Posco, and 2.5 per cent by Taiwan's **China** Steel Corporation.

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The banks will provide about a third of the money in their own right, and a similar amount backed by guarantees from the five export credit agencies - the Export-Import Bank of Korea, Korea Trade Insurance Corporation, Japan Bank for International Co-operation, Nippon Export and Investment Insurance, and the Export-Import Bank of the United States. The final third will come from the export agencies themselves.

Roy Hill will start exporting several years later than originally hoped, but the signing of the debt deal despite recent weakness in the **iron ore** price vindicates the strategy that Hancock and its joint debt advisers, BNP and NAB, pursued.

Two years ago Hancock sold a 30 per cent **equity stake** in the project to Marubeni (15 per cent) Posco (12.5 per cent) and **China** steel (2.5 per cent).

That created a base for debt negotiations by securing initial funding for the development and also locking in export markets. Roy Hill's 30 per cent shareholders will between them buy more than 30 per cent of Roy Hill's **iron ore** production.

Another slice of production is reserved for **Chinese** steel mills, and a year ago Roy Hill signed a fixed-price project construction contract with Korea's Samsung group.

Informal debt discussions with export credit agencies began around the time the Japanese, Korean and Taiwanese groups acquired **equity** in the project and committed as customers, and kicked off formally in December 2012.

By that time, the **iron ore mining** industry had received a shock. After peaking above \$US190 a tonne early in 2011, the **iron ore** price fell below \$US140 a tonne in the middle of 2012. It plunged below \$US100 a tonne in August, and hit a low of \$US86.70 a tonne in early September.

It was back above \$US110 a tonne by the time the Roy Hill debt financing talks began in December, however, and the introduction of Marubeni, Posco and **China** Steel as shareholder-customers and the subsequent signing of Samsung as **lead** project contractor created a pathway for the negotiation of credit agency funding from Japan and Korea. That in turn gave the private banks more confidence to participate. The debt raising was over-subscribed in the end.

All the groups taking exposure are making a call on Roy Hill's underlying economics. They won't know for sure that they have backed a winner until the mine is up and running.

The lending group has agreed to finance the project despite renewed pressure on the **iron ore** price that pushed it to a low of \$US104.70 a fortnight ago (it was \$US110.70 on Friday). However, they are doing so because they believe Roy Hill has plenty of commercial headroom.

The mine is slated to begin exporting in September 2015, and is expected to ramp up to production to 55 **million** tonnes a year by 2018. It will tip extra **iron ore** into the global market, adding pressure on prices that experts including Citigroup and Goldman Sachs think are headed down towards \$US80 a tonne in the medium term. But Roy Hill is expected to be a relatively low-cost producer, sitting comfortably below the 40th percentile of the global cost curve for **iron ore** mined, delivered and loaded for export.

That's not the lowest cost base in the Pilbara. Rio Tinto leads the pack, followed by BHP Billiton. Roy Hill's debt suppliers must be confident, however, that the project will be in a similar position to the two Pilbara giants after it ramps up: able to keep producing in the face of price weakness, in the expectation that production cuts that pull up on the **iron ore** price will eventually be delivered by higher-cost competitors.

#### Fed's cautious game

The markets continue to jump at shadows. They fell on Thursday after US Federal Reserve chairman Janet Yellen told a news conference that the Fed's commitment to hold its benchmark federal funds rate at close to zero for a "considerable time" after it finished unwinding quantitative easing "probably means something on the order of around six months".

That would see the fed funds rate moving up by the middle of next year, about six months earlier than the market hoped for, but Yellen added the obvious caveat: it all depends on how the US economy is travelling.

At its midweek meeting the Fed continued to reduce its quantitative easing cash splash for the US economy, but also said it was no longer tying rate increases to a sub-6.5 per cent US unemployment rate.

Unemployment is already down to 6.7 per cent, and it is no longer a trigger because the Fed thinks it may be overstating the strength of the jobs market and the economy.

The Fed will take a wider read before moving, will not move if the economy weakens, will be moving off the lowest-ever base when it does start pushing rates higher, and doesn't expect to take rates as high as it usually does in the rate-rise cycle. Not exactly a recipe for a market meltdown.

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