

SE Business
HD **Forrest digs his way out of a hole**
BY Elizabeth Knight
WC 788 words
PD 16 January 2014
SN The Age
SC AGEE
ED First
PG 28
LA English
CY © 2014 Copyright John Fairfax Holdings Limited.

LP

Eighteen months ago Andrew Forrest experienced the early 1990s Rupert Murdoch moment - a financial crisis resulting from the inability to digest debt used to fund rapid expansion. Corporate historians will remember Murdoch's survival came down to the wire and his recovery is now legendary.

Forrest's story of clawing his way back from the brink is just as tantalising - combining a mixture of the man's ability to convince debt markets to renegotiate deals, and luck that the **iron ore** price has defied gravity over the past year.

TD

The renaissance of Forrest's Fortescue Metals took another step on Wednesday when chief executive Nev Power said it would again accelerate its debt reduction by redeeming \$US1.6 **billion** of unsecured notes next month.

Power said the **iron ore** price had held up even better than he had expected and he did not see the price of **iron ore** moving much in 2014.

Last month Fortescue repaid \$US1 **billion** in debt and a lease facility. These initiatives, combined with Forrest's successful negotiations to lower the cost of remaining debt, have shaved \$US3 **billion** off the group's debt in as many months and reduced interest payments by \$US300 **million**.

Fortescue remains at the risky end of producers but if the **iron ore** price remains at even close to the current \$US130 a tonne the rapid reduction in debt should allow the **company** to fulfil its dream of producing 155 **million** tonnes annually.

The plan is to continue to expedite debt reduction to a more conservative gearing of 40 per cent, which represents net debt of about \$US5 **billion** to \$US5.5 **billion**. The days of scorched earth over costs are not over but the **company** supply of Tim Tams is no longer threatened.

The bigger issue is that talk of selling a **stake** in Fortescue's rail and port infrastructure is no longer a feature of its financial landscape. The **sale** has not been taken off the agenda but it has been postponed so that the market largely is no longer factoring it into the equation. The **company** said it did not get an attractive enough offer but the reality is that Fortescue no longer needs the proceeds.

While it has some scheduled debt repayments to make in 2015, the big licks do not fall due until 2018. And as production moves towards 155 **million** tonnes, Fortescue will receive tailwinds from increased revenue, lower production costs and reduced interest payments.

Getting to a point where increased cash flows would remove the increased leverage taken on to fund the expansion was always a juggling act for Forrest. This week's announcement suggests the scales are tipped in Fortescue's favour.

It would have been a different outcome had the **iron ore** price sunk below \$US100 a tonne, as many analysts expected. While some were more bullish, it is safe to say that none predicted the **iron ore**

price would have survived the last quarter of the 2013 calendar year at current levels. And the experts still predict prices will soften in 2014. But the worst of the danger period is now over for Fortescue.

There has been a similar division between analysts on whether Fortescue is a good punt or an accident waiting to happen. Short-sellers harvested fantastic returns late in 2012, betting on Fortescue's share price to fall.

And some experts remain of the view that Fortescue is too risky - recommending BHP or Rio Tinto as a safer exposure to **iron ore**. But its sharemarket performance has been stellar since it hit a low in June last year, improving about 80 per cent, including a 16¢ gain on Wednesday. And this is more than can be said for BHP and Rio.

Bullish outlook

At the head of the bull herd, Deutsche Bank's Australian head of strategy, Tim Baker, released his Ten Key Questions (and answers) for the 2014 year. Among them was the inevitable one on the strength of commodity prices, and he takes the view that demand will remain, and taking a 90-year perspective that current prices are not particularly high.

Baker agrees with a number of strategists that the sharemarket will continue its positive run in 2014 in the face of corporate downgrades. The broad consensus among investment banks is that markets will rise again this year, but more modestly.

Baker says downgrades to earnings happen most years and over the past six months the rate of downgrades has been quite mild.

Deutsche's positive outlook for commodities is fed by its view that **China's** GDP will grow by 8.6 per cent this year.

IN i22 : Primary Metals | i221 : Iron/Steel/Ferroalloys | imet : Mining/Quarrying | ibasicm : Basic Materials/Resources

NS c171 : Share Capital | reqmmm : Suggested Reading Metals/Mining | c17 : Funding/Capital | cactio : Corporate Actions | ccat : Corporate/Industrial News | ncat : Content Types | nfact : Factiva Filters | nfcpin : FC&E Industry News Filter | redit : Selection of Top Stories/Trends/Analysis | reqr : Suggested Reading Industry News

RE austr : Australia | apacz : Asia Pacific | ausnz : Australia/Oceania

PUB Fairfax Media Management Pty Limited

AN Document AGEE000020140115ea1g0004j