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HD **Resources boom long way from swinging to bust**

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There's a new reality for business in the state as miners look to cut costs

THE bigger they come, the harder they fall.

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That's how Deloitte Access Economics sums up the West Australian economy as the state adapts to the end of the biggest boom in its history, a feverish period of investment in mega-resources projects that created tens of thousands of jobs and generated incredible wealth.

Just as the decade-long boom was huge, the slowdown feels that way, too. WA has entered a transition period during which the key driver of its economic growth is shifting from construction to production, as scores of major projects are built and begin exporting to key Asian markets.

This new era promises to deliver billions of dollars in tax and royalty revenue to governments.

But it also means there will be lower spending on the ground and fewer jobs for the armies of cashed-up construction workers who have been building huge projects, such as Chevron's Gorgon and Wheatstone LNG developments, and the Pilbara iron ore expansions of miners Rio Tinto, BHP Billiton and Fortescue Metals **Group**.

The recent collapse of Perth-based mining contractor Forge **Group**, and the subsequent loss of 1800 jobs, is emblematic of an industry that is desperately trying to slash costs and struggling to cope with the end of the good times.

According to the WA Department of Mines and Petroleum, there are still more than $140 billion worth of projects either committed or under consideration during the next few years.

But closer analysis shows that this pipeline of big projects is rapidly drying up. Chevron's $US54bn ($58.24bn) Gorgon LNG project in the Pilbara — the biggest resources development ever undertaken in Australia — accounts for a big chunk of the $140bn in investment, yet construction of that project is due to be completed by early next year.

"The total value of projects has continued to trend down, as project completions have outpaced the new developments coming on line," Deloitte said in a recent report on the state of the WA economy. "All else (being) equal, that leaves a $100bn hole in the project pipeline." Although WA's tumble from its economic zenith has been painful at times, nobody should be feeling overly sorry for the resource-rich state.

The value of the state's mineral and petroleum sector hit a record $113.8bn last year, breaking the previous record of $108bn set in 2011, according to figures released by the WA government. The fall in prices for most commodities during the past year was more than offset by the gains made from the depreciation of the Australian dollar and increases in the total volume of commodities **sold**.

The WA Chamber of Commerce and Industry is forecasting the state will record economic growth of 5 per cent in 2013-14 and a further 4.75 per cent next financial year, underpinned by the lift in commodities exports.

It says continued strong population growth, rising consumer confidence and a still-low unemployment rate will drive consumer spending up by 4 per cent this year and another 4.5 per cent in 2014-15.

Dwelling investment is expected to grow by 10 per cent in 2013-14 and a further 5 per cent next year.

And despite the spate of recent job losses, WA's unemployment rate fell by one percentage point, from 5.9 per cent to 4.9 per cent, in March.

In recent weeks, WA's two best-known mining billionaires — Andrew Forrest and Gina Rinehart — have achieved major milestones at their iron ore projects in the Pilbara, defying the naysayers who have long argued that the price of the export commodity will collapse because the market is headed for drastic oversupply.

In late March, Forrest presided over a ceremony to formally mark Fortescue's long-held goal of producing iron ore at the rate of 155 million tonnes per annum and the completion of the miner's $US9.2bn expansion program.

Forrest was particularly delighted that this expansion had been achieved at a time that many analysts had consistently — and wrongly — predicted that the iron ore price would fall to around $US80 a tonne.

(The price has remained well above $US100 a tonne, delivering viability to Fortescue's mines).

"Analysts said none of this would be built until 2018,'' Forrest said at the **site** of Fortescue's Kings mine at its Solomon hub. "So look around you now and look at how wrong that assessment was." A few days earlier, Rinehart announced she had finally secured the funding for her own $10bn iron ore mine, Roy Hill, in the Pilbara, fulfilling a vision started by her prospector father Lang Hancock in the 1950s.

Rinehart's $US7.2bn debt package is the biggest project financing ever completed for a mining project worldwide. That she was able to raise the money at the denouement of the **China**-fuelled commodities boom proved that high-quality projects can still proceed in this market.

If all goes to plan during construction, Rinehart will be sitting on a mine capable of producing 55mtpa of iron ore by the end of 2015.

All of this means WA's resources sector is hardly grinding to a halt. But it is undeniable that there is a new reality for business in the state.

Forrest and his chief executive at Fortescue, Nev Power, are unwilling to commit to expanding the miner's operations beyond 155mtpa. That's because the famously bullish **company** is pausing for breath for the first time in its 11-year history as it seeks to repay its debt pile and bring costs under control. Power remains confident, however, that **Chinese** steel demand will support the price of iron ore, meaning future investment is still possible.

"There's quite a bit of new supply coming into the market, but most of that has already come in, with a large (part) of that coming from ourselves and other Pilbara miners during the last 12 months,'' he says. "We're seeing that supply being absorbed by incredibly strong steel and imported iron ore demand.'' The multinationals are also slowing things down, with an intense focus on cost-cutting and productivity gains.

Rio Tinto is planning to save up to $US3bn by pursuing brownfields expansions in the Pilbara rather than building expensive new mines. BHP has put plans for new iron ore mines and other infrastructure on the backburner, while looking to sell its nickel and aluminium assets in the state.

But it's in the capital-intensive petroleum sector that spiralling costs are really being given the squeeze.

At the Australian Petroleum Production and Exploration Association annual conference in Perth last month, the mood was vastly different to past years, as senior oil and gas executives lined up to warn about the need to slash costs.

Federal Industry Minister Ian Macfarlane set the tone when he declared that wages and conditions had become so generous in the LNG sector that he doubted whether any new projects, or any planned expansions to existing projects, would go ahead in the next decade.

Four LNG projects currently under construction off WA's coast are all due to come online in the next few years.

Chevron's Gorgon Project on Barrow **Island** is scheduled for start-up early next year, while the US-owned **company**'s $US29bn Wheatstone project, near Onslow, is due to be operational in 2016.

Japanese **company** Inpex's Ichthys project, which will process gas from WA's Browse Basin at Darwin, is expected to be operational in 2017, around the same time Royal Dutch Shell's Prelude floating LNG project off WA's northern coast is also scheduled to begin exporting.

Other key projects, including Woodside Petroleum's planned Browse LNG onshore plant in the Kimberley, have been abandoned because of fast-rising costs. But the Woodside-operated North West Shelf and Pluto LNG projects in the Pilbara have been operating since 1989 and 2012 respectively.

Macfarlane told the APPEA conference that trade unions had been able to secure wages and conditions for some construction workers that were unrivalled anywhere else in the world, including salaries in the hundreds of thousands and a $40,000 annual allowance for sharing living quarters with another person.

"To pay someone $40,000 a year to do that, you don't have to be Einstein to work out that that's driving our costs through the roof," he said.

"I think two years ago I said there wouldn't be another greenfields (project) in Australia for LNG; I'm starting to wonder if there'll be a brownfield in the next decade." But not everyone is so keen to write off future LNG investment in WA. Industry consultant RISC says the factors that have driven cost blowouts in LNG projects are not necessarily confined to Australia.

And it does not agree with the conventional wisdom that the shale gas revolution in the US, as well as planned new projects in Canada and East Africa, will render future Australian LNG projects uncompetitive.RISC principal adviser Martin Wilkes says the recent decline in value of the Australian dollar makes Australian projects more competitive, as does the country's proximity to major Asian markets, where he believes demand will remain high.

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