Opportunistic financing and treasury strategies for miners in a 'new normal' market

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While the recovery in commodity prices has alleviated much of the immediate balance sheet pressure to divest assets, mining and resources companies remain keenly focused on capital discipline, balance sheet strengthening and portfolio optimisation.

WITH SUSTAINED EFFORTS TO maximise operational efficiencies delivering progressively stronger cash flows and more attractive margins for miners, recent asset sales have been principally undertaken on a strategic basis – in order to realign portfolios and reduce debt – with vendors seeking to achieve full value from divestments.

Notwithstanding improvements in the credit outlook for the sector, strategic buyers, in turn, are evaluating opportunities cautiously. Mining companies are applying heightened financial discipline in their pursuit of growth. Portfolio alignment remains a critical focus for miners, as they consider both organic capital investments and inorganic growth options.

FINANCING AND TREASURY STRATEGIES KEY IN DELIVERING CAPITAL EFFICIENCY – AND ACHIEVING COMPETITIVE ADVANTAGE

Despite improved forecasts, operational efficiency, cost containment and productivity enhancement remain vitally important across the sector. As part of a business-wide concentration on capital discipline, miners are looking beyond traditional financing approaches, to a range of alternative funding structures designed to enhance balance sheet efficiency, optimise working capital, extract liquidity and reduce reliance on external debt funding.

Structured leasing arrangements and sale and leaseback transactions are tailored:

- to maximise value from the relevant assets while allowing the corporate lessee to retain operational flexibility; and
- to release capital from the corporate's balance sheet.

As part of a vigilant approach to managing cash and minimising risk, corporate treasurers are also opportunistically employing securitisation and other financing techniques:

- to monetise accounts receivables;
- to enhance supply chain arrangements; and
- to optimise inventory management.

Funding quality has become a competitive differentiator within industries, and working capital optimisation is a critical enabler for value creation. Capital efficient businesses are better placed to finance investment and growth, and more resilient in the face of market volatility, scarcer liquidity and increases in funding costs.

STRATEGIC LIABILITY MANAGEMENT FOCUSES ON REDUCING THE COST OF CAPITAL, EXTENDING THE CORPORATE MATURITY PROFILE AND ENHANCING OPERATIONAL FLEXIBILITY

While mining and resources companies have already achieved significant deleveraging, balance sheet strength and productivity remains a priority across the sector. Further opportunities to reduce debt and diversify funding sources are presented as strategic divestments are executed and operational efficiency gains realised.

With significant maturities looming during the next 18 months, miners are proactively focused on maximising execution certainty, including through early debt refinancing. Opportunistic early capital markets issues – undertaken prior to the maturity of existing instruments in order to take advantage of favourable market conditions, competitive pricing or other commercial imperatives – are facilitated through tender offers, exchange offers and various other liability management strategies.

Liability management is also advantageous where an issuer's outstanding notes are trading at a discount; by repurchasing its notes at less than par and then cancelling such instruments, the issuer is able to improve its capital position.

Tender offers (whereby an issuer makes an offer to repurchase outstanding notes for cash) and exchange offers (pursuant to which an issuer offers to exchange existing instruments for new notes having an extended maturity, a lower interest rate or different terms) facilitate the retirement of all or a significant portion of a class of debt securities.

Privately negotiated and open market purchases may be undertaken where an issuer is seeking to only repurchase a small percentage of an outstanding class of debt securities; however, such purchases must be executed in a manner that avoids triggering application

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of tender offer rules under the US Securities Exchange Act and related regulations. Moreover, in advance of any liability management exercise, an issuer must consider whether it is in possession of material non-public information that securities laws require it to disclose.

Where not required by the terms of relevant debt instruments and bank facilities, mining companies may also elect to apply proceeds realised from strategic divestments to repayment of outstanding debt – thus achieving further deleveraging and reducing interest costs.

STRATEGIC FINANCING OPPORTUNITIES FOR STRATEGIC BUYERS

With improved sentiment across the sector, and a narrowing in the valuation gap that has hampered successful execution during periods of rapid commodity price recovery, industry players are well placed to pursue strategic acquisitions.

Divestment activity – particularly in respect of metallurgical and thermal coal assets, smaller size operating gold and copper assets, and exploration assets – is anticipated to continue to present opportunities for single asset or pure play companies to acquire high quality assets and for mid-tiers to consolidate their positions through the acquisition of assets that fit strategically within their portfolio.

While capital investment remains restrained and, with notable exceptions, transactions have generally been smaller, strategic buyers will require that event-driven debt financings are structured to ensure maximum operational flexibility for the business going forward.

Senior notes offered in the US high yield market feature incurrence covenants – tested only when the corporate issuer wishes to incur additional debt or undertake certain other corporate actions (such as paying a dividend or making an investment).

In contrast, traditional bank facilities reflect financial maintenance covenants, assessed semi-annually or quarterly. Subject to market openings, event-driven financing can be accomplished through the issuance of 'acquisition bonds' prior to the closing of the acquisition; more typically, a senior notes issuance refinances acquisition bank debt.

In addition, alternative sources of funding, such as streaming, offtakes and royalties, can be employed in conjunction with traditional debt and equity raisings to finance acquisition transactions and project development.

CORPORATE TREASURY TEAMS CAN BE VALUE CREATORS

Strategic financing and treasury approaches facilitate capital efficiency, enhance liquidity and strengthen miners' resilience in the face of cyclical shocks. The opportunities for value creation afforded through operationally efficient, tailored funding solutions are significant.