

QRC STATE OF THE SECTOR

DECEMBER QUARTER 2018





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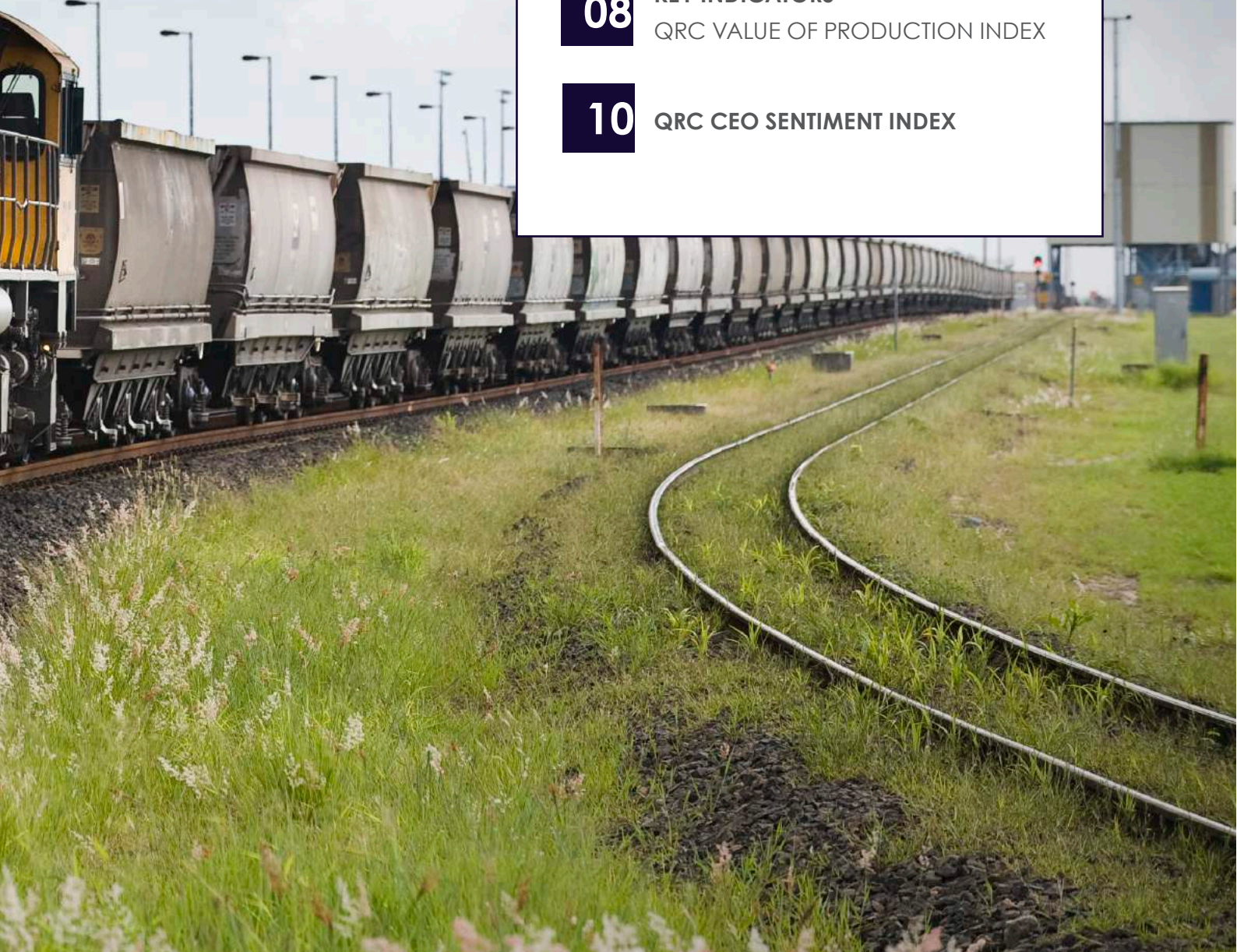
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DIGGING DEEPER FOR SHARED VALUE

The whole mining industry needs to have a much more compelling narrative about its contribution to society...we are seen as part of the problem and not part of the solution"

JS Jacques Chief Executive Officer, Rio Tinto

The Edelman Trust Barometer, a global annual survey measuring the state of trust in society, highlighted in 2018 that trust across all Australian institutions, media, NGOs, government and business is now at 'crisis point' with Edelman CEO Steven Spurr commenting, **"trust cannot fall much further in Australia"**. While early signs from the recently released [2019 survey](#) indicate a slight recovery from 2018 levels, distrust continues to persist in Australia.

Unlike corporate reputation, which is based on past actions, trust is a leading indicator of performance. Stakeholders give trusted organisations scope to take risks, experiment and enter new markets¹, not to mention the employee attraction and retention benefits. In the foreword to the landmark Shared Value Initiative Report *Extracting with Purpose*² Harvard Business School Professor Michael E Porter said:

...the norm is to respond to conflicts by focusing on the visible causes of tension – protests, permit delays, negative media coverage and demands from local influencers – so-called non-technical risks...[however, this approach], is not an effective long-term community engagement strategy, nor does it deliver meaningful societal outcomes"

Today, more than ever, a strong licence to operate built on trust is vital to the success of resource operations, with EY suggesting it is the number one business risk facing mining and metals in 2019-20 and should be at the top of the agenda for leadership teams³.

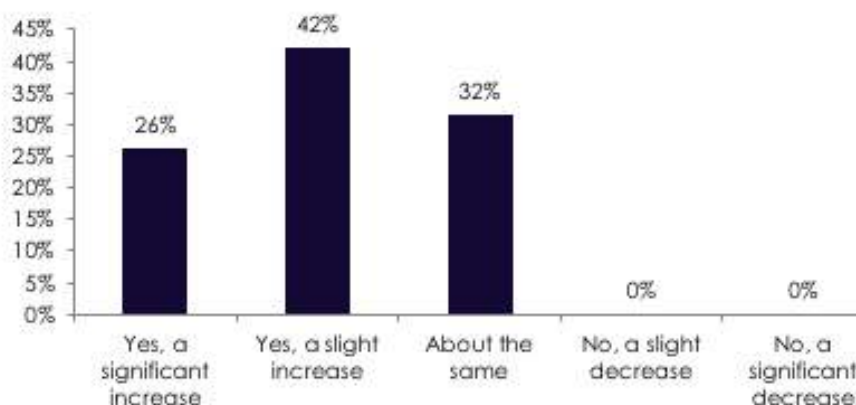
QRC member CEOs recognise the business challenge that low levels of trust presents with 94% concerned the lack of trust in Australian businesses and government will have implications for the resources industry in Queensland. Their concern is warranted. Of the 15 business sectors ranked in the 2018 Edelman survey only 'energy' and 'financial services' were the least trusted to 'do what is right'.

This trust deficit means companies are increasingly focusing their time and resources on this area. 73% of QRC members report community and social performance is embedded in their day-to-day business decision making and 84% of CEO's estimate they spend about the same or more time on community and social aspects of their business as they do economic and technical. An overwhelming majority expect this to increase over the next 12 months.

Along with their own time, 68% of member CEOs anticipate they will increase their internal capability to address community and social performance challenges over the next 12 months. The remaining 32% will 'maintain' their capability, with no companies anticipating a decrease in resources for this area.

CHART 1: GROWTH IN COMMUNITY AND SOCIAL PERFORMANCE CAPABILITY

Over the next 12 months, does your organisation plan to increase community and social performance capability?



Source: QRC December 2018

“As an industry, we need to be strengthening our linkage with our communities and local stakeholders. Mining offers so much locally - yet we are not doing a great job in reinforcing these links”

QRC CEO Sentiment Survey

At the local level, member CEOs indicated regional communities continue to report enhancing employment and business opportunities as the key issues for their regions, followed by managing environmental impacts.

“Licence to operate has evolved beyond the narrow focus on social and environmental issues. There are now increasing expectations of true shared value outcomes from mining projects”

EY, Top 10 business risks facing mining and metals in 2019-20

QRC members invest heavily in regional communities within their operational footprint. The QRC 2017-18 Economic Contribution Report found 1,260 community groups were supported by surveyed companies. This represented a 38.5% increase compared to 2016-17. Company investment approaches continue to evolve and although sponsorships and donations feature in investment portfolios, the focus has shifted over time to support community-driven, long-term partnerships.

Some recent examples include the [Rio Tinto Western Cape Community Development Fund](#) where funding is linked to the socioeconomic baseline and community plans and local stakeholders are involved in the decision making process. Another example is the [Shell Business Navigator partnership](#) with Toowoomba and Surat Basin Enterprises, an in-region accelerator program that aims to support and develop existing and new businesses in the Western Downs, an economic development priority for the region.

Resource companies are also starting to think about Shared Value and 30% of member CEOs report implementing shared value initiatives in their organisations. Shared value is defined as activities that measurably improve socio-economic outcomes, while also improving business performance (e.g., decreased operational costs, enhanced productivity, and/or a predictable and stable business environment).

“Shared value is not social responsibility, philanthropy, or sustainability, but a new way for companies to achieve economic success”

Michael E. Porter and Mark Kramer, “[Creating Shared Value](#),” Harvard Business Review

This is a huge area of opportunity for companies to simultaneously deliver shareholder and social value. An example is the [Evolution Mining Shared Value partnership](#) with the Gudjuda Reference Group Aboriginal Corporation to establish a native plant nursery and market garden. The project will create jobs, provide industry-related transferable skills for Indigenous people in the region and will generate much needed revenue for Gudjuda to grow their training arm. Evolution anticipates cost savings through the local purchase of native plants for their site rehabilitation activities.



Image: Eddie Smallwood, Chairman of Gudjuda, with Evolution employees

DIGGING DEEPER FOR SHARED VALUE CONTINUED

“Use of local town sewage water for mine processes and dust mitigation”

“Local property leasing for primary production and assists with land management”

QRC CEO Sentiment Survey

The survey results suggest more work can be done in the industry to understand the outcomes of social investment programs, with only half of respondents confirming their social investments are underpinned by a monitoring and evaluation framework. This final step is critical to move beyond 'dollars spent' and demonstrate the broader social value created, along with ensuring continuous improvement of programs and decision making.

“As the mining industry's value proposition is increasingly called into question, mining companies are beginning to see that they cannot succeed into the future unless they change the way they operate. This is about more than enhancing efficiencies. It's about re-establishing trust with stakeholders and collaborating to devise better responses.”

Deloitte, Tracking the Trends 2018

Heading into 2019, the business sector, including the resources industry, will increasingly be judged not only on their financial performance but on their relationship with employees, communities and regulators as well as their impact on society at large. Companies developing positive community partnerships and earning and maintaining licence to operate is becoming a pivotal strategic issue, with Deloitte suggesting that it will **“either differentiate mining companies or derail them”**.⁴

“... the Australian public are more accepting of the mining industry in Australia when industry and governments work together to build trust in the industry. Holding a social licence to operate continues, therefore, to be the responsibility of governments and industry working with communities and wider society to promote effective, constructive, and mutually beneficial relationships”

CSIRO, “Attitudes towards Mining in Australia”

As highlighted in the 2017 CSIRO Attitudes Towards Mining in Australia report, while mining is essential to everyday life in Australia, social acceptance of the industry is complex. Re-building trust in the industry will ultimately depend not only on the actions of individual companies, but the ability of all interested stakeholders including companies, governments, communities and society more generally to work together.



Image: Heart of Australia assisting regional communities

KEY INDICATORS

QRC PRODUCTION VOLUME INDEX

PEDAL TO THE METAL

The QRC's quarterly Production Volume Index tracks changes in the total production of Queensland's major commodity exports—alumina, aluminium, bauxite, coal, copper, gold, lead, LNG, silver and zinc.

The Production Volume Index is weighted by the value of each commodity. This means changes in

the volume of coking coal (which is over half of the total index value) has a proportionately larger impact on the quarterly index result than, for example, changes in thermal coal volumes (representing approximately 10–15 % of total value).

For the September 2018 quarter (the latest available data), the QRC's Production Volume Index increased to 124 points, three points above the June 2018 quarter and well above the 118 points achieved in same quarter of 2017. The index result can be interpreted as Queensland's resources production is now 24% higher than when the index began in 2006.

Queensland metals operations drove much of the increase in the Production Volume Index this quarter. Zinc production continued its rise, increasing by 36% compared to the previous quarter thanks to increased production at Lady Loretta and New Century zinc mines. Meanwhile steady increases in bauxite (7%), lead (6%) and silver (5%) production, all offset a minor decrease in coal (-2%) and gold (-4%) production for the quarter.

Looking ahead to the final quarter of 2018, the QRC's Production Volume Index can expect another strong result. According to recent data, Queensland LNG and coal exports both delivered export records in 2018. Queensland exported a record 20.6 million tonnes of LNG in 2018, up nearly 2% on the last year's 20.2 million tonnes. Queensland continues to enjoy the benefits of growing Chinese LNG demand, with 14.25 million tonnes or nearly 70% of Queensland LNG heading to China in 2018.⁵ Meanwhile, Queensland coal exporters surpassed their 2016 volume record by two million tonnes—exporting 223 million tonnes to 30 different countries or territories in 2018.⁶

EXPORT OUTLOOK

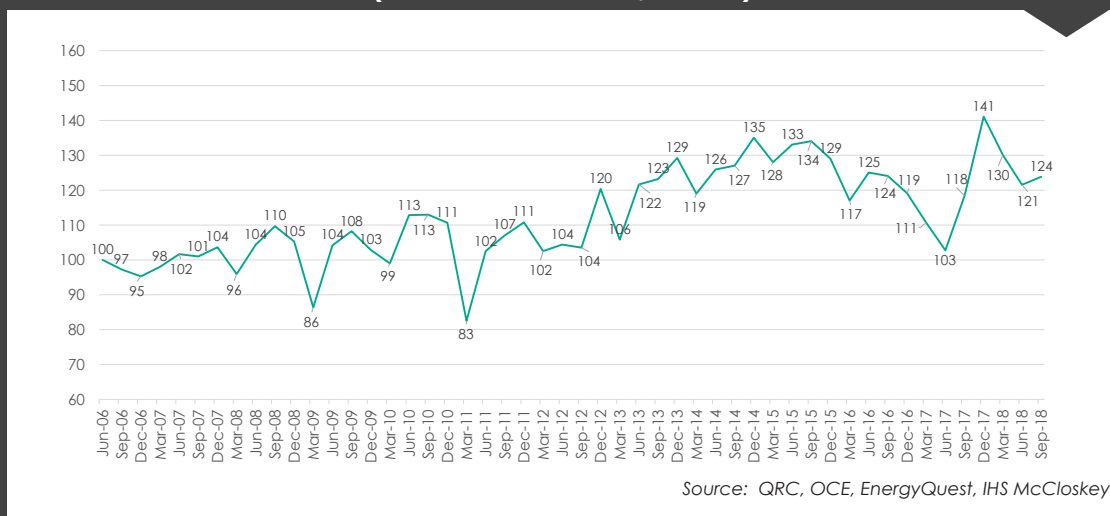
FEEDING ASIAN GROWTH

Queensland could expect more record volumes of coal and LNG in the year ahead, as demand for Queensland exports continues to grow.

Throughout 2019, Queensland metallurgical coal producers will continue to benefit from Asia's growing steel demand. According to the Office of the Chief Economist, India, Vietnam, Indonesia and Malaysia are all investing in additional steel capacity, with India forecast to become the largest metallurgical coal importer by 2020. In the year to November 2018 alone, India's metallurgical coal imports grew 19%.⁷

Growing energy demand across Asia will also support demand for our energy resources. IHS forecasts India's thermal coal demand to grow at a yearly average growth rate of around 3.5% from 777 million tonnes in FY 2018 to 1,180 million tonnes in FY 2030. That's nearly an extra Carmichael mine of demand growth each year.⁸

CHART 2: QRC PRODUCTION VOLUME INDEX (A\$) (QUARTERLY)
(INDEX BASE JUNE 05/06=100)



⁷Department of Industry, Innovation and Science, Office of the Chief Economist, [Resources and Energy Quarterly](#), December 2018

⁸IHS, India Coal Market Profile: December 2018

KEY INDICATORS CONTINUED

Queensland thermal coal producers should also continue to benefit from higher prices. The Office of the Chief Economist forecasts thermal coal prices to remain well above the lows of 2015 and 2016 as the lack of substantial investment in new thermal coal capacity will provide a floor for thermal coal prices.

Our major trading partners are also demanding more LNG. China's LNG demand has grown strongly thanks to its policies to reduce air pollution—making it the world's largest importer of LNG at more than 36 million tonnes. That's nearly twice the size of Queensland's record LNG exports in 2018. Meanwhile, the Office of the Chief Economist forecasts India's LNG to nearly double in three years, from 18 million tonnes in 2017 to 33 million tonnes in 2020.

Queensland can also look forward to stronger bauxite exports in 2019 as new projects ramp up production. In December 2018, Metro Mining's Bauxite Hills Mine announced its intentions to increase planned bauxite production over 2019 to 3.5 million tonnes, while Rio Tinto's Amrun project is also scheduled to hit full production in 2019. The ramp up of these projects will mean Australia's bauxite production is projected to grow at an annual average rate of 12 per cent, to 119 million tonnes in 2019–20.⁹



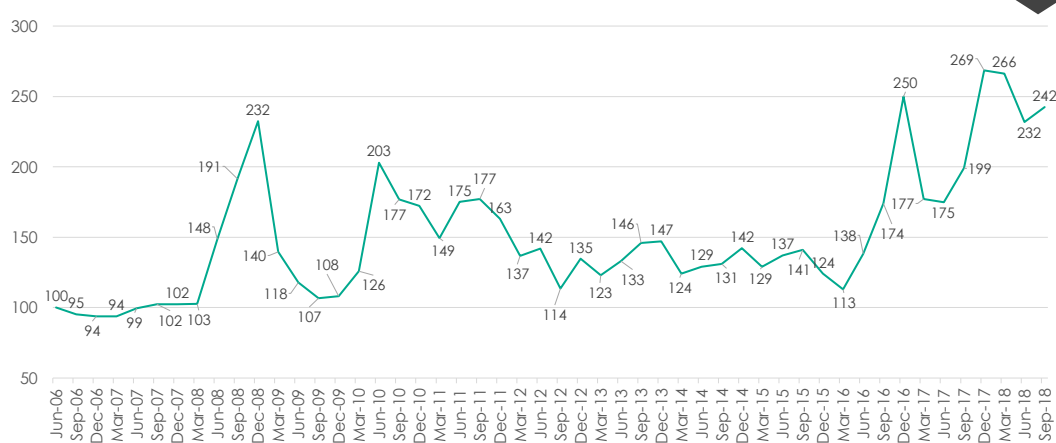
Metro Mining's Bauxite Hills mine

QRC VALUE OF PRODUCTION INDEX MODERATE GAINS FROM ENERGY RESOURCES

QRC's Value of Production Index reflects changes in the prices of the resources that Queensland produces. The weighted index reflects the same mix of commodities as the QRC production volume index, which includes LNG production from the

December 2016 quarter. Over the September 2018 quarter, the QRC's Value of Production Index increased from 232 points to 242 points — well below the December 2017 Index record, yet still 43 index points higher than the same quarter in 2017.

CHART 3: QRC VALUE OF PRODUCTION INDEX (QUARTERLY)
(INDEX BASE JUNE 05/06=100)



Source: QRC, OCE, IHS McCloskey

⁹Department of Industry, Innovation and Science, Office of the Chief Economist, Resources and Energy Quarterly, December 2018.
Metro Mining, 2018 Production Guidance Achieved

QRC STATE OF THE SECTOR

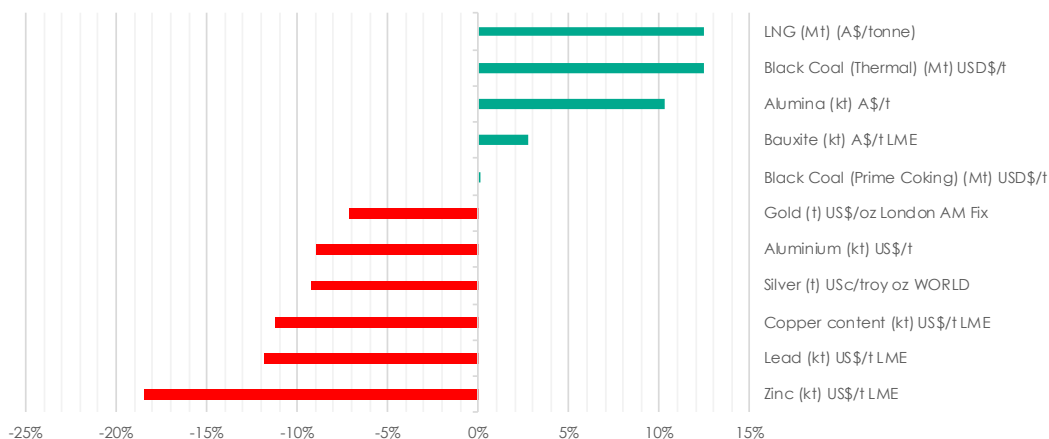
QRC VALUE OF PRODUCTION INDEX CONTINUED

Chart 4 provides a breakdown of this quarter's average price changes for each commodity. Only four commodities enjoyed spot price gains over the quarter. Queensland's energy commodities, LNG and thermal coal both lead the pack, each achieving 12% gains. Queensland's metals bore the brunt of the spot price falls with zinc and lead both experiencing strong falls (-18% and -12%).

Chart 5 shows both the volume and value of Queensland commodities bounced back in the September 2018 quarter from \$19.1 to nearly \$20 billion dollars.

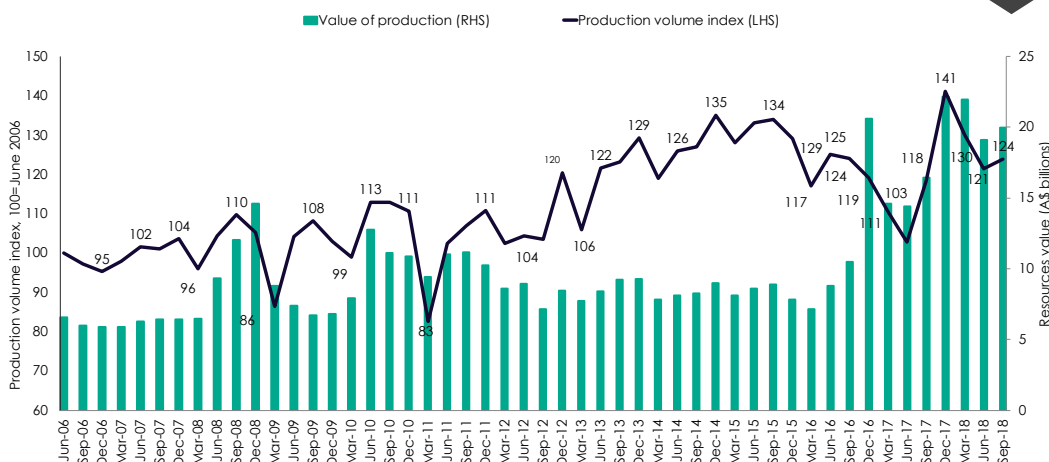
Chart 6 provides a breakdown of the value of Queensland's resource production in the quarter. LNG achieved its highest share of Queensland resource production value at 18%, thanks to strong prices and volumes. Meanwhile coal continues to account for the bulk of Queensland's resource production value at 65% in the quarter.

CHART 4: AVERAGE QUARTERLY COMMODITY PRICES CHANGES — SEPT QTR 2018



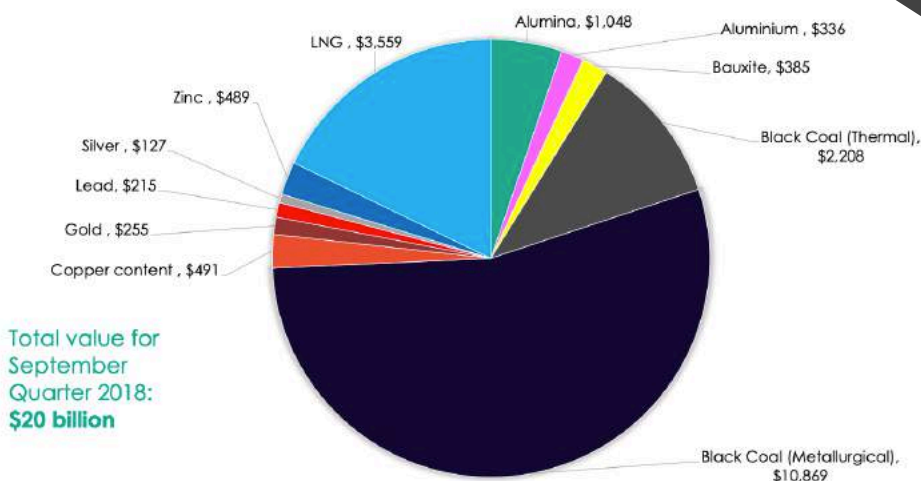
Source: OCE, IHS McCloskey

CHART 5: QUEENSLAND COMMODITY VOLUMES VERSUS VALUES



Source: OCE, GPC, IHS Markit

CHART 6: QUEENSLAND RESOURCE PRODUCTION VALUE IN SEPT QTR 2018



Source: QRC, OCE, EnergyQuest, IHS McCloskey

QRC CEO SENTIMENT INDEX

Each quarter, the QRC prepares its CEO Sentiment Index by surveying its producer and explorer member CEOs. The survey typically receives between 20-35 responses from mining and energy, minerals processing, contracting, exploration, electricity generation and oil and gas extraction members in Queensland.

Each survey asks CEOs to nominate the extent they expect a series of eleven factors will impact on the objectives of their organisation over the next 12 months. All responses are weighted to arrive at a single sentiment value for that factor. The weighting means the factors generating the greatest concern receive the lowest scores and are lower down on the negative axis.

For the December 2018 quarter, CEOs were once again the most negative towards *attracting or retaining skilled employees* — now in its third quarter as the top concern for CEOs. Yet the scarcity of skills should not come as a surprise given the substantial resources jobs growth in 2018. Over the year to November 2018, jobs in the mining industry grew in Queensland by 20% and 18% across Australia.¹⁰



Our organisation is building 4 operations in 18 months and the demand on human resources will be high. Finding skilled resources to fill the 400 positions will be a challenge."

"Attracting and retaining capable leaders and engineering candidates is a key issue"

"Finding skilled labour, particularly statutory qualified personnel in the underground industry, is a significant challenge"

"Our key concern is finding available people and equipment"

Alongside the challenges of industry growth, CEOs are watching global economic conditions closely, with the survey's *global macroeconomy* sentiment category now the second highest concern for CEOs. A rapid rise from the sentiment category's fifth position in the December 2017 quarter. CEOs comments typically pointed to specific threats of trade wars to the global economy:

Several CEOs referred to difficulties in attracting skilled employees to their organisations in the quarter:



Uncertainty around Trump policies and other international issues such as China have created instability in the markets."

"The sudden decision by the Chinese central government to impose import restrictions on Southern import terminals has a dreadful effect on the global coal market."

"China is increasingly playing games with artificial trade barriers"

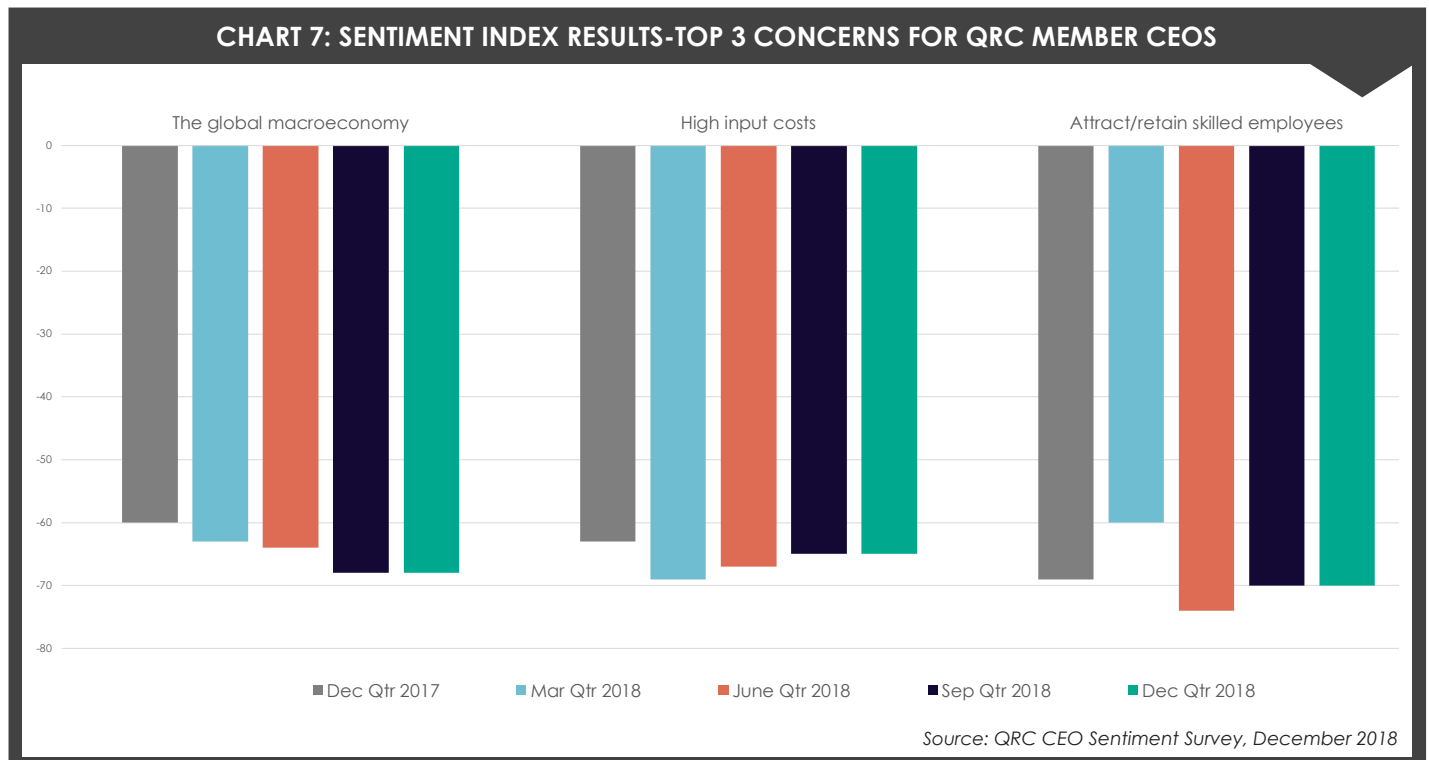
QRC STATE OF THE SECTOR

Echoing the concerns of QRC CEOs, the International Monetary Fund is wary of the impact of trade tensions on financial markets, with the two previously decoupled issues now intertwining. The IMF warned:

“An escalation of trade tensions and a worsening of financial conditions are key sources of risk to the outlook. Higher trade uncertainty will further dampen investment and disrupt global supply chains. A more serious tightening of financial conditions is particularly costly given the high levels of private and public sector debt in countries.”¹¹

Finally in more positive news, *Uncertain and/ or poor regulation*, typically the most troubling category for CEOs, has continued to recede, dropping 12 index points to sixth position and a level not seen since the December quarter 2015.

Chart 7 illustrates the change in sentiment over recent quarters for our member CEOs' top three concerns.





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