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'COMPELLING CASE FOR INFRASTRUCTURE INVESTMENT'

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The QRC has presented Treasurer Tim Nicholls with a compelling case for investment in productivity-enhancing infrastructure.

The submission on how funds from the Strong Choices Investment Program (SCIP) might be allocated for lasting value emphasises quality infrastructure to boost the financial viability of resources projects, and in turn, employment and revenue growth.

QRC has no objection to the long term leasing of some state assets in order to reduce state debt. Our caveat has always been that appropriate commercial and regulatory protections for users are essential.

We also support capital recycling to encourage new projects and enhance the productive capacity of the state's four economic pillars.

The international competitiveness of the resources sector has relied upon the availability of high quality economic infrastructure ahead of demand.

Ports, rail, roads, airports, dams and power fall into that category – and so does social infrastructure to attract workers, their families and support industries to regional communities.

These are essential to the competitive positioning of Queensland producers on global cost curves and incremental growth, noting that coal exports have grown from 125 million tonnes in 2002 to 209 million tonnes in 2013-14.

The result has been large economic returns for the state, with the resources sector's annual $38 billion spend in Queensland on wages and goods and services generating one in every four dollars of Queensland's Gross Regional Product.

For Queensland to take advantage of demand growth from Asia, industry and government must consider how to best provide infrastructure ahead of demand and at the lowest cost.

While there is no shortage of resources projects 'on the books' – at either the publicly announced, feasibility or committed stages – many are uneconomic because of industry's obligation to adopt almost all the risks and costs associated with them.

This contrasts with the thrust of the government's soon-to-be-launched ResourcesQ initiative – a 'thriving partnership' between industry and government. Arguably, that should extend to a reasonable sharing of costs and benefits from resources investment.

The way governments approach social and economic infrastructure is of such importance to the resources sector that it should figure in the design and administration of both the Strong Choices Investment Program and Royalties for the Regions (R4R).

R4R was a welcome initiative of the Newman government and has been a main source of infrastructure funding for regions adjusting to resources sector development with some $495 million earmarked over four years to 2015-16.

Meantime, more than $8 billion in royalties and approximately $160 billion in export earnings will have been delivered to Queensland by the resources sector over this period.

To date $306 million have been committed to 39 local governments over three funding rounds, but in the next, a further $200 million will be 'refocused' on strategic projects linked to the Queensland Plan and priorities from the RegionsQ initiative.

RegionsQ covers the state with the exception of metropolitan Brisbane, so QRC is naturally concerned about the dilution of R4R funding.

The fact the program is over-subscribed in coal regions over a period of benign growth suggests a backlog of projects.

R4R is an important and very welcome new program which should be given the time to operate according to design. Infrastructure funding programs whose guidelines are continually modified make it difficult for proponents to plan, budget and act strategically to ensure delivery ahead of demand. The upshot is calls on resources companies through other channels such as new rates charges that bear no relationship to the costs projects could impose on local councils.

The QRC's 2015 election policy agenda document urges both the state government and the opposition to commit to a continuation of the $200 million Royalties for the Regions program with a focus on resource communities.

QRC submission: Strong Choices Investment Program

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- Feature article: Fossil fuel fumbles
- QRC CEO Sentiment Index

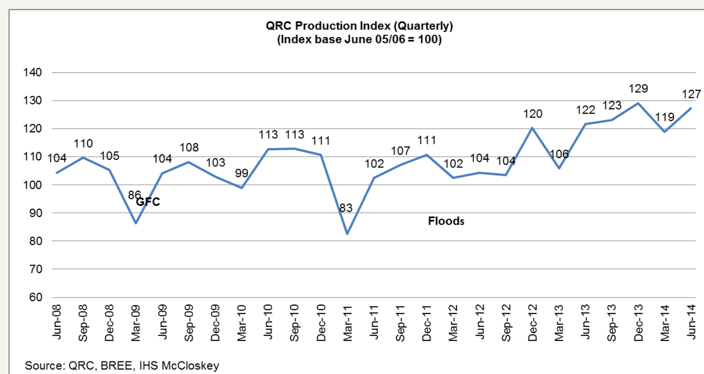
KEY INDICATORS

QRC PRODUCTION INDEX

The QRC production index is a composite weighted index that tracks percentage increases and decreases in the total production of Queensland bauxite, alumina, aluminium, coal, copper, gold, lead, silver, and zinc quarter to quarter.

Weightings are on a value of production basis; hence changes in coal production (representing 70% of the Queensland resource sector's total value of production) have a proportionately larger impact on the index than changes in silver production for example (representing just 5% of total value of production). Note – because Queensland is not yet selling export LNG this output has not been included.

The index at the end of the June 2014 quarter (latest available data in October 2014) reached 127 points. This is an increase of 8 percentage points from the March 2014 quarter and an overall increase in 5 percentage points over the 12 month period (June 13 - June 14) (June 2006=100).



The total volume of Queensland coal exported in the June quarter was up 12% from 48.6 million tonnes reported in the March quarter to 55.2 million tonnes including record monthly exports for June alone reaching 19.6 million tonnes. September quarter data tells us that production has maintained high volumes with total Queensland coal exports for 2014 (year to date ending September) reaching 158 million tonnes. We expect total exports for the calendar year to exceed 210 million tonnes based on the annualised figures for the first 9 months of 2014.

The majority of commodities including alumina (1,555 kt to 1,877 kt) aluminium (129kt to 136 kt), bauxite (6,116 kt to 6,363 kt), and zinc (233 kt to 237 kt), and) recorded higher production volumes over the June quarter. Gold (4 t) production remained constant and only copper (68 t to 36 t), lead (118 kt to 113 kt) and silver (387 t to 368 t) reduced production volumes.

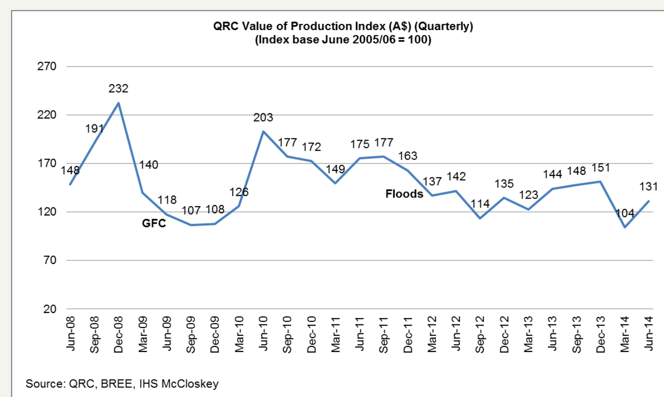
QRC VALUE OF PRODUCTION INDEX

Comprising the same basket of goods as the QRC production index, the QRC value of production index is also a weighted index. It combines domestic production and average global benchmark prices to track percentage increases and decreases in the Queensland resource sector's total value of production.

The index at the end of the June 2014 quarter (latest available data) reached 131 index points up from 124 in the previous quarter. In aggregate, the resources sector recorded sales of A$8.3 billion in the June quarter, up from A$7.7 billion in the March 2014 quarter.

This slight increase was primarily on account of the increase in alumina production (21 per cent) in conjunction with a 1.8 per cent increase in spot premium metallurgical coal prices over the quarter (US$113/t up to $115) paired with an increase in production. There was no change in the average thermal coal price (US $73). The slight depreciation of the $AUD against the $USD will have also contributed towards the increased index.

Aluminium (US$1,708/t to US$1,772/t) and zinc (US$2,031/t to US$2,058/t) recorded increases whilst alumina (USA314/t to $US306/t), copper (US$7,054/t to US$6,787/t), gold ($US1,293/oz to $US1,289/oz), lead (US$2,104/t to US$2,091/t) and silver (US$2,048/troy oz to US$1,961/troy oz) recorded decreases over the quarter.



PRICE OUTLOOK

There is considerable uncertainty in the coal market about the longer-term impact of the Chinese imposed import tax (effective 15 October 2014). According to IHS McCloskey, sources predict a period of a few weeks of reduced trade to China from Australia as both markets work out the impact. China last imposed tariffs on coal imports in 2007. The new rates will be 6% for thermal coal and 4% for coking coal used in steel making. Australian Government Ministers are expressing confidence that the free trade agreement negotiations with China will overcome the recent unwelcome coal tariff surprise.

The situation has also been complicated by the announcement of a separate ban on the import of lower ranked coals (high ash and sulphur) in a move designed to reduce air pollution. Queensland coal exports to China are primarily coking coal, used in the steel making rather than thermal coal used in power production. Also, Queensland exports of thermal coal tend to be in the high ranked (low ash and low sulphur coal) which are not subject to the ban.

FEATURE: FOSSIL FUEL FUMBLES

While there's rarely a shortage of commentators critical of fossil fuels, the biggest story in recent weeks has been confirmation of the gap between their perceptions and reality.

Take for example the Anglican Diocese of Perth's announcement that it would be selling its holdings in fossil fuel companies.

'I'm not a financial person, I'm not an accountant, I'm a bishop, and it is for the trustees themselves to determine if they will move from fossil fuel exposed industries and shares into renewables,' Bishop Tom Wilmott told the ABC.

'But just take, for example, the return on coal; over the last two years coal has gone from $125 a tonne to $65, and in the international market the smart money is moving into renewables as well.'

The Bishop was wise to issue a caveat about his expertise, but a higher quality explanation was expected from Canberra's Australian National University after its withdrawal of investments in resources companies Santos, Newcrest Mining,

Iluka Resources, Sandfire Resources, Oil Search, Independence Group and Sirius.

As reported by the ABC: 'The seven companies represent $16 million, or 1 per cent, of ANU's estimated $1 billion of investment holdings. They're all resources companies, but many aren't fossil fuel related.'

Acting on advice from an 'independent environmental adviser', a cement-maker and one of Asia's largest resources and energy investors escaped sanction, but the last word was delivered a few days later with the induction of Santos as a South Australian National Trust Corporate Icon.

Alan Oxley, from ITS Global told the ABC that most investors looked at the figures, and according to the International Energy Agency, coal use would continue, and even rise, until almost 2050.

'What's happening is a lot of financial institutions are feeling like they have to 'do the right thing' and they're making statements they won't do this and they won't do that, but really it has very little impact on their investment strategies,' he said.

During a visit to Brisbane to address to the Mining Resources Convention, the former Australian trade representative told the Australian Financial Review (AFR) that 'big investment funds might be breaching their fiduciary duties if they no longer invested in resources companies, because these delivered the best returns for shareholders.'

'In Australia, there is a law that requires fund managers to perform their fiduciary duties. And their fiduciary duty is an obligation to provide the best returns for investors,' Oxley told AFR's Mark Ludlow.

The AFR went on to record: 'Australian National University, Local Government Super and HESTA have announced divestments of some fossil fuel companies, and Sydney University is weighing a move.

'But the universities of NSW, Melbourne and Adelaide, as well as large super funds such as Cbus, have resisted the push.'

Oxley's assessment was reinforced by Manhattan Institute Senior Fellow and US energy commentator Robert Bryce.

In a report NOT BEYOND COAL: How the Global Thirst for Low-Cost Electricity Continues Driving Coal Demand, Bryce says that since 1973, coal consumption has grown faster than any other form of energy.

Furthermore, growth in coal consumption has been critical to electricity access in developing countries.

'Based on the results of three different estimates, between 1990 and 2010, about 830 million people—the vast majority in developing countries—gained access to electricity due to coal-fired generation,' Bryce says in opening his report.

'Indeed, roughly twice as many people gained access to electricity due to coal as due to natural gas; and for every person who obtained access to electricity over that period from non-hydro renewable sources, such as wind and solar, about 13 gained access due to coal.

Why is that important?

QRC Chief Executive Michael Roche sought to explain it to Sydney Morning Herald (SMH) readers in an as yet unpublished response to an article called 'Why Abbott's faith in coal could be wrong - very wrong'.

Here's an excerpt of what the SMH won't let their readers hear:

The International Energy Agency and the United Nations tell us around 1.3 billion people have no access to electricity and 2.7 billion people rely on biomass and dung for cooking on open fires.

The World Health Organisation (WHO) estimates that more than 1.45 million people die prematurely every year from household air pollution due to inefficient biomass combustion.

WHO says that by 2030 indoor pollution will kill more people than malaria, HIV/AIDS and tuberculosis combined.

There are multiple technologies that could start to address this problem, just as the developed world did last century with centralised coal-fired power generation and distribution.

In developing Asia, coal is the future for two key reasons – availability and economics.

While the thermal coal market is currently oversupplied, Asian import demand is forecast by market analysts at HDR to more than double by 2030, growing at around 46 million tonnes a year, every year.

That's the outlook for thermal coal – not the metallurgical coal being produced by the Caval Ridge and Goonyella-Riverside Mines that both featured in your (SMH) report.

Metallurgical or coking coal is an essential component for 70 percent of the world's steel production.

The Bureau of Resource and Energy Economics forecasts this component of Australia's coal export inventory will be worth around $31 billion by 2018-19.

Robert Bryce again: 'Coal-fired-generation capacity continues to grow in wealthy countries, too. For electricity production, no other energy source can currently match the black fuel when it comes to cost, scale, and reliability. In all, more than 500 gigawatts of new coal-fired capacity will likely be built worldwide by 2040. Given coal's pivotal role in providing electricity to poor and wealthy countries alike, it is highly unlikely that global carbon-dioxide emissions will fall anytime soon.'

The future of fossil fuels is certain to come under international scrutiny during the G20 in Brisbane, but perhaps the most informed commentary will be found at Brisbane City Hall on 12 November.

Brisbane's Global Café series in association with the G20 includes a session called Powering Future Economies, sponsored by QRC member Peabody Energy.

Speakers include Glenn Kellow, Chief Operating Officer at Peabody Energy; Matt Rogers, Director, McKinsey & Company; David Knox, CEO, Santos; Dr Bjorn Lomborg, Copenhagen Consensus Centre; John Connor, CEO, The Climate Change Institute and Dr Alex Wonhas, Executive Director, Energy and Resources, CSIRO.

Links for further reading:

Australian National University dumps mining stocks as global 'divestment campaign' focused on universities starts to gain traction in Australia

Santos recognised as a National Trust Heritage icon

Alan Oxley's divestment presentation, Brisbane Mining Resources Convention 2014

Not Beyond Coal: How the Global Thirst for Low-Cost Electricity Continues Driving Coal Demand

Brisbane G20 Global Café Series: Powering Future Economies, 12 November 2014

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QRC CEO SENTIMENT INDEX

The QRC CEO Sentiment Index is a survey of the QRC's 78 full member company chief executives.

These companies cover the majority of mining, minerals processing, contracting, exploration, electricity generation and oil and gas extraction activity in Queensland.

The following charts focus on the change in sentiment beginning September quarter 2011. Chart 1 demonstrates the high ongoing concern for the global operating environment. This uncertainty is particularly centred on the ability of China to sustain growth levels and the difficulty in raising capital given low commodity prices and high input costs.

Chart 2 reveals the increasing concern for industrial relations (IR) and social licence to operate, particularly over the last twelve months. This deterioration in sentiment is largely attributed to inflexible IR systems and the need to address concerns about labour productivity and structural wage cost issues. The sentiment towards attract/retain employees has significantly improved over the period.

Chart 1: Macroeconomic concerns

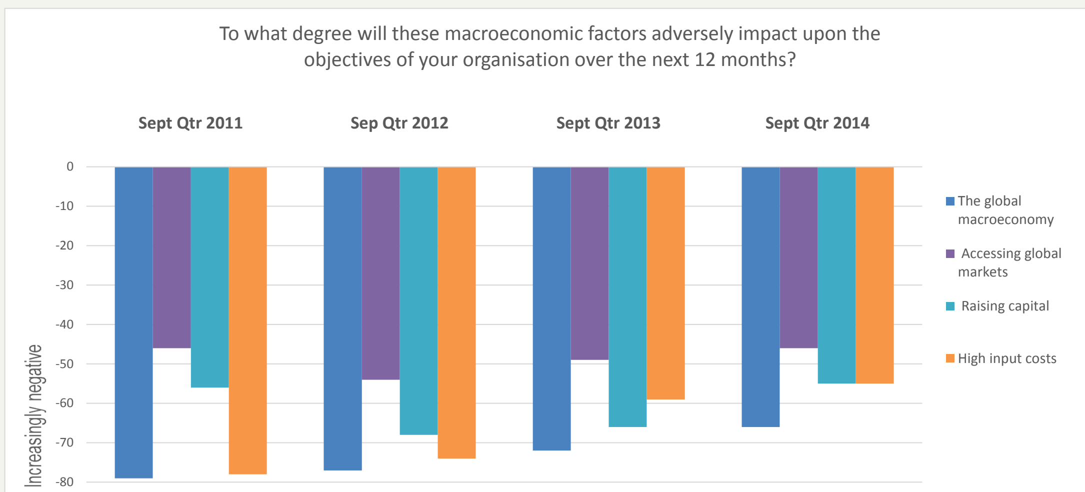
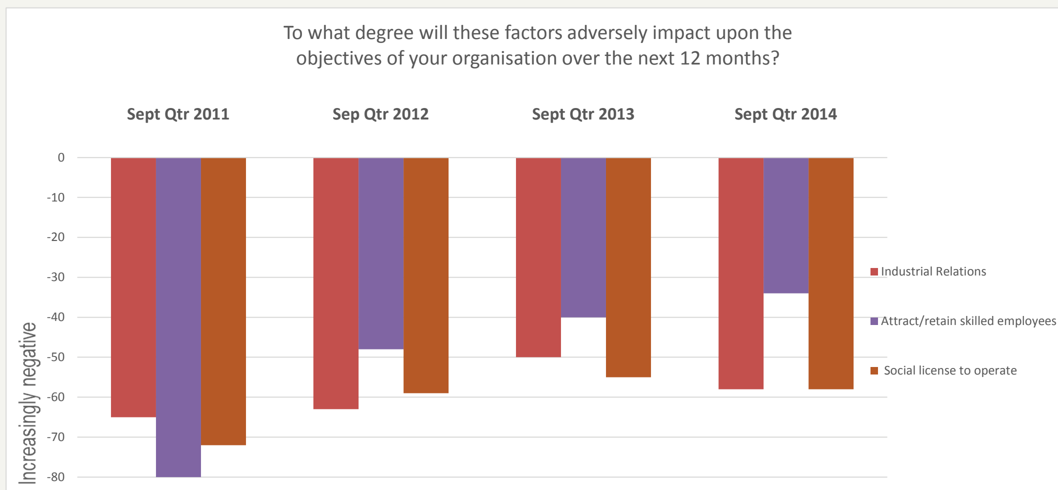


Chart 2: Industrial relations and social licence concerns



Written and prepared by the Queensland Resources Council, which is the peak representative body for 266 companies with interests in the state's minerals and energy sector. The data and information for this publication comes from a number of public sources – notably members directly, mccloskeycoal.com, the Bureau of Resources and Energy Economics and the Australian Bureau of Statistics. For more information, contact the Queensland Resources Council on (07) 3295 9560 or www.qrc.org.au.

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