

QRC STATE OF THE SECTOR

SEPTEMBER QUARTER 2015

IN THIS EDITION:

Key indicators: QRC Production Index, QRC Value of Production Index and Market Outlook

Feature: Time to recognise approvals system needs urgent reform

QRC CEO **Sentiment** Index

QUEENSLAND'S RESOURCES DELIVERING FOR ALL CITIZENS



By Michael Roche, Chief Executive Queensland Resources Council

QRC's latest economic contribution report confirmed that our resources sector again delivered massive statewide economic and employment benefits to Queensland: one in five dollars in the economy, one in every six jobs,

supporting more than 24,000 businesses and delivering \$2.1 billion in royalties to fund schools, hospitals and roads. All of those benefits are delivered while mining and gas operations used just one tenth of one per cent (i.e. 0.1%) of the state's land mass.

On the Darling Downs, coal and gas operations support over 15,000 or 13 percent of all jobs in the region and do so while using just 0.3 percent of that region's land.

These are facts worth bearing in mind in considering the merits of some extreme positions put forward by anti-coal and anti-gas activists. You will never hear from those green activists an acknowledgement that Queensland's extraordinary natural endowment of mineral and petroleum wealth belongs to all Queenslanders. This fact was well understood when the Australian constitution was drafted.

Queensland's longstanding land access laws strike a fair balance, between providing the community the benefits from development of the state's resource wealth, and respecting the rights of farmers to keep running their businesses.

No one is saying that resource companies should have the right to place mines and gas wells anywhere. Farmers should have the right to determine who can come onto their land and when. That is exactly what Queensland's land access laws do.

Those laws require resource companies to understand a farmer's business and how they might affect that business before they enter the land. The law makes it the resource company's responsibility to arrange compensation for any impacts on the farmer's business and both parties must agree to this contract before any impacts occur.

In Queensland more than 5,000 conduct and compensation agreements have been struck between resource companies and landholders under the Land Access Framework that has been operating successfully since 2010. Queensland's Land Access laws draw no distinction between freehold and leasehold farming land - both owners and leasehold farmers are recognised and compensated.

Under those agreements farmers have benefited to the tune of hundreds of millions of dollars in compensation. Once compensation is given to the farming business, the resources can be produced, which generates revenue to fund essential federal and state government services that benefit all Queenslanders every day.

Some politicians appear to have opted for the easy populist position by suggesting that it is appropriate for individuals to be able to block the extraction of certain resources. They should know better because they are in effect arguing against the property rights enshrined in our constitution, rights that confirm the resources belong to each and every one of us.

Those politicians have an obligation to calmly explain the difference between the crude right of veto and the more useful right to have a say in how and when land may be accessed. Negotiation around what is possible on the farm protects both the public interest and that of the landholder. Negotiation isn't easy, but it is in the best interest of all Queensland citizens. The resource company will also pay for the farmer to get the best advice in these negotiations, so the farmer is not out of pocket.

There are many hundreds of success stories across regional Queensland of farmers integrating resource infrastructure to the benefit of their family and their farms. The current access laws provide landholders the opportunity to negotiate terms that can ensure farms operate as they currently do, or to invest in improving their business.

It's time that all politicians had the courage to explain these facts to the public. To their credit, Federal Resources and Energy Shadow Minister Gary Gray and Queensland Natural Resources and Mines Minister Anthony Lynham have done just that.

Explaining these facts against the background of an emotion-charged set of circumstances will most likely draw a strong rebuke from Sydney shock jocks, from activist groups like Lock the Gate and of course from the Greens. I should know, having been personally villified by them in recent days.

The last thing these industry opponents want to discuss is the huge set of benefits being delivered to Queenslanders as a whole and to many, many individual landholders under the existing land access laws in our State.

To turn those land access laws on their head would be a sure recipe for driving resource investment from our state and from our nation.



TIME TO RECOGNISE APPROVALS SYSTEM NEEDS URGENT REFORM

There will be another upturn in minerals and energy demand globally, but the big question is whether Queensland is positioned to take hold of it.

The reality is that we desperately need a fit for purpose state and Federal approvals system to enable us to take advantage of the growing markets for our coal and gas in India and South East Asia as well as continuing strong demand in traditional markets like Japan and Korea.

The legal hurdles now confronting resource projects seeking to finalise their regulatory approvals would have been unimaginable just a few years ago.

Just consider the history of GVK Hancock's \$10 billion Alpha coal project in the Galilee Basin.

Seven years after the Queensland Government declared Alpha a 'significant project' in September 2008, multiple legal appeals by activist groups based in inner-city Brisbane continue to hold up this important job-generating project.

By August 2012, the project had approval from the Queensland Coordinator-General and the Federal Environment Minister.

The Environmental Defenders' Office (EDO) then lodged objections in the Queensland Land Court against the Alpha project in February 2013 on behalf of green activist group Coast and Country, which is simply a front organisation for other green activist groups.

The Land Court made its recommendation on objections to Alpha some fourteen months later in April 2014.

With a Land Court decision in hand, normally ministers would then be able to issue an environmental authority and a mining lease, but the game has well and truly changed.

In August 2014, Coast and Country lodged an appeal in the Supreme Court against parts of the Land Court decision. Those appeals were dismissed by the Supreme Court more than a year later, in September 2015, and awarded costs against Coast and Country, a group with 99 cents in the bank.

So was that the end of the activists' blocking tactics? Of course not.

The EDO, on behalf of Coast and Country, has now appealed to the Queensland Court of Appeal. That case will not even be heard until 2016. So, more than three and a half years since the federal environment minister handed down his approval for the Alpha project, GVK will not be building a mine and shipping coal. No, they will be in yet another court room.

And what if the activists don't like the Court of Appeal decision? Well they can seek leave to have the matter heard by the High Court.

At the forefront of the legal assault by EDO and Coast and Country is an argument against the Alpha project on the basis of climate change impacts, in particular the so-called Scope 3 carbon emissions.

Scope 3 carbon emissions occur during burning of exported coal in another country. This is like arguing that Saudi Arabia should take responsibility for the vehicle emissions in Australia because we import most of our liquid fuel.

The Land Court and Supreme Court have in a number of cases since 2011 rejected the Scope 3 emissions argument. In its 2014 Alpha Mine decision the Land Court found that "the clear and unambiguous facts showed that there would be no reduction of greenhouse gas emissions if the Alpha Mine was refused and because, depending on the source of replacement coal, such replacement coal may well on the evidence result in an increase in such emissions". This position was upheld by the Queensland Supreme Court in 2015. In spite of these unequivocal court findings, the activists can apparently still lodge further appeals and delay projects through the due process of the courts.

Can anything be done about these blocking tactics? We would argue that, at a minimum, the law should be amended to prevent objections on matters such as Scope 3 emissions, which have previously been decided by the courts.

This phoney Scope 3 emissions argument has again been invoked by the Australian Conservation Foundation (ACF) in its challenge to Federal Minister Greg Hunt's second Adani Mine approval.

It is noteworthy that the anti-coal movement has dropped the pretence of hiding behind local conservation groups and have brought out the big guns from latte-sipping central in Melbourne and Sydney.

And this should come as no surprise. This use of litigation is at the heart of the 'disrupt and delay' strategy outlined in the anti-coal movement's *Stopping the Australian Coal Export Boom*.

Governments really do need to rethink these approval processes and opportunities for legal delay. This rampant behaviour by activists groups in the case of the Alpha and Carmichael projects may well be the new normal for resource projects.

If investors believe that governments are not prepared to step in and halt this legal merry-go-round, then we can kiss goodbye any major new projects to take advantage of the market upturn.

Right now the biggest fear must be that governments do not have the resolve to, in any way, curtail the opportunities our laws give to motivated and well-funded activists to disrupt and delay large job-generating resource projects.

KEY INDICATORS

QRC PRODUCTION INDEX

QRC's quarterly production index tracks changes in the total production of Queensland's traditional resource¹ exports – alumina, aluminium, bauxite, coal, copper, gold, lead, silver and zinc.

The index is weighted by the value of production. This means changes in the volume of coking coal produced (more than 50% of the value of Queensland resources production) has a proportionately larger impact on the index than, for example, changes in thermal coal production (representing approximately 10-15% of total value).

Total production volume increases

The index at the end of the June 2015 quarter (latest available data) rose to 133 points up from 128 points last quarter. This compares to an index of 126 during the June quarter last year. The index base is June 2006 = 100, so the total volume of production has grown one third or 33% since that time.

Coal exports in the June quarter were 55 million tonnes, an increase of 3 million tonnes on the previous quarter. Total coal exports for the 2014-15 financial year were a record 219 million tonnes.

Despite low prices by historical levels, most commodities recorded increased production volumes over the June quarter including alumina (1,607 kt to 1,627 kt), aluminium (142 kt to 145 kt), bauxite (6,704 kt to 6,941 kt), lead (107 kt to 110 kt) and zinc (253 kt to 274 kt). Gold production (4 t) remained constant and only copper (79 kt to 76 kt) and silver (246 t to 142 t) recorded a decrease in production volumes.

Weighing up the net result of these changes in production volumes, weighted by value generates the 5 point increase in the QRC Production Index over the last quarter.

QRC VALUE OF PRODUCTION INDEX

QRC's value of production index reflects changes in the quantities produced by Queensland's resources at average global benchmark prices. The weighted index reflects the same mix of commodities as the QRC production index. Once again, LNG exports are not yet included in the index.

Total value drops

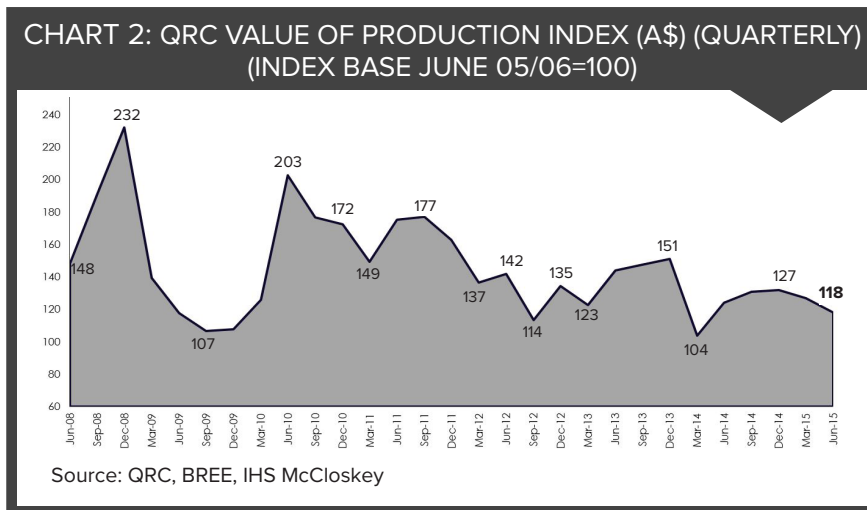
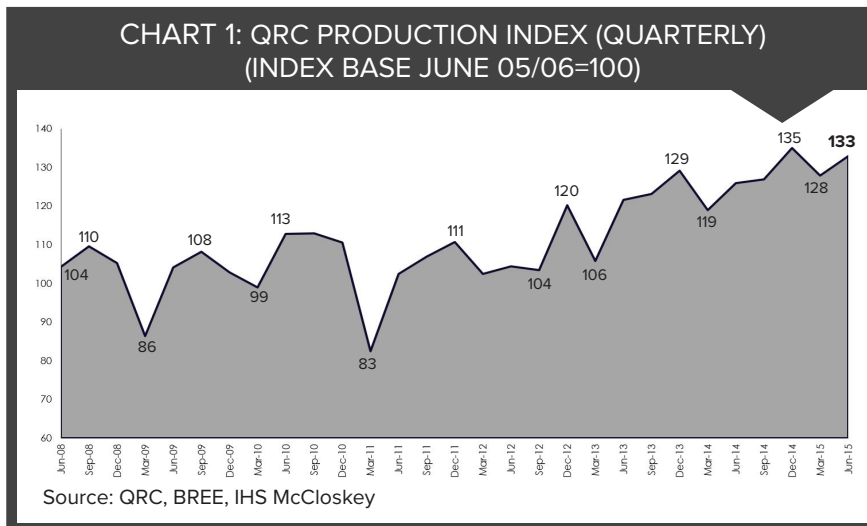
The persistent oversupply for many commodities and slowing consumption growth have meant most mineral and energy commodity prices declined in the past year. The index at the end of the June 2015 quarter (latest available data) fell to 118 points, down from 127 in the previous quarter. In aggregate, the resources sector produced goods valued at \$AU7.42 billion in the June quarter, down from \$AU7.96 billion in the previous quarter.

The June quarter decrease was a result of further declines for all commodities excluding copper (\$US5,818/t to \$US6,043/t), lead (\$US1,806/t to \$US1,973/t) and zinc (\$US2,080/t to \$US2,194/t) which all recorded price increases. The largest price decreases were for both thermal (\$US63 down to \$US58) and metallurgical coal (\$US111 down to \$US92).

MARKET OUTLOOK

The following outlook information is largely drawn from the September edition of the Resources and Energy Quarterly, produced by the Office of the Chief Economist, Department of Industry, Innovation and Science.

Overall the greatest price relief for Australian commodities has been in the depreciation of the Australian dollar against the US dollar over the past year. The Office of the Chief Economist forecast the AUD-USD exchange rate to average 0.74 US in 2015-16 with a strong risk that the AUD could depreciate further. Over the medium term, the Office forecast the AUD to return to its long term average of around 0.75 USD by 2019-2020.



¹ Please note, due to limited data availability, we are yet to integrate LNG prices and volumes into the index.



QRC STATE OF THE SECTOR

Metallurgical coal

Metallurgical spot prices declined substantially in the first eight months of 2015 and the market is forecast to remain well supplied until demand growth recovers and announced production cuts materialise. For 2015 as a whole, the Office of the Chief Economist expects contract prices to average around US\$102/t, or 19 per cent lower than 2014, while 2016 prices are forecast to average US\$97/t. Despite these price pressures, Australia managed to increase its share of world metallurgical coal exports from 52 per cent in 2013 to 56 per cent in 2014 as higher cost production vacated North America.

Thermal coal

Thermal coal will remain an important source of energy for the medium term, evident through the large volume of new coal-fired capacity under construction or approved, particularly in non-OECD countries. New investments in coal fired generation in these countries is expected to focus on high efficiency, low emissions (HELE) technology. As these generators require low emission coal, this change will present an advantage for Queensland's thermal coal producers.

Eastern Australian gas prices

Domestic gas prices across the Eastern seaboard have risen over the last quarter with considerable volatility since late 2014. The key driver for this volatility has been the varying degrees of uncontracted gas available to the market during this time. Eastern Australia gas production is projected to increase from 38.6 billion cubic metres in 2015–16 to 53.5 billion cubic metres in 2019–20. Almost all of the production increase will be from CSG fields in the Bowen-Surat basins in Queensland associated with the three LNG projects in Gladstone.

Metals

The September edition of the Resources and Energy Quarterly notes that over the short term, slowing global consumption growth is expected to continue to place downward pressure on prices for most commodities. However, over the medium term, relatively slow supply growth is expected to contribute and place upward pressure on prices.

QRC CEO SENTIMENT INDEX

The QRC CEO Sentiment Index is conducted quarterly across producer members with the typical response ranging between 20-35 responses. The participating companies cover the majority of mining, minerals processing, contracting, exploration, electricity generation and oil and gas extraction activity in Queensland. In addition to the standard sentiment questions, we also took the opportunity to ask members two additional questions regarding future production and price forecasts. Aggregated responses to these questions are shown in Chart 4.

The following chart focuses on the change in sentiment towards five key issues over the last twelve months (Chart 3).

More than one third of respondents anticipate production volumes will remain much the same over the next 12 months. In a largely over supplied market for most commodities it is interesting that only 16% of respondents expect to decrease production while close to two thirds of respondents anticipate prices will remain much the same over the next 12 months. Encouragingly of the 9% of respondents that anticipate further price reductions, there were no respondents that forecast prices to fall by more than 10% over the next 12 months.

CHART 3: CEO SENTIMENT RESULTS (TOP 5 WITH STRONGLY NEGATIVE SENTIMENT)

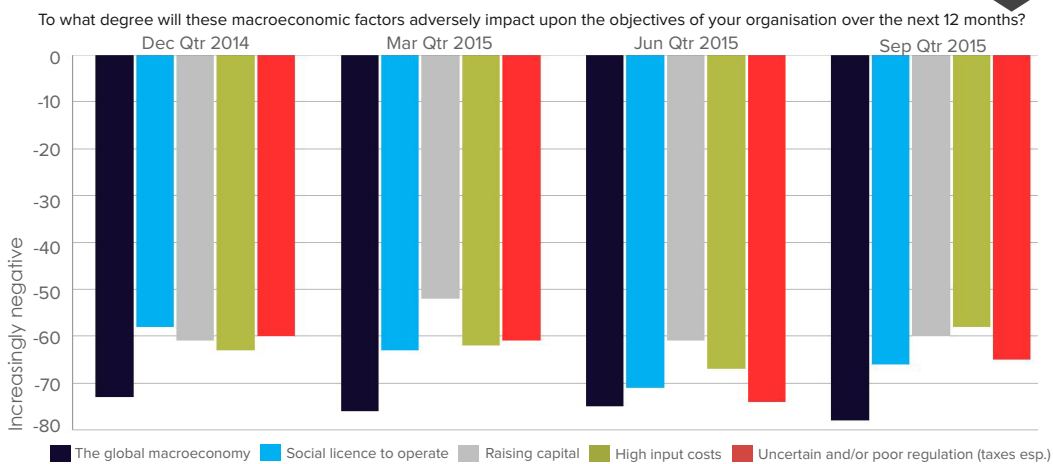


CHART 4: FORECAST PRODUCTION AND PRICE

