Welcome to the second edition of QRC’s State of the Sector Report. Importantly, it's also our first edition with the QRC’s unique CEO Sentiment Index included.

Representing the views of the QRC’s full-member company CEOs, the index tells us the extent to which a number of core issues are likely to impact upon the economic, environmental and social objectives of the Queensland resources sector over the next 12 months.

It is perhaps no surprise that the number-one issue keeping the sector’s CEOs awake at night is the global macroeconomic environment.

The sharp deterioration in global economic conditions has had a significant impact on resource demand and prices. The pace and severity of the deterioration has been significant and the short-term outlook, regretfully, remains uncertain.

There are however some indications that the economic downturn might be beginning to stabilise. For example, renewed enthusiasm in some coal markets was experienced in June, and prices for some base and precious metals rebounded slightly.

Despite this, global economic activity is expected to continue to be weak during 2009 and possibly into 2010.

Against the backdrop of higher costs and intensifying global competition, the priority for resource companies will be to weather this storm, and in doing so, continue to look for efficiencies in their operations and new market opportunities.

The number-two issue for CEOs at the moment is the proposed Carbon Pollution Reduction Scheme (CPRS). The Queensland coal and black coal electricity generation sectors will be particularly disadvantaged by this scheme.

Under the current proposal, the Australian coal industry will pay approximately $15 billion in carbon costs over the next 10 years.

However, and despite being eligible for approximately $9 billion in free permits as transitional assistance, the Australian Government will instead return the industry a mere $750 million over the first five years under the proposed Climate Change Action Fund.

This multi-billion dollar carbon liability will have a significant impact on the Australian coal industry.

Modelling demonstrates that premature shutdowns and cut backs in production are likely, and new investment will be discouraged. More information on this issue is outlined in our feature piece—The Carbon Pollution Reduction Scheme—Impacts on the Queensland coal industry.

Queensland’s black coal electricity generators will also be severely disadvantaged. Under the CPRS, the current formula for the Electricity Sector Adjustment Scheme (ESAS) will provide the black coal generation fleet with a disproportionately low level of compensation.

Despite estimates that the CPRS will impose a $3 billion direct asset loss on the Queensland fleet over its remaining life, the ESAS will allow for only $100 million in assistance out of a total $3.5 billion. This compares with $2.45 billion of assistance likely to be provided to Victoria’s brown coal generators, which are considerably more carbon emissions-intensive than Queensland’s black coal generators.

The QRC believes this sends a perverse message about the environmental outcomes the CPRS is designed to achieve.

In short, very high domestic carbon costs, coupled with expectations of strong future global demand for resources will lead to Queensland jobs being lost offshore, most likely to countries with poorer environmental controls than ours.

With the CPRS legislation yet to be passed, the QRC continues to work hard with our national colleagues to bring about changes. Furthermore, we encourage communities and the hard workers of this sector to voice their concerns to their parliamentarians.

IN THIS EDITION:

- Key indicators: QRC Production and Price Indexes
- Feature: The Carbon Pollution Reduction Scheme—impacts on the Queensland coal industry
- Industry sentiment: The QRC CEO Sentiment Index
State of the Sector

Queensland Coal Industry—Impacts on the Sector

Feature: The Carbon Pollution Reduction Scheme: Macquarie University, Australia

Queensland coal industry will incur approximately $15 billion in carbon costs. This is recognition that high carbon costs will damage those industries that are ‘trade exposed’, are ‘price takers’ in global markets and can’t pass costs on and, who compete against countries with no such carbon costs.

To this end, carbon liabilities should not be so high that incentives to abate will be compromised. Further, the timing of carbon liabilities needs to be aligned with the availability of technological options.

No technology exists to retrofit coal mining operations and currently, the only likely means to take significant periods of carbon cost reductions are by substituting coal with cleaner fuels. This is an unlikely solution to address the impact carbon price pressures. The National Greenhouse and Energy Rating System (NGER) and the Energy Rating Scheme have yet to demonstrate viability that these measures can deliver carbon leakage (where the cost of carbon permits is smaller than the potential global savings).

To put this into context, a small Queensland coal mine, producing 2 million tonnes of coal per year, emitted 300,000 tonnes of CO2e per year in 2008. Emissions are mainly in the form of fugitives (i.e., methane from the coal seam), diesel and air methane.

Four separately commissioned economic reports demonstrate that the CPRs as proposed will contribute to shutdown prematurely or scale back production. In addition, this is because the availability of a global emissions price is below the level that would be expected at 1.3 per cent per annum. Further, there will be no carbon leakage.

By 2020 and 2030, when compared to business as usual, the Queensland coal industry will incur approximately $15 billion in carbon costs. This is recognition that high carbon costs will damage those industries that are ‘trade exposed’, are ‘price takers’ in global markets and can’t pass costs on and who compete against countries with no such carbon costs.
The QRc Production index is a weighted index that tracks percentage increases and decreases in the total production of Queensland bauxite, alumina, aluminium, coal (all saleable), copper, gold, lead, silver, zinc, oil, gas, and electricity (NEM) quarter to quarter.

The QRc Production index at the end of the March 2009 quarter (latest available data) reached 99 index points (June 2005/06 = 100). Compared to the December 2008 quarter, this represents a 14 percent decrease in output of Queensland’s main resources. In dollar terms, this represents a $5.2 billion decrease in the value of production.

Approximately $4 billion of this decrease was on account of lower coal sales, predominantly metallurgical coal.

The demand outlook for resources looks uncertain but generally positive. For example, in the period April–June 2009, companies reported stronger coal sales to a number of markets, notably China, Brazil and Europe.

The QRc Price index, comprising the same basket of goods as the QRc Production index, reached 119 index points (June 2005/06 = 100). Compared to the March 2009 quarter, this represents a 47 percent decrease in prices across Queensland’s main resources. This comprises a significant decrease in coal prices; slight increases in spot prices for aluminium, copper, lead, and zinc; and slight decreases for gold, alumina, and silver.
The employment effects in the Australian minerals industry from the proposed carbon pollution reduction scheme in Australia commissioned for the Australian minerals industry by Concept Economics (May 2009)

• Reports 1 and 2 commissioned for the Council for the Australian Federation Secretariat (the State and Territory Governments) by Access Economics (May 2009)

• Economic assessment of CPRS’ treatment of coal mining commissioned for the Australian coal industry by ACIL Tasman (May 2009)

• CPRS Impacts on EITE Mining/Processing Activities commissioned for the QRC by ACIL Tasman (November 2008)

These reports can be accessed at http://www.qrc.org.au and go to publications.

**QRC CEO SENTIMENT INDEX**

The QRC CEO Sentiment Index is a survey of the QRC’s 79 full-member company chief executives.

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

CEOs on 10 June 2009 were asked: Answering ‘not at all’, ‘less than normal’, ‘same’, ‘more than normal’, or ‘very strongly’, to what degree will the following adversely impact upon the economic, environmental, and social objectives of your organisation over the next 12 months?

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<tr>
<th>The macroeconomic environment</th>
<th>High input costs</th>
<th>Difficulty in raising capital</th>
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<td>Difficulty in accessing global markets</td>
<td>Difficulty in attracting and retaining skilled employees</td>
<td>Social licence to operate pressures</td>
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<td>Domestic climate change policies</td>
<td>Domestic workplace relations policies</td>
<td>Hard infrastructure availability</td>
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<td>Soft infrastructure availability</td>
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The responses are collated and weighted with each issue receiving a unique index scoring. A score between 0-20 indicates ‘not at all’, 20-40 ‘less than normal’, 40-60 ‘same’, 60-80 ‘more than normal’, and 80-100 ‘very strongly’.

**Summary of key findings June Quarter 2009**

In priority order, issues that will ‘very strongly’ and ‘more than normal’ impact on the Queensland resources sector over the next 12 months are:

1. **The global economic environment** (uncertainty in relation to when global recovery will occur and future demand and price levels) [score 75]

2. **Domestic climate change policies** (concerns in relation to the very high costs coupled with few abatement options and negligible transitional assistance) [score 68]

3. **Uncertain and/or poor regulation** (concerns in relation to land access, namely future policies regarding the mining of more closely settled lands and compensation of landholders when exploration occurs; sovereign risk associated with royalty changes; Native Title processes; review of the Queensland Mining Safety and Health Act; increasingly anomalous position in relation to the continued prohibition on uranium mining; and increasing environmental regulations) [score 64]

4. **Domestic workplace relations policies** (uncertainty in relation to future third-party influence; increased costs emanating from the award modernisation process and the new unfair dismissal laws; and ensuring adequate flexibility in agreement making) [score 63]

5. **Difficulty in raising capital** (high-risk premiums and greater prudential controls by lenders; and capital remains expensive and scarce) [score 62]

6. **Hard infrastructure availability** (concerns re access and performance following the proposed privatisation of Queensland’s export related assets; and inherent inefficiencies in export transport chains due to competing interests) [score 60]

7. **High input costs** (concerns in relation to the cumulative impact of greater regulatory impose) [score 60]

**QRC PROFILE**

The Queensland Resources Council is the peak representative body for almost 160 companies with interests in the state’s minerals and energy sector. The QRC’s 79 full-member companies comprise explorers, miners, contractors, mineral processors, oil and gas producers and electricity generators. QRC service companies cover the gamut of professional services provided to the resources sector in the four corners of Queensland.