Mining Sector Delivers Spectacular Results for 2005

By ***PricewaterhouseCoopers***

The mining sector has delivered another spectacular increase in profits during 2005, on the back of a further strengthening in commodity prices. This is one of the key trends highlighted in 'mine let the good times roll', the third annual review of the global mining industry by PricewaterhouseCoopers. Russia is considered to be a great investment field for those looking for world class mines and ready to overcome certain challenges.

The 40 mining companies included in the analysis, which represent over 80% of the total global industry by market capitalisation, reported a 59% increase in aggregate net profits for 2005, up from $28bn to $45bn. This compares to aggregate profits of just $5bn in 2002. These results have prompted the companies to increase the amount returned to shareholders to $16bn in 2005 with further distributions and buy-backs announced in the early part of 2006. Two Russian companies – MMC Norilsk Nickel and Alrosa were covered by the analysis.

The report shows that investor confidence in the mining industry and its prospects have continued to strengthen: over the last two years mining stocks have outperformed both the S&P 500 and the Dow Jones Industrial Average by over 300%, and in 2005 alone the industry's market capitalisation increased by 72% to $791bn.

John Gross, Russia and CEE Mining leader, PricewaterhouseCoopers said:

> *"We are now firmly in a mining boom and 2005 was an exceptional year by any performance measure. The key question on everyone's mind is how long this can last, but early indications suggest the results in 2006 will be even stronger."*

Other financial highlights for the companies analysed include:

- Revenue increased by 25% to $222bn;
- Net profit margin improved to 20% from 16% in 2004;
- Net cash inflow from operations increased by 34% to $58bn;
- Capital expenditure increased by 31% to $31bn;
- Exploration expenditure increased by 29% to $2bn;
- Gearing dropped to just 16% with year-end cash balances totalling $32bn;
- Return on equity has increased from less than 7% in 2002 to 25% in 2005.

Commodity price increases, particularly in iron ore, coal, copper and gold are the main drivers of this outstanding performance. With the notable exception of iron ore, aggregate production did not change significantly for most commodities. Also, this improvement in profitability masks a 16% increase in operating costs, reflecting continued pressure on many input costs and a strong focus across the industry on maximising production.

PricewaterhouseCoopers' experts highlight a number of advantages that make Russian mining industry attractive for investors and support expectations of growth in the industry:

- High mineral prospectivity: opportunity to convert known deposits into reserves;
- Positive experience of foreign mining companies in doing business in Russia and establishing joint ventures with Russian miners and local governments;
- Move towards transparency by Russian mining companies has been significant over the past few years.

However there is a number of challenges that Russian mining industry faces:

- There is still uncertainty in government policy towards mining taxes and foreign investments;
- Distant location of deposits from existing infrastructure;
- Relatively low health and safety standards.

John Gross commented on the situation in Russia:

> *"There could be significant changes in the structure of the Russian mining industry, with significant changes in the Russian mining majors, domestic companies being acquired by inbound investment, increased direct entry into Russia by the major global mining companies and an increase in the outbound investment by Russian companies. Although Russia offers great opportunities for investors searching for tomorrow's world class mines, there are many challenges to overcome."* ☐