BFL CANADA

BFL MAKES A DIFFERENCE

The Cover Note

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EDITORIAL

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Mining is a major part of Canadian history as it has, without a doubt, significantly contributed to the development of our country. To this day, it remains an important economic activity from coast to coast. The word “mining” refers to a broad spectrum of activities and includes exploration, operation, and transformation of components found in just about every object we use and in many foods we consume in our daily lives. These components are also used in medical equipment and entertainment technology. They include: iron ore, gold, salt, diamonds, aluminum, copper, coal, oil, gas, potash, zinc, silver, nickel, and so on.

In 2012, the mining industry invested $22 billion in Canada, represented 3.5% of our GDP and over 20% of exports, provided 418,000 direct jobs, retained the services of 3,200 suppliers and accounted for more than 50% of railway transportation revenues. That year, four provinces – Quebec, Ontario, Saskatchewan and British Columbia – generated more than $8 billion in mining activity. Yet, this industry is somewhat unknown or misunderstood by many Canadians and gives rise to very passionate debates.

In the second half of 2013, this truly Canada-wide industry was affected by a hiccup in demand and prices on the international scene. This has undoubtedly impacted the economic contribution of mining in our country, at least for a little while. However, we should stay optimistic about the future since we saw prices going up again early in 2014. In addition to dealing with such market preoccupations (as all businesses do in their own sectors), mining encounters an assortment of challenges, including:

- The availability of financing;
- The availability of qualified workers;
- Regulation affecting claims, exploration, operations and royalties;
- Environmental activism and regulation;
- Safety;
- Technology.

These concerns add to the already unique depth and breadth of risk management issues and requirements that the mining industry has to face. Industry players need to dedicate a lot of efforts to overcome these challenges and issues, but also to navigate through their evolving environment and reach an equilibrium acceptable to all stakeholders.

With the constant presence of pending accidents related to the sheer size, nature or complexity of some of the activities of mining companies, it is of the utmost importance that they implement all feasible measures to avoid events of many types. So far, risk managers working in the mining industry have been doing an outstanding job. However, despite all their efforts, this industry is occasionally linked to tragic incidents, as has been the case some days ago in a mine near Sudbury. Moreover, many Canadians still remain uncomfortable regarding the footprint that mining activity is leaving on the environment.

Clearly we cannot live without the products of “mining” and the best way to enjoy the benefits of mining, our workers’ safety and a pristine environment is for all stakeholders to work together to achieve progress on all fronts.

In this issue, Janet McLean, National Practice Leader – Mining of our Vancouver office, discusses the financing of this industry in Canada. Tim Wade, Benefits Consultant at BFL CANADA Consulting Services, for his part, shares some tips on employee benefits programs. ♦

In this issue

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FINANCING MINE BUILDING PROJECTS—ARE LENDERS STILL SAYING NO?

Janet McLean, C.A.A.C., Vice-President, National Practice Leader (Western Region) - Mines
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Among many challenges a mine build project faces, one of the most difficult has recently been finding sufficient capital to bring the feasibility study to life, from the construction of the mine's infrastructure to its operation. The real problem when extensive feasibility studies are done – examining in detail using independent third party service providers and illustrating the proposed project – is showing it is an economically profitable project.

There are several concerns related to this, but one issue is that the feasibility studies sometimes utilize overly optimistic estimates of mineral pricing. These forecasts are subject to such volatile market changes that the numbers can quickly prove to be wrong. Another issue with these assessments can be incorrect estimates of costs for the construction of the mine, thus producing project overruns. Running out of money mid-construction and being unable to borrow more capital as the increased costs make the project unprofitable means serious defaults to lenders and often large losses to shareholders.

Are lenders beginning to revisit investments into mining projects? We are seeing some cautious interest from venture capital companies and from foreign governments such as China. There are very different reasonings driving interest in the mining sector from these two sources. Venture capital often seeks out investment into a slightly higher risk enterprise because the interest rates will be much higher than for a mainstream enterprise. Foreign governments' interests are often driven by the need for an end product: their motivation for being involved is to capture the product and funnel it back into their country in order to facilitate their own economy's growth.

Each situation bears a different end result: venture capital will most often tend toward a pure lender relationship, occasionally taking a small equity position whereas China's approach will generally be that of an outright purchaser of the mining company, although it might sometimes take a large equity position with a product purchase arrangement attached to it.

The impact of lower mineral prices coupled with lenders' reluctance to open their wallets is that small to mid-size mining companies with promising properties that are rich in high grade mineralization cannot move forward to realize profits from an exceptional asset. This also affects share prices and dampens investor interest in these companies and in the mining industry as a whole. The revenue for a small exploration company solely dependent on the stock market for cash is now in an expensive holding pattern betting that mineral prices will recover and/or that lenders will re-enter the arena.

Mining companies with one or two operating mines seem to be able to fare better than most by being able to reduce costs quickly, conserve cash and continue operations, albeit at a reduced profit margin. This revenue stream makes them a more attractive recipient for lenders' attention as they have weathered the price reductions and stayed profitable. These companies often remain in a position to go forward with plans to build another mine, but in a scaled back manner. The cost of the production equipment and the size of the throughput of the mill are revamped into a much smaller version of the initial plan, all in an effort to save money. They still progress into a revenue stream from which they can fund

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expansion plans in the future, slowly building the mine up into the large throughput operation they had planned at the onset of the feasibility study.

Large international mining companies seem to be too big to respond quickly to the mineral price bear market. They don't appear to change their budgeted spending mid-year as smaller mines can. As a result, they suffer losses that perhaps don't show until the next fiscal year, but that are still growing to larger losses. The big picture strategies start being pulled back to cost savings measures much later ; decisions seem to take much longer to implement once they are finally inked into their plans and budgets. While they are probably not cash poor, they do, in my opinion suffer from a much more serious impact to their stock price as their profit margins don't meet the big market analysts' expectations.

This kind of mineral pricing environment is conducive to mergers and acquisition activities. Some are born out of necessity, such as the small explorers with great proven property and a feasibility study that shows great promises but without capital to move into construction and not enough cash to keep the doors open. They become 'for sale' at exceptionally low prices for anyone brave enough to enter the sector and pay the carrying costs long enough to wait out the return of higher mineral prices. Also, larger mining companies with cash rich bank accounts can now afford to move on to mid and small companies in friendly (but often hostile) takeover actions profiting from their depressed stock prices to acquire mineral rich properties.

Whatever the play is, one of the biggest problems the mining sector faces is the lack of capital available to build mines. Most current mineral prices are still high enough to turn a tidy profit for most well-run mining operations, particularly in lower cash cost jurisdictions, like Mexico. In addition, world demand for gold, silver, copper, zinc and other minerals is not slowing down but rather growing. Why are we not seeing capital moving back into mines construction more rapidly?

If we wish to move successfully forward, I believe we need to stop being so concerned by what the stock market analysts think a company should have done in the short term, quarter after quarter, and start realizing that we need to put into play longer-term plans for the future of this industry and have the fortitude to stay the course to achieve success from them. In my opinion, the plan starts with moving capital into the Canadian mining industry thereby supporting our own economy in numerous ways by funding mine builds beginning in our own backyard! ♦

EMPLOYEE BENEFITS UPDATE

Tim Wade, Benefits Consultant, BFL CANADA Consulting Services Inc., Montreal

This is the first time in history that four generations share the workforce at the same time. The Boomers use more maintenance drugs, paramedical services and appliances and dental care. Gen X needs more acute type medication (i.e. antibiotics), some maintenance drugs (for the older part of Gen X), hospital visits, paramedical services and basic dental coverage. As for Gen Y, it views benefits in a more proactive way, using mostly paramedical care, vision care and basic dental care.

Each has their own view of the workplace and each group's claims apply pressure differently to a plan. **So what can you do?**

1. Inform and educate

- Cholesterol, blood pressure and diabetes can all be addressed in some way with a better diet and exercise. Set up educational lunches and seminars or at-work participation programs. An at-work program can be as simple as group walks at break time. What about setting up a Wellness Committee to find ways to be healthier in the workplace and at home?

2. Encourage better spending behaviours

- Ensure that the drug definition is "Mandatory Generic". Employees will be able to obtain their drugs while employers will be paying the lowest price possible for the correct treatment. This could lead to 2 to 5% savings annually.
- Could employees pay for dispensing fees (or even part of it)? This will encourage employees to shop for lower cost providers.
- Implement Specialty Medication Management Programs. This type of program has shown to be of great value with pointed delivery and advice through designated pharmacies that specialize in particular serious conditions and complex drug therapies.
- Implement a Preferred Pharmacy Program to help control drug costs and dispensing fees. It can result in savings of 4 to 10% per prescription.

3. Create flexibility for both employer and employee

- Utilize Health Spending Accounts (HSA) to fix costs. Some benefits can be better provided through a HSA to ensure stable future pricing and more equitable distribution. Using a HSA allows employees the flexibility to cover the claims that are important to them. The HSA amount is controlled by the employer, not the insurance carrier.

4. Ensure competitive pooled rates

- The pooled benefits (Life, AD&D, Dependent Life and LTD) are demographic and industry driven. Review the marketplace every three or four years.

5. Help them plan for their future

- Over 3.5 million working Canadians do not have access to any sort of pension/retirement plan at their place of work. A retirement plan is simple to administer and to set up.
- The insurance carriers have fantastic planning tools for employees.
- Your broker can provide annual group education seminars and governance.
- Employer contributions *may* bypass payroll taxes (EI, CPP/QPP, EHT and WSIB/CSST), depending on your particular situation.

These are a few measures you can implement to protect your program and ensure that you continue delivering coverage and corporate policy to your personnel on how to deal with death, disability, high medical costs and retirement. It is important that your coverage be perceived as an "employee benefit" and assist in attracting and retaining your biggest asset : current and future employees. ♦

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