2016 BDO GLOBAL MINING MIDDLE MARKET MONITOR

Shoots of Optimism Emerge for a Battered Global Industry

It's no surprise that the global mining sector has endured a difficult few years and, for many mining companies, optimism has been in short supply. Persistently low commodity prices, waning demand, and tightening capital and credit markets have been squeezing the industry, and no one has been immune to the pain. Mining companies of all sizes—from the giants to the juniors—have seen the strong profits of 2011 and 2012 give way to painful losses, and exploration has slowed to a trickle as the industry waits to see if and when the markets begin to cycle upward.

But according to BDO's inaugural ***Global Mining Middle Market Monitor***, the end of the latest downturn may be in sight. The study found that although companies continue to struggle, there is reason for optimism: Among global middle market mining companies from 2014 to 2015, median exploration expenditures grew 17 percent, median price-earnings (PE) ratios grew 15 percent, and median cash balances increased a modest—but still promising—2 percent.

"The global mining industry has had to navigate intensely murky waters over the past half decade, first digging out of the fallout of the 2008-2009 financial crisis and rebuilding, only to falter again amid volatile commodity prices and softening Chinese demand. Creativity in this industry, then, may be the ultimate kingmaker: Mining companies that are able to find effective ways to streamline their businesses, maximise their resources, collaborate with the right partners, and develop a nimble core business will be the first able to take advantage of any market rebound."

Charles Dewhurst, Leader of the Global Natural Resources Practice at BDO

Please see the methodology note at the end of this report for more information on the ***2016 BDO Global Mining Middle Market Monitor***.

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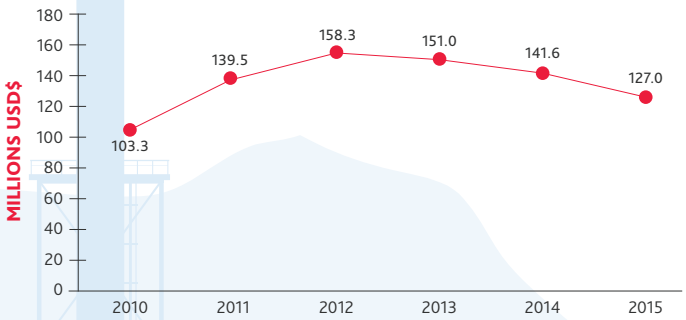
Revenue & Income

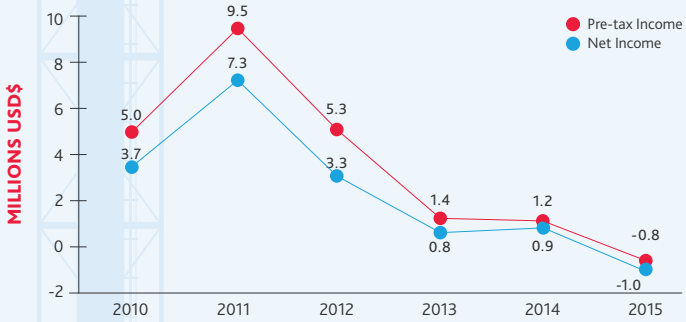
GLOBAL MEDIAN REVENUE



MEDIAN REVENUE among middle market mining companies in 2015 was **DOWN 10%** from 2014, but **UP 23%** from 2010.

*In comparison, among the world's 28 largest mining companies, **MEDIAN REVENUE WAS DOWN 16%** from 2014, and up just 4% from 2010.*

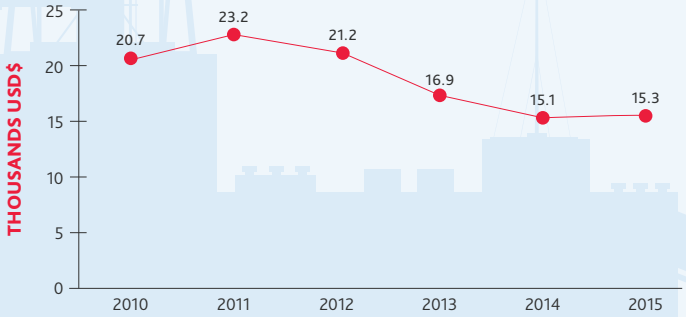
GLOBAL MEDIAN PRETAX & NET INCOME



MEDIAN PRETAX INCOME DECREASED BY 116% and **net income PLUMMETED 127%** since 2010.

*As a result of these losses, the **MEDIAN EFFECTIVE TAX RATE DECLINED TO 0%** from a 5-year high of 17.8% in 2011.*

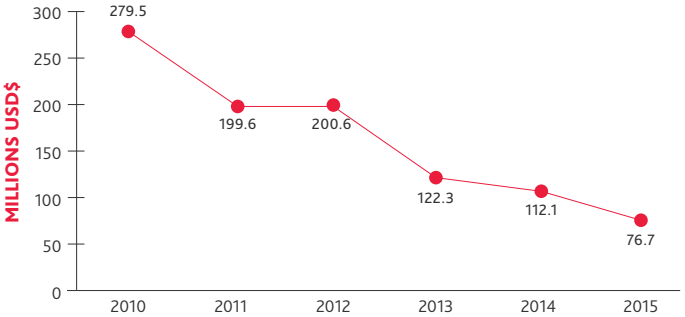
GLOBAL MEDIAN CASH BALANCE & SHORT-TERM INVESTMENTS



MEDIAN CASH BALANCE and short-term investments **DECLINED 26%** from 2010 to 2015, but **GREW 2%** between 2014 and 2015.

Investor Confidence

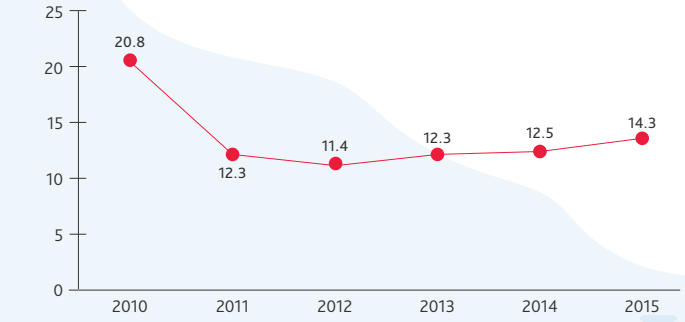
GLOBAL MEDIAN MARKET CAPITALISATION



THE MEDIAN MARKET CAPITALISATION DECLINED 73% between 2010 and 2015, and **32%** between 2014 and 2015.

The decrease seen from 2014 to 2015 among middle market companies mirrored the decline seen among the larger players (37%).

GLOBAL MEDIAN PE RATIO



THE MEDIAN PE RATIO DECREASED BY 31% from 2010 to 2015, but **GREW 15%** between 2014 and 2015.

Among the largest mining companies, the median PE ratio actually decreased by 2% from 2014 to 2015.

Exploration

In 2015, median exploration expenditure **DECLINED BY 48%** from 2010 levels, but **GREW 17%** from 2014 levels.

What Lies Ahead for the Global Mining Industry?

The primary takeaway the mining industry should glean from the *2016 Global Mining Middle Market Monitor* is that, although we're beginning to see positive momentum in the sector, we have a long way to go before the industry regains full strength. Even as commodity prices slowly inch upward, capital remains tight, and global demand is unlikely to soon reach the levels the industry once enjoyed.

But middle market mining companies tend to exhibit a high degree of flexibility and manoeuvrability when compared to their larger counterparts, and they are looking for opportunities to streamline their businesses across the board. But the key to maintaining this nimbleness and securing a sustainable recovery is making cuts without handicapping the ability to grow operations and make smart investments as the markets improve. While companies should always evaluate their operations and assets to determine where to trim the fat, here are three key areas where miners would be well-advised to eschew austerity and embrace innovation:

Regulation

2017 promises to be a time of considerable political turbulence. Between a new U.S. presidential administration, the fallout of Brexit, China's growing economic power, global efforts to curb climate change and protracted conflict in resource-rich regions, mining companies must keep a wary eye on how the geopolitical tides turn in the coming year. New regulations may emerge, or old ones may take on renewed urgency as governments seek to crack down on fraud, environmental damage and human rights violations. While the cost of regulatory compliance is often high, this is one area where mining companies cannot afford to cut corners.

Consolidation

There is no single, obvious global trend line for M&A activity in the mining sector. In some countries, like Canada, consolidation has been an important avenue for struggling companies to shed underperforming assets, shore up their operations and stay afloat. But in other countries, such as the U.K., the cost of M&A is too high, and capital is too scarce for transactions to be a viable option. Mining companies seeking to merge or sell off some portion of their business must ask themselves several key questions to ensure they're making a good deal: Are buyer and seller seeing eye-to-eye on valuations? If exploring a merger, what liabilities might the combined business carry? What will integration look like? What are the tax implications of the sale? A sub-optimally structured or failed transaction can be particularly costly in the current market, and could cause more problems than those it set out to address.

It may be some time before the mining industry enters another boom phase, but there is reason to believe the worst of the bust is now behind us. Key trends to watch in 2017 include continued increases in exploration and gradual movement toward increased M&A activity—if these trends begin to pick up steam, we could be looking at much brighter days ahead.

Labour

In a low-commodity-price environment, many mining companies have been forced to implement significant layoffs. The tradeoff, of course, is that a downsized labour force may not be large enough or may lack the breadth of skills required to take advantage of an eventual industry turnaround. Combined with regulatory scrutiny surrounding health and safety standards for workers, mining companies must make difficult decisions to contain their labour costs without cutting themselves off at the knees. Savvy mining companies are using a scalpel to make the necessary labour cuts—not a chainsaw.

ABOUT THE BDO GLOBAL MINING MIDDLE MARKET MONITOR

The ***2016 BDO Global Mining Middle Market Monitor*** reviews and analyses financial data reported by 528 publicly traded middle market mining and diversified metals companies from 61 country and international stock exchanges from 2010 to 2015. Countries represented include Argentina, Australia, Canada, China, Greece, Hong Kong, India, Indonesia, Japan, South Africa, South Korea, Taiwan, the United Kingdom and the United States, among others.

The companies analysed reported revenues up to $1 billion, with median revenue of $127 million.

Data was gathered from S&P Capital IQ. All monetary data was converted to U.S dollars.

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