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BHP shuns China price cut plea

BARRY FITZGERALD THE AUSTRALIAN AUGUST 08, 2013 12:00AM

Andrew Mackenzie, centre, speaks with Liberal MP Josh Frydenberg, right, and Asia Society chairman Warwick Smith in Melbourne yesterday. Picture: Mcevoy Stuart Source: TheAustralian

BHP Billiton's new chief executive, Andrew Mackenzie, has stared down a request from the highest levels of China's new leadership for lower iron ore prices.

Mr Mackenzie, chief executive of the world's biggest miner since May 10, revealed to The Australian yesterday that the request came from Chinese Premier Li Keqiang in June at a private meeting between China's new leadership and chief executives from select foreign businesses important to the now slowing Chinese economy.

During the meeting, Mr Li side-stepped his interpreter and said to Mr Mackenzie: "Lower prices, lower prices."

While not specifically mentioning iron ore -- Australia's biggest export earner with annual sales of more than $US57 billion ($64bn), according to government estimates -- the steelmaking raw material is the commodity China is most exposed to on imports from Australia.

Fresh from making his first major local speech yesterday as BHP's new chief executive to an audience of 510 people at an Asia Society in Melbourne, Mr Mackenzie said he reminded the Premier that prices "were now at more sustainable

levels" and were already "quite low".

Source: TheAustralian

In mid-June the spot iron ore price was $US115 a tonne. While that was well short of the $US180-a-tonne levels of April 2011, it was also sharply higher than the $US87-a-tonne iron ore price low in September last year. Iron ore prices have moved higher since June, and were last quoted at $US131 a tonne.

Iron ore prices surged 12 per cent in July alone despite a slowing economy as China's steel mills worked at restocking, lifting purchases to the highest levels since the December quarter last year. The strength in iron ore prices -- it remains highly profitable at current prices -- is despite fears of over-supply in the Chinese steel industry at a time of slowdown.

Last month Mr Li said China needed to be vigilant against a sharp downturn in the economy. He was quoted on state TV as saying that as long as growth stayed within a comfort zone, there would be no need for changes in economic policies. The leadership believes a 7 per cent economic growth target is achievable. Macquarie analysts said yesterday that it still expected China's steel industry to make production cuts, leading to a "benign" outlook for iron ore, which would see prices fluctuating around the level of $US125-$US130 a tonne.

Mr Mackenzie stressed that he believed that Mr Li's opening request to him for lower prices was a friendly quip. "I met him privately later and he kind of said it with a cheeky grin," Mr Mackenzie said.

Jocular or not, the Premier's wish for lower prices represents a continuation of the friction that has existed between the Australian iron ore industry and its major customer ever since the the steel-intensive nature of China's previous double-digit economic growth fuelled bumper prices for iron ore. Current prices are at multiples to the cost of production by the three companies that dominate the seaborne trade in the product -- Rio Tinto, BHP and Brazil's Vale.

But Mr Mackenzie believes that if anything, the "Chinese are becoming more comfortable with the way in which they get their supply from world markets".

"And they are more accepting about the price-setting mechanism that happens through many of the things that my predecessor (Marius Kloppers) and others have introduced," Mr Mackenzie said. The main change has been the switch from annual benchmark pricing to spot or index-related pricing, which has removed the annual antagonism that benchmark pricing used to cause.

Mr Mackenzie said that China's acceptance of a market clearing price for iron ore was growing. "Their people are more comfortable on the transparency and comfortable that they will get the supply," he said.

But at the same time, Mr Li and other leaders across Asia are aware of the dependency on the supply from Australia. "And they hope that we continue to honour that. It's a kind of mutual relationship," Mr Mackenzie said.

Earlier in his speech, Mr Mackenzie said resources were fundamental to Australia's relationship with Asia. He said it was a relationship that "secures economic prosperity for both and provides new opportunities from agriculture to education to tourism, while promoting stability in the Asia-Pacific".

"Customers and governments in Asia have made it clear to me that they are relying on BHP and Australia to continue to supply the resources needed to fuel their economic growth," he said.

Mr Mackenzie said in his speech that he had told Mr Li in June that China and other developing nations "can count on BHP and Australia to work to deliver the sustainable, low-cost and secure supply of basic raw materials that Asia and the world need to grow".

But the now-revealed request from the Premier for "lower prices" was not part of the speech.