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# The Resources Company Growth Challenge

Graeme Stanway – Director, Slate Advisory

Established resources companies are facing significant risk through the strategic choices that they will be making over the next few years.

Since the end of the China-driven resources boom, most miners have spent the past 5 years aggressively cutting costs and focusing on productivity, while at the same time enjoying strengthening commodity prices. The mantra has typically been “value over volume”, “returning cash to stakeholders” and “building the platform for future growth”. As a result, many are now in rude financial health and with strong balance sheets in place are inevitably starting to turn their focus towards growth. And therein lies the risk – so is everyone else!

Resources companies mostly grow through acquisition, whether focused on the early stage and seeking exploration farm-ins, or focused on the late stage and seeking fully developed assets. Either way, when buyers emerge en masse, the potential for asset prices to exceed real long-term value is high.

So, what can CEOs and Boards do about this conundrum of wanting to grow, while needing to differentiate from the herd? The answer is necessarily bespoke and complex, but a few focal points are offered for consideration.

*1. Go where competitive advantage is real*

The first challenge is to be brutally honest about whether or not the business has a truly privileged position when acquiring an asset. Mounting pressure from stakeholders to grow, coupled with natural biases in self-assessment, inevitably cloud this judgement. Assembling a high quality deal team to acquire assets, having a team of disciplined and effective operators, or possessing a reputation for safe and sustainable operations may be necessary components but by themselves are typically insufficient to build an “asymmetric” position when acquiring assets. So then, what is the real advantage?

Durable competitive advantage is typically unique for a given business and not a selection of pre-packaged choices. It is built through an integrated blend of social, process and technological

competencies that have been invested in over a lengthy period. By definition, **competitive advantage demands innovation leadership in aspects of both the business and operating model.**

A business' real advantage should dictate its acquisition focus, be it an asset's position on the development value chain (greenfields to reclamation), its geography or, of course, the product. The lure of an apparent opportunity which is not well aligned with competitive advantage, but opportunistic, is risky. It is extremely high risk in an environment where competition for assets is high.

Having said this, there will be certain occasions when assets are compelling value and where acquisitions are used as a deliberate and measured means of augmenting or shifting competitive advantage - particularly in advance of shifting external trends.

*2. Get the macro external calls right*

Overpaying for assets, or over investing in development, is a big risk for miners. An asset that is high quality and a good potential business fit, says nothing about whether the price paid is value accretive. When one looks at the ledger of failed acquisitions, causes invariably include buying or expanding too late in the cyclical upturn or misinterpreting long term demand signals. What is often less clear, however, is perhaps the bigger opportunity cost of not acting to invest countercyclically when asset values are compelling. Acquisition failures also include simply misunderstanding the quality of a given asset, but this has little to do with the macro calls and everything to do with the competency requirements described in point 1 earlier.

The challenge with making macro external calls is that many aspects of the long term external environment are highly uncertain. One frequently hears the disclaimer in strategy presentations that the future is impossible to predict, along with the associated decision to adopt analysts' consensus perspectives of the future. These are invariably short term and tend to be extrapolations of the past, and therefore not particularly helpful for the longer term in which perspectives typically from 5 – 20 years are required. This fatalistic response is a bit like driving in the dark, without headlights and continuing "straight ahead".

So, what can be done? The key is ongoing scanning and analysis of the external environment to **understand potential scenarios and the pathways and triggers which could lead to their development.** Strategic conversation to form interpretation relevant to the business and decisiveness in making investments (or divestments) where there is reasonable certainty and building in optionality where there is significant uncertainty, but high potential upside (or downside). The challenge in maintaining capability to effectively conduct this type of work is real as it requires a breadth of skills, deep external insight and continuously challenging inevitable industry and internal executive biases and norms which develop. But given the upside, the payoff is worth the effort.

*3. Play the long game*

If a truly multi-decade perspective is taken in managing the business for long term success then points 1 and 2 are feasible. If not, then they are nearly impossible.


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Companies that are committed to being in business, and thriving in say 30 or 50 years' time, seem to find the patience and have the fore-sight to invest countercyclically and are prepared to allocate risk capital for innovation in competitive advantage mindful of well understood and internalised long term external scenarios.

Big private companies in particular are noted for doing this well, as are certain national cultures. However, western public companies faced with relentless short term financial performance expectations from investors and CEO tenures and incentives packages which typically have a much shorter duration than economic cycles, very often struggle to play the long game.

This is a deeply institutional and cultural challenge, and perhaps the most difficult, and most important, of all the points raised in this article, particularly in resources industry where investments are multi-decade decisions. Irrespective of investor external pressures, ultimately playing the long game starts with the **board and the executive leadership understanding of the external environment, developing and sticking with long term strategy and in making their case to investors.**

Ironically, the companies that have done this well, are the ones that are probably less uncertain about how to grow now and are therefore at less risk form herd behaviour, because the options are already in place!


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