Australia's BHP restructures in a bid to appease the markets

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Paul Anderson, CEO of Australian mining giant BHP, announced late last month plans for a further restructuring of the company in an attempt to halt the sharp slide in BHP shares. Once the largest company in Australia, BHP has been overtaken by firms such as Rupert Murdoch's News Ltd. as investors shift from industrial stocks into the technology, telecommunications and media sector.

Much of the five-year plan that Anderson paraded before an audience of stockbrokers had already been announced at the end of last year. It involves more asset sales, floating its Long Products Steel Division and driving up productivity to unprecedented levels. Thousands of jobs are threatened and remaining workers face the elimination of the most basic conditions.

Less than two months ago, BHP shares were valued at just over $A22; they are now hovering around the $16 mark, wiping out almost $9 billion from the company's market capitalisation. Anderson was forced to address a Securities Institute of Australia luncheon to sell BHP's plan. There was a “great deal of value still to be delivered from restructuring,” he claimed. “I do not think this potential is fully appreciated by the market”.

Anderson said BHP had set itself a target of achieving a 12 percent return on capital over the next five years. “I appreciate that the market is eager for information on the next phase of BHP's activities—the value delivery phase... These performance measures are a response to your feedback that you would find it useful to have some quantification or milestones by which you can monitor our progress”.

Some financial analysts immediately criticised Anderson, insisting that the benchmark needed to be 15 percent. Since 1997 BHP's returns on investment have fallen from 7.4 percent to 6.6 percent in 1998 and a 3.5 percent last year, despite asset sales of nearly $6 billion.

Anderson told the Institute that, “In a portfolio and financial-management sense, considerable progress has been made to address dysfunctional parts of the BHP portfolio.” BHP is now dealing with its “dysfunctional parts” by selling parts of its Steel Division and imposing individual contracts on its iron ore miners in line with its competitors.

The five-year plan includes cutting costs by $1.5 billion or 2 percent each year, raising $4 billion from divestments over the next 16 months and generating a cash flow of $11 billion within two years to create a war chest aimed at increasing BHP's assets in minerals and petroleum. BHP is restructuring into a business where minerals constitute 40-50 percent of its holdings and petroleum 30-40 percent, with steel less than 20 percent. At present, minerals are 45 percent, petroleum 25 percent and steel 30 percent.

The company's president of minerals development told a private mining conference in New York two weeks ago that BHP had re-commenced negotiations with Rio Tinto for a $14 billion merger of the two firms' iron ore operations. If successful, the merger would virtually monopolise Australian iron ore sales to the Japanese steel industry, potentially driving up ore prices and reducing costs for both firms.

Rio Tinto canceled merger talks in last July, claiming BHP was overvaluing its iron ore operations and was not “aggressive enough” in driving up productivity through changes to work practices. Rio Tinto is currently mining iron ore at $7 a ton less than BHP at its mines in West Australia's Pilbara region and Brazil. BHP responded to the collapse of the merger talks by introducing individual contracts in the Pilbara, a move Rio Tinto made years earlier.

Anderson specifically raised the Pilbara issue in his Institute address. “Our iron ore assets are world class and we have a responsibility to ensure that the right value is extracted from them. The individual workplace agreements in place [by Rio Tinto] in Western Australia are already delivering the sort of work arrangements we know are possible in iron ore from our workforce.”

National industrial action last month against BHP's individual contracts led to a series of closed-door meetings between the company and the union leadership. Negotiations between the Australian Council of Trade Unions (ACTU) and BHP were called off late last month, pending a Full Federal Court ruling on the legality of BHP's individual contracts.

Anderson indicated that the ACTU leaders know exactly what BHP expects of them. “We have been in discussion with the unions and they now have a clear understanding of the changes in behaviours and business outcomes that are required in our iron ore business.” Union officials have said they are ready to strike a deal that “everyone can live with” despite BHP's iron ore president Graeme Hunt declaring that total company control of staffing, hours, rosters and salaries was “not negotiable”.

Workers in the Steel Division face immediate job losses. Last November BHP announced a plan to sell or trade $3 billion (nearly half) of the Division. It appears, however, that BHP was unable to find a buyer. Its board of directors voted last week to accept a recommendation from the company's financial advisers, Credit Suisse First Boston, to float the $2 billion Long Products Steel Division. In a bid to dump the Division on current shareholders, former BHP Steel chief Bob Every will form a new company (Alliance Steel) and shareholders will be enticed to buy shares with a two-to-one stock swap. The float would relieve BHP of $1 billion in debts.

Every has hinted that the new firm would reduce the 2,000-strong workforce employed by the Long Products Division in the Hunter Valley. BHP's Steel Flat Products manager George Edgar signaled a decrease in the 6,500 workforce at the Port Kembla steel plant. Management and unions at Port Kembla assured workers last November that their jobs were relatively secure, but Edgar said departments at the plant would be closed down or sold. “There is an urgency about making changes now,” he added.