MELBOURNE MINING CLUB
8 February 2018
Speech by Alberto Calderon

Sustaining our economic successes

Thank you for that introduction Patrick.

I would like to acknowledge the traditional owners of the land on which we meet, and pay my respects to their elders, past and present.

I also acknowledge our distinguished guests today, including the Patron of the Melbourne Mining Club, Sir Arvi Parbo.

It is an honour to be speaking here today. I was at the last Melbourne Mining Club event in December, when we celebrated the 100th Club event. It is fitting that today, in the first of the next 100 speeches, we revisit the industry's contribution to Australia's prosperity and consider some of the challenges our nation faces to maintain our standard of living.

Let me begin by exploring what is at stake.

The resources sector's contribution to Australia's standard of living and economic growth

Australia is experiencing the longest period of sustained economic growth for at least the past 50 years. In 2017, we recorded 26 years of uninterrupted economic growth. This far exceeds the booms of the 1970s and 80s, which lasted only seven or eight years, and makes us unique amongst major developed economies. To put this in a workplace perspective, Australian-born employees younger than their mid-forties have never experienced a recession in their working lives. For them, the impact of major economic shocks is something observed from afar. Australia cruised through the Asian economic crisis in the late 1990s and we actually grew when the dot.com bubble burst and the US entered recession in 2001. Our economy continued to grow through the 2008 Global Financial Crisis and our GDP growth since the GFC has exceeded the rate of most major economies, including the US, the UK, the Euro region and Japan.

What has driven our economic resilience and prosperity? The distinguishing factor has been private business investment. Data from the Reserve Bank shows that investment as a percentage of the Australian economy rose to a multi-decade high around 2012. This contrasts with the experience in nearly every other country, with the exception of China, and it is not by accident this coincided with the once-in-a-lifetime resources boom.

Private investment from the mining sector peaked at around nine percent of the economy, and The Minerals Council of Australia estimates that more than $400 billion was invested in mining, energy and infrastructure projects. The other strong contributor to investment growth was of course residential construction.

We have enjoyed a long period of growth and dodged the economic shocks that have impacted other countries, but where does this leave us? The fundamental drivers of our performance, mining investment and housing construction, have peaked. Mining investment is expected to remain at its more normalised, long-term level of around three per cent of GDP, and residential construction is forecast to experience negative growth in the coming years.

So where will our future growth come from?

In very general terms, economies grow and living standards rise when households are spending, business is investing, and net exports are growing.

Let's look briefly at the largest element of the economy, consumption. While household consumption has contributed solidly to GDP growth in volume terms, growth in household expenditure is almost the lowest on record. And the outlook is not good. Our savings ratio, at three per cent, is the lowest it has been in almost 60 years, with the exception of the early years of the 2000s, and our household debt to GDP ratio is among the highest of the developed world. Even if we avoid a housing price crash, the low savings ratio and high private debt level imply that household consumption will contribute significantly less to growth than in the past decades.

The outlook for net exports is also subdued, and likely to be a drag on growth. The current account deficit is forecast to grow to somewhere between three and four per cent in the medium term.

Government spending is supporting growth and could reach almost 19% of GDP. However, as we all know, long term growth does not come from the public sector. Sustainable growth can only come via the private sector, and given that this will not come from mining or housing, it must come from non-mining business investment.

Guy Debelle, the Deputy Governor of the RBA, recently delivered a very good speech on Business Investment in Australia. He highlighted that non-mining business investment as a percentage of GDP is currently at its lowest level since 1960 – around nine per cent. His explanation is that "expectations of weak future conditions are plausibly restraining business investment even more than current conditions" and that "there are signs that the generalised improvement in business sentiment is leading to a global reassessment of investment decisions…".

The conclusions are clear. The main drivers of growth during the past two decades – mining and housing – will no longer contribute at the same level and household consumption will not be able to fill the gap. This underscores the need to create the right conditions to boost business investment and capital productivity.

But under the current tax and regulatory environment it is difficult to see how business investment is going to fill the void left by the mining and housing sectors.

We need a tax environment that is conducive to growth and is competitive relative to the countries against which we compete for capital. Doing nothing will not awaken the animal spirits Debelle mentioned in his speech. Doing nothing will in time - maybe not next year but certainly in the near future – without a doubt, lead to very low levels of growth.

I am not necessarily suggesting we blindly follow the United States in its tax strategy. There should be much more discussion around the optimal combination to create the greatest benefits for society, and the largest impact on growth. There is a view that a reduction in the corporate tax rate would result in increased investment activity, the creation of more jobs and higher wages. However, our franking system makes the analysis a little more complex. If we simply pass on any tax cut to shareholders through increased dividends instead of financing new investment, the benefit to the investor is offset by reduced franking credits. The impact would also be particularly relevant for retirees whose income projections rely on the imputation credits at thirty per cent.

There are complementary and alternative ways to encourage local and offshore companies to invest in Australia. Companies invest to expand their operations, build new plants and factories, buy equipment and develop new technologies to boost productivity. It would seem to me that introducing targeted incentives in areas such as these can directly increase activity in Australia, in a way that provides lasting benefits. This could be achieved by improving the Australian research and development incentive, introducing better capital allowances either directly or through accelerated depreciation, or targeted reductions in tax rates for capital intensive or high technology manufacturing. A tax environment that incentivises investment will benefit all Australians through job creation, increased wages and improved living standards in the long term.

Changes to the tax regime alone will not induce long term, sustainable economic growth. If we are to support private investment, our regulatory regimes for energy, transport, water, land access, telecommunications and other infrastructure services need to support, not add to the cost and timeliness of projects and the cost of operations. It's equally important that access to mobile and skilled workers is not hampered by populist politics.

Harnessing our comparative advantage

While these matters fall largely to governments, the task of value and wealth creation sits squarely with industry. We are responsible for creating the jobs and value to support our living standards.

So, what must we, as industry, as the nation's wealth creators, do to sustain our advantage?

We know value is maximised when countries focus on their comparative advantage. Australia is, we all know, a global resources powerhouse. While there is an urgent imperative to lift investment in the non-mining sector, we must not lose sight of the importance of the resources industry to our economy. By building on our natural advantage and global scale, the resources industry can continue to contribute to growth and living standards.

We are already responding to the challenge. Our industry is being reimagined. Robotics, automation, big data and the Internet-of-Things are transforming every element of our value chain – from exploration, mining and processing to transport. New technologies are delivering significant advances in safety, environmental and productivity outcomes. We are lifting utilisation rates, operating more precisely, reducing maintenance costs and increasing asset life.

The opportunity for individual companies and the broader economy is significant. At a company level, innovation is extending mine life, improving bottom-line financial, safety and environmental performance, and making our businesses more resilient and globally competitive.

For Australia, the opportunity is to establish ourselves as a global leader in mining automation, expand our mining services sector, increase our knowledge-based exports and apply our experience to other sectors. We have a comparative advantage in natural resources, we have the necessary human capital and expertise - Australia is a natural home for mining innovation.

Orica has a unique vantage point and role to play in this transformation. We are an Australian-based, global mining services provider with a long history and strong commitment to innovation. We spend a lot of our time with customers, listening to what is driving them, and finding ways to deliver change that is important to them.

Our expertise is blasting, and history shows that blasting can contribute significantly to productivity and safety. The introduction of ammonium nitrate as a bulk explosive in the 1950s and 1960s was critical to the commercial development of large, open cut mining operations. The growing use of emulsions in the 1980s lifted productivity again, and in the early 2000s, Orica commercialised electronic detonators which delivered the next big step change in blasting precision.

It’s interesting though that blasting is one of the few processes in the mining value chain that remains largely untouched by automation. Our customers are working to change that. And so are we.

Last year, we commercialised the world’s first wireless detonator – WebGen™ 100. We believe this breakthrough is at least as big as any of the major milestones I’ve just listed, and it will put our customers one step closer to true automation. WebGen™ uses wireless technology to initiate blasts through rock, water or air from surface control rooms. With the manual task of connecting wires removed, our customers are removing people from harm’s way, and eliminating productivity losses caused through damaged wires. The use of this new technology has allowed one of our customers in North America to alter the mining sequence in their underground mines, delivering significant productivity gains.

The automation of drill and blast will be a game changer for the industry, just like the introduction of ammonium nitrate was in the 1950s and 60s. We’re proud of the role we’re playing alongside our customers as they deliver this transformation, and we’re excited about the benefits it will deliver for us too.

In Australia, for example, we ended last year on a high note with the win of a significant BHP Iron Ore contract in Western Australia, and started the year with the win of the Roy Hill contract, also in Western Australia. Our contract with BHP includes a technology partnership through which we will develop, trial and introduce new technologies. This will support BHP’s ability to incrementally bring automation and technology to bear on their drilling and blasting challenges. Only we have the technology building blocks to support their ambitions, and we’re excited to have been selected as their partner to help achieve such an important breakthrough.

Another major theme we’re responding to is Big Data. Our customers collect huge volumes of data at mine sites, but only a fraction of it is used. Part of their frustration is that the data often remains disconnected in disparate systems owned by customers and service providers. There’s an obvious opportunity to change that. If our customers can capture and analyse data from right across the value chain, they can fully understand the impact blasting has on other parts of the mining value chain. And because blasting is so early in the value chain, the potential to improve overall mine productivity is high. Our BlastIQ™ product brings together data from existing systems. It puts information about the impact of each blast in the hands of the teams that manage the blasts. When they can measure the value of their decisions, they can start to close the continuous improvement loop to achieve better safety and productivity.

Conclusion

These are merely two examples from our rapidly changing world. The full potential for change is yet to be explored. Australia has an opportunity to be at the forefront of industry transformation, but we need a regulatory environment that is attractive to capital investment and that promotes and rewards investment in technology and innovation. This will be key to ensuring we not only remain competitive against other countries, but that we also leverage our strengths in human capital and innovation to build on our natural advantage and global scale in resources, and continue to contribute to Australia’s economic success.

Thank you.