



**The American Chamber of Commerce in Australia  
Address by Orica CEO, Alberto Calderon**

**1 September 2016**

Introduction

Good afternoon. It's a pleasure to be here today with one of Australia's most highly regarded business associations.

For some of you in this room, the linkages between Orica and America may not be well known, so let me give you a brief overview of this.

Orica is uniquely geographically diversified. We have around 12,000 people working around the globe, servicing customers across more than 100 countries.

We operate along regional lines, with our four regions being Australia Pacific & Indonesia, Latin America, North America, and a number of smaller, dispersed customer centres in one conglomerate regional grouping of Europe, Africa and Asia.

Orica has a legacy spanning more than 140 years, through every part of every mining cycle over that time. We command a leading market share in most of our major markets.

Orica is an Australian company, a Melbourne icon. Maybe because of that it sometimes comes as a surprise to people that North America is actually an important and successful market for us.

Our North American business has been operating in some form or another for more than 100 years<sup>1</sup>.

It has almost 800 people working across around 50 sites, covering mining services and supply, manufacturing and our Minova ground support business. Our North American business is well diversified, serving customers predominantly in the gold, coal, iron ore, and copper mining, and quarrying and construction industries. The region accounts for around 26% of our Group-wide revenue and is our second largest market after Australia Pacific & Indonesia.

We have a highly competitive position in a market that is notoriously tough. When I talk to business people all over the world, it's a relatively consensus view that a company that achieves merely 5% market share in North America is a company doing well. By contrast, Orica has more than 40% market share, along with a double digit Return on Capital Employed. We have achieved this through our combination of exceptional quality, competitively located assets and logistics infrastructure, and world class service. But we are not content to stand still, and our team there is working to be even better.

However, there are significant challenges not only in North America but globally, given the tough market conditions the mining sector has been facing.

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<sup>1</sup> Atlas Powder formed in 1912 out of DuPont.

## Market context

Before I talk about Orica's approach to managing through the cycle, it's worth taking a step back and understanding where the market is now, and where we have come from.

From 2004, Australia experienced a decade of unprecedented growth in the resources sector, with the price of our mining exports more than tripling, driven predominantly by China's industrialisation.

But over the past couple of years, China's growth has slowed and the pricing outlook for metals and mining remains relatively subdued. Furthermore, the coal industry globally is certainly facing a structural shift in demand, as the world attempts to move to lower carbon alternatives. In the US market, coal has been adversely affected by the fall in the natural gas price – a result of more unconventional exploration and production efforts. Coal's traditional advantages over natural gas of cheap abundance no longer apply. New regulations in the US, such as the Clean Air Act, MATS and the efforts to regulate carbon emissions, have also collectively sped up the retirement of older coal-fired power plants. Coal, of course, still has a strong future for the short to medium term, but it's impossible to predict its demand curve over the longer term.

Meanwhile, Ammonium Nitrate – a core Orica manufactured product – remains in oversupply in both the US and Australian markets.

Despite the fact that mining is cyclical, the speed and severity of the recent pricing downturn was not anticipated. And while the cycle will also eventually turn, the timing of the upswing has been historically difficult to predict.

What we know for sure is that the most recent commodity price boom is well and truly over, and the resources sector has had to adjust relatively swiftly to a new norm of lower prices. Of course, what affects the mining industry has a flow on impact on the mining services sector, and Orica has not been immune to this.

Given the current environment, the mining industry has had to re-define the way they work, and by and large they have done an outstanding job of this. One sizable Australian iron ore house, for example, has reduced its cash costs per tonne by almost 70% compared with four years ago. The industry is filled with companies that have re-invented the way in which they work to realise greater efficiencies.

So in the cyclical reality in which we currently exist, we all have to adapt in order to thrive in this new environment. In my view, the companies that will perform best in the challenging times and be best positioned to benefit when the cycle inevitably turns will be those that:

- firstly, effectively control all the elements they can;
- secondly, have the right culture;
- thirdly, have effective leadership at all levels of the organisation; and
- finally, have a deep and enduring understanding of their customers.

So today, I would like to talk to you about how we at Orica are facing up to these challenges.

### A basis for optimism

Despite the tough market conditions in the short to medium term, we believe our differentiated strategy will enable us to create greater value for our shareholders and customers over the long term, by bringing together our industry expertise; quality product and service applications; and safe and reliable supply; underpinned by our unmatched investment in innovation to deliver better solutions.

We are also increasingly focusing the *whole organisation* on the customer to become a truly customer-centric organisation, with a deep understanding of our customers' needs for a better outcome for them and us.

Together, our strategy and customer focus will drive our growth. However, our current circumstances also requires us to prioritise some actions that will see us emerge stronger from the challenges that we face today. These are:

- controlling the elements we can;
- having the right culture; and
- ensuring the right leadership within every level of the organisation.

### Controlling the elements we can

We have taken decisive action at Orica to control those elements that we can. We have introduced a range of business improvement initiatives to deliver sustainable savings. In our half year result in May, we announced that we had achieved net benefits of 52 million dollars through this program of work, with 80% of those benefits baked in – that is, repeatable for the long term. Our forecast is to deliver benefits of between 70 and 80 million dollars by the end of this financial year.

At the same time, we have continued to strengthen our contract profile, locking in volumes through the down cycle for better certainty.

Last year, in response to a continued oversupply of ammonium nitrate in Australia, we rationalised our supply from our Yarwun operation in Queensland to effectively balance the Australian east coast supply.

The re-establishment of our Minova ground support business as a separate entity with its reinvigorated brand is enabling the turnaround of that business. We are embedding the turnaround strategy and simultaneously examining markets that could facilitate Minova's growth.

Around this time last calendar year we realigned the balance sheet to more accurately reflect the market conditions. This has enabled us to set clear performance metrics for each business in each region, based on a realistic understanding of the business.

### Back to basics

Our starting point for growth is to go back to basics. This sounds easy, but is actually the most difficult part of running a large, complex organisation.

We turned our attention to a stringent and disciplined approach to capital management. Now, more than ever before, we have to ensure that every dollar invested in the business delivers a satisfactory return. For our people, this heralded the reintroduction of discipline and rigour as baseline expectations throughout Orica.

We implemented a Capital and Investment Management framework, governed by a formalised Investment Committee with Terms of Reference and Standards.

Capex is now categorised as either Growth or Sustenance. Growth covers major growth, contractual growth and growth improvement. Each of these growth sub categories will need to meet set financial metrics including NPV and RONA.

Any capex will, firstly, address critical business risks and regulatory requirements; and secondly, focus on growth projects that generate higher returns.

With this in place, we find we are making better decisions and investing in the right areas of the business. Continued investment in the business is critical always, but these disciplines will help ensure that we invest wisely, regardless of where we are in the cycle.

#### Good costs versus bad costs

In the face of a downturn, the normal instinct is to attack costs, which generally inflate during the 'good' times. Usually, this type of cost cutting is achieved through mandated cost reduction targets for expediency.

Sometimes this is necessary, particularly if a 'cost shock' needs to be felt throughout the organisation to help instil a sense of urgency. The challenge, though, is that this approach doesn't discriminate between 'good' and 'bad' costs, and a good management team needs to be able to distinguish 'bad' costs from 'good'. Good costs are those that bring net benefits to the business. Bad costs are the inefficiencies in the business that if they are reduced will increase value.

Unfortunately, because removing bad costs often means addressing poor practices, systems or processes, these are often the last costs to be addressed. While good costs tend to be simpler to remove, doing so destroys value for the company. An example at Orica is when we closed the specialised Minova sales division. This significantly affected our ability to compete in the profitable 'non-mining' natural market for Minova, and while we benefitted from the cost reduction in the short-term, it actually destroyed value. And trust me, rebuilding value is harder than maintaining it.

Identifying 'bad' costs can be challenging. Without the right level of transparency, these costs can lurk in an organisation – a cancer that quietly chips away at the bottom line. We believe that the work we are doing in developing and embedding our new operating model has helped us to identify, and remove these costs.

#### Optimising our global manufacturing network

We have also turned our attention to defining our ideal long-term supply network for our initiating systems manufacturing operations. Orica has a highly geographically dispersed manufacturing footprint, which we need to leverage more effectively for the benefit of our customers and Orica,



while not compromising on the elements that are most important to our customers - safety, reliability and quality.

We have embarked on a project that will utilise our highly automated plants, like those in Gyttorp (Sweden) and Brownsburg (Canada), to produce a high quality product, consistently and efficiently. Given a critical factor for our customers is supply reliability, we are also standardising products where possible, and obtaining the required certifications to supply in all jurisdictions that our customers operate in from all the manufacturing locations in our vast global network. This provides customers with assurance of a consistently high quality, regardless of its manufacturing origin. As the products become more standard, they also benefit from even better security of supply as we will be able to ship our products from any number of manufacturing plants, all over the world, to meet their needs.

Where it makes sense, we will also continue to seek opportunities to partner with external parties to leverage others' capabilities and better serve our customers.

Underpinning this is the new operating model we launched last year, which brings greater visibility to every part of the organisation through common processes, systems and data, which will allow us to unlock the value of our unrivalled manufacturing network. It also supports our drive towards becoming a truly customer-focused organisation.

#### Transforming into a customer-centric organisation

Many organisations talk about being customer-focused, but in reality truly customer-centric organisations are hard to find. However, as a services company, we know that our success depends on our ability to transition to an organisation whose customers *believe and acknowledge* that Orica deeply understands their needs and is therefore critical to their operations.

We designed a new operating model with our customers at the centre. This then defined how we are structured around the world, to improve our responsiveness to customers. The result is a model where the parameters for performance are set at the Group level, while the four regional management teams have accountability for end-to-end customer service delivery, and on-the-ground operational and financial performance.

We firmly believe this will allow us to provide the same, consistently high quality of products and services to customers everywhere. The same Orica experience around the world.

Supporting this will be a single, standard SAP system that drives common processes and data. This will deliver the required visibility of performance across our landscape.

This delivers value on a number of fronts. For example, in targeting 'bad' costs, the visibility that the operating model delivers provides clarity on the inefficiencies to target. As the operating model defines accountabilities of each and every role, we can benchmark against best in class and understand where the opportunities to remove 'bad costs' exist.

This approach ensures that we are feeding the business where we need to and becoming leaner in the areas that we can.

When you consider our global footprint, this visibility of performance translates into an invaluable source of intelligence for us. We have people in more locations than anyone else – some 450 mine sites across every type of market and operation. We undertake around 1,500 blasts around the world, every day. This means we have an expansive ‘big data’ collection and knowledge base that can be fully leveraged to link customers’ sites and regions and enable the very best in knowledge transfer.

We see this as a key differentiator for us and continue to leverage it further by investing around three times more than our competitors in R&D. We consider this investment necessary and can demonstrate how this leads to improved productivity for our customers through advanced blasting services, data recording, management and analysis for optimal productive blasting results.

So all the actions we are taking deliver the strategies, frameworks, systems and processes for optimal results. In the end, however, we understand that all this is wasted without the right people and culture to support these. In the end, it will be our people that make the difference to our customers and to our business performance, and this continues to be a core focus for me and my leadership team.

#### Our people and culture

Initially, the focus was getting the right people in the right roles to support our new operating model. In a little over 12 months, we refreshed our senior leadership team. In fact, around 60% of our senior leadership team is new, either to the organisation or to their roles. Most importantly, we have empowered the senior leaders to run their functions and businesses. We provided clarity on what we need to achieve, but then trusted them to be the professionals that they are.

I truly believe that the culture of an organisation can make the difference in whether that company reaches its potential. Therefore culture is a priority for me and my leadership team. We want to build an organisational culture that is a magnet for the best people and the best ideas, and one that reflects the appropriate values and behaviours in our interactions with each other, and with our customers. After all, we have publicly committed to partnering with our customers. This requires a singular and specific mindset.

#### Re-setting our customer relationships

To that end, understanding our customers and their business objective is absolutely critical. This means changing from a sales target mindset to one that favours the quality of the relationship. It’s about moving away from chasing short term revenue targets that may damage long term customer relationships. In other words, we have to recognise that in some instances our customers don’t want the ‘bells and whistles’ or technologically advanced suite of products. Instead, they want a simple, basic, reliable product. They want a product that conforms to the highest degree of safety and of a consistent high quality. It is unsustainable to think we can impose upon them a product or service they don’t want or necessarily need.

Chasing short term financial gains by upselling to an unwilling customer is self-defeating in the long run. We have pledged to understand our customers and sell what adds the most value *to them*. We are also developing technologies, like our Field Information Systems, which will allow us to use actual data, to factually demonstrate how we add value.



For all of our customers we strive to provide a safe, reliable, high quality product that is supported by efficient service. For some customers, it might mean leveraging the investments we make in technologically advanced blasting products, to deliver even greater value. Within the industry, it is a well-known fact that we invest far more in research and development than our competitors. The onus is on us to be transparent and work collaboratively to demonstrate how we can develop resourceful solutions that help companies identify and realise opportunities to increase productivity.

We must always honour our commitments to our customers and keep their goals front and centre. When we do this consistently, across geographies, products and services, we can say we have truly become a customer-centric organisation.

### Summary

So, in summary, the actions that we are taking today in controlling the challenges that we face will see us emerge stronger through this down cycle and be in a far better position to take advantages of the opportunities when growth returns. Over our more than 140 years, we have worked hard to ensure that as an organisation, we adapt to changing circumstances and shape our destiny, and that won't change regardless of where the cycle takes us.

Yes, the market presents as challenging now and in the short to medium term, but despite that there seems to be some stabilisation in the mining world. We see our customers certainly getting on with the job of producing, despite the cyclical downturn. Just to be clear: I am certainly not calling the end of the downturn. We are still operating in fragile times.

But we are confident that we are focusing on the right things for both the downtimes and the up-cycle, when it comes.

We are continuing to control all the elements we can. We are transforming Orica into a leaner, more efficient organisation. Efficiencies are being embedded in the business to counteract the cyclical declines in volumes and prices that our industry has experienced.

We have worked hard to ensure that as an organisation, we adapt to changing circumstances and shape our destiny over the years.

Moreover, we are actively building a culture that supports our people, and that ensures that we work collaboratively with each other and with our customers, to create recognised value for us and them. We are deeply committed to our customers being at the forefront of everything we do, while understanding our value to them is in the assurance of consistently safe, reliable and quality products and services.

Thank you.