

# The Australian

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## Chinese buyers are keen to grab mineral sands

- by: Paul Garvey
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Drilling at Diatreme Resources Cyclone prospect in the Eucla Basin.

**TONY Fawdon didn't have to do much to get a good grip on China's current interest in mineral sands generally and zircon in particular.**

While standing in the lobby outside last week's TZMI Congress in Hong Kong waiting to meet The Australian, the Diatreme Resources executive chairman had representatives from three separate Chinese companies approach him to ask about securing offtake from Diatreme's early stage Cyclone mineral sands project in Western Australia's Eucla Basin.

That's despite the fact Diatreme is still a \$25 million minnow with a lot of work to do before it can get Cyclone into production, which Fawdon hopes will take place by 2014.

The level of interest being shown by customers towards less advanced players like Diatreme is indicative of the eagerness being shown by Chinese buyers of zircon and other mineral sands.

The prevailing mood over the two-day TZMI forum, which ranks as the key annual get-together for all participants in the mineral sands business, was an air of quiet self-confidence among miners and a faint whiff of panic among buyers who are increasingly concerned over supply.

There was also a distinct hint of opportunism from the much stronger turnout from investors and fund managers at this year's event, eager to get a piece of what has been one of the best performed pockets of the resources sector in the past year.

The continued strength of demand from China for zircon and the other mineral sands, coupled with only a few significant sources of new supply, has helped make Perth-based Iluka Resources one of the best performed stocks on the ASX.

It's also driven ASX-listed Mineral Deposits and Base Resources to pursue big new developments on either side of Africa, and left Diatreme weighing up Chinese deals that could force the market into a re-rating of its stock.

For all the uncertainty that has gripped equity markets this year, mineral sands remain in a sweet spot. Industry consultant TZMI forecasts demand to significantly eclipse supply of zircon in the coming years, explaining why buyers were so eager to talk offtake deals at this year's event.

The industry is not immune to the uncertainty that has gripped markets in recent years, but the fundamentals in the zircon market appear sounder than other parts of the mining industry.

The major end use for zircon is in ceramics and tiles.

Iluka chief executive David Robb says the regions with a cultural predisposition towards tiles and ceramics, such as Asia and the Middle East, are not those regions where countries are buckling under the weight of government debt and mismanagement.

Another reason for optimism among the mineral sands miners is that rising commodity prices haven't hurt the profitability of the customers buying them.

Robb says Iluka's customers are becoming more profitable even as they pay more for their feedstock. The products sold by Iluka represent only a small portion of the cost of the end product, meaning big increases in mineral sands prices have been easily passed on from Iluka's customers to consumers.

The improved market dynamics have helped Iluka shares increase from a low of \$2.69 in mid-2009 to \$17.52 on Friday, with the company now boasting a market capitalisation of about \$7.3 billion.

Merrill Lynch forecasts Iluka to post a net profit before one-offs of \$535m this year and more than \$1bn next year, compared with the \$84m loss in 2009. Robb and his fellow directors are weighing up just what Iluka does with that cash, but is giving away little as to what its windfall will mean in terms of dividends or acquisitions.

"It is important to us that this is not a flash in the pan, that this is a sustained, high-returns business," Robb says.

"We've got a long way to go before we can look back on a long period of achievement, and I don't think we would be so arrogant as to claim success based on only 12 to 18 months."

Much of the TZMI conference focused on the new sources of supply being lined up, but Robb believes much of the new capacity will only cover the growth in demand from China alone, not other growing markets such as Indonesia and India.

Jean-Francois Turgeon, managing director of Rio Tinto's iron and titanium division, adds his voice to those flagging a healthy outlook for the sector.

Turgeon says central and western China continue to boom, contributing to a forecast doubling in demand for Rio's mineral sands over the next 15 years.

"There's been little new capacity investment over the past decade," he says. "Major ore bodies are nearing depletion, and bringing new ore bodies on line will not happen overnight."

Rio used the conference to flag a major -- if long-dated -- overhaul of its international mineral sands operations, with Turgeon outlining Project TiO4.

The project involves developing two new mineral sands discoveries in Mozambique, improving efficiencies in Rio's Madagascar operation, rejuvenating the ageing Richards Bay mine in South Africa and finding a way to

increase volumes at its Canadian mines. It has already committed \$US800m earlier this year to extending the life of its Canadian operations until 2050.

There is very little detail about how much the program will cost or what sort of production increase it will lead to, but Turgeon says the expansion will rank as significant "even in a Rio Tinto sense".

Despite all the talk about new sources of supply, no one is forecasting a return to oversupply soon.

Goldman Sachs resources strategist Malcolm Southwood notes that China -- which is driving demand growth -- has very few domestic sources of mineral sands.

"The commodities you want to be investing in are the ones that China struggles to supply for itself," he says.

And there seems little chance of China finding makeshift solutions to its shortages, as it has by mining low-grade iron ore and importing poor-quality nickel ore.

"China always has the capacity to surprise us when it comes to the supply of raw materials," Southwood says.

"But geologically, it seems there's little likelihood that China will become more significant in zircon production and ilmenite production, certainly not in high-grade rutile production," Southwood says.

Fawdon, meanwhile, won't be giving away the offtake rights being sought by any of those Chinese firms soon, unless they provide cash to help in the project's development. The mineral sands market firmly seems to be favouring the miners, and Fawdon is determined to exploit that situation.

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