

Mining



DIFFICULT DECISIONS

By Martin Irving

As the world tries to adjust to the financial slowdown and the reality of global recession, companies around the world are slowing down, postponing projects, reducing costs and tightening their belts. The diamond industry is no different.

At the rough diamond production end of the pipeline, producers are cutting back. The diamond pipeline is slowly drying up as majors such as De Beers and Alrosa reduce production. Smaller players such as Rockwell Diamonds, DiamondEx and Petra Diamonds are also reducing production or suspending operations. Over the coming year, the diamond producers will monitor the economic situation, the demand for diamonds, and most importantly the price of rough, and will adjust production upwards or downwards as required. Within limits, the supply of rough diamonds from the producers can be adjusted downwards and then back upwards again relatively quickly. The upper limit is of

course the production capacity of the existing mining operations. However, some mining operations will be using this “downtime” to make some necessary maintenance and operational changes to increase production capacity. So, as the economy turns around, and demand improves, these companies will then be able to take advantage of the return to good times with more efficient and productive mining operations.

Downstream, the dealers and wholesalers are working to move the inventory they have. With the reduction of the incoming product, their focus will be on reducing inventory, paying down debt and maintaining positive cash flow. A focus on debt reduction will certainly reduce pressure and help reduce the worry lines on the foreheads of the industry bankers. These businesses can also adjust their levels of activity downwards and then upwards again, as the business and the economy regain strength in the

coming year. As with the mining sector, increased efficiencies required during these tough times will also provide benefits in the good times.

Further upstream, the diamond exploration sector has been significantly impacted by the current economic situation. Junior mining companies rely on equity financing through the stock markets to obtain the necessary capital to undertake exploration programs. It is their life blood. Current record-low share prices and the non-existent demand from investors have led most junior companies to cut staff, reduce expenditures and focus on key projects. There are now geologists, who were in huge demand last year, looking for work. Less exploration work will be done, fewer samples collected, less drilling, fewer results. Companies in this sector are reducing activity and waiting for better times.

However, once the economy picks up again, and things begin to improve, it is not easy to restart the exploration process. It takes time for exploration companies to gear back up again and move projects forward. As we have seen over the past 15 years, there has been a lack of new diamond discoveries, and even just a year ago, there were questions about where the diamonds would come from to feed the anticipated future growth in demand from China and India. While the global economic situation has substantially changed the industry's current situation, the future anticipated growth in demand is still potentially there. However, now, instead of being an issue for next year, it may be an issue for the industry in 2013 and 2014.

While the tight economic circumstances will prevent numerous exploration projects from advancing significantly over the next six to 12 months, the Shore Gold project in central Saskatchewan, Canada, should continue to advance. The Star kimberlite project (100 percent owned by Shore Gold) and the adjacent Orion project (owned 60 percent by Shore Gold and 40 percent by Newmont Mining) have begun the permitting process. Shore Gold submitted a project proposal to the Saskatchewan Ministry of Environment in November 2008. While exploration work will continue, focusing on Orion, much of the effort over the next year will be on moving the project through the regulatory process.

The environmental assessment process will be led by the government of Saskatchewan. Based on the Project Proposal, the Ministry of the Environment, in consultation with other Saskatchewan government ministries and agencies, and with federal government

departments, will develop Project Guidelines. After some public review, the guidelines will be finalized, perhaps by February 2009. Based on the issues and concerns identified in the guidelines, Shore Gold will develop their Environmental Assessment Project Description. The entire review and approval process could be completed by the end of 2009.

The other critical issue for Shore Gold is financing. The mine will require approximately \$1 billion to construct. It is not realistic to believe that Shore Gold will obtain this funding through either the equity markets or debt financing. It is more likely that a major mining company with available cash and financing will be brought in, as a partner. Of course, given the low level of Shore Gold's share price (around \$0.30), the market capitalization is about \$60 million, the company could just be bought lock, stock and exploration project.

As a final comment, it is during these difficult times that industry leaders need to step up and help provide confidence in their industry and in the future. If the industry leaders do not have confidence in the future, then who will? This is why I was disappointed to hear that the GIA has cancelled the Gemological Research Conference scheduled for August 2009. Given the economic situation, I can certainly understand that adjustments to the program, size and scale of the Conference would be in order. After all, money is tighter, the future less certain and so "value" for the attendees of a conference or event is of even greater importance.

Research is an important aspect for the industry. Undertaking, supporting and promoting research has been a strong part of the GIA's role as an industry leader. I believe the GIA missed an opportunity to make a strong statement of its belief in the future of the industry. The conference could have been adjusted to be less of a celebration of the industry, as some of the past events have been, and focus more on how research is providing some answers to the issues, economic as well as others, facing the industry, and explore ways that all involved can work together and grow the industry even in these difficult economic times. ■



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