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Committee Secretary
Senate Economics Committee
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Inquiry into foreign investment by state-owned entities

I submitted my concerns about the Rio/Chinalco deal to the committee on 24 April, and since that time have seen press comments on the price Chinalco is proposing to pay for Rio assets. The Financial Review on 11 May reported that the British institutional investors in Rio are unconcerned about the sale of Rio assets "as they are being made at greater than the assets net present value".

I ask the committee to examine this proposition in the context of Australia's national interest.

The agreement provides Chinalco with direct equity participation in Rio's Australian aluminium assets comprising, the Yarwun refinery (50%), the Weipa bauxite deposit (30%), and the Boyne island smelter (29.4%), with the attached power station (20.6%). The agreement also includes direct equity in Australian iron ore assets (15%).

My understanding of NPV is as a measure of the financial viability of investing in a new project, or in the expansion of an existing project. Certain assumptions are required with respect to the price that will be obtained for the product, the cost of the project, and analysis is based on a discount rate that reflects the cost of capital, and the risk of the outcome being achieved over time.

Adopting a discount rate within any normally accepted range will render the present value of cash flows beyond about 30 years negligible.

For natural resource assets such as Weipa bauxite and Pilbara iron ore which are so large that by any reasonable extraction rate assumption will last well into the next century, I don't consider that the NPV analysis of the presently configured asset accounts fairly for Australia's interest in that portion of the resource remaining in 30 years from now. The NPV analysis probably does not even include the value of expansion options that may occur within the next 30 years.

It could be that the value of very long life and irreplaceable assets cannot be fairly valued as the future is too uncertain. In that case, I contend that, in the national interest, the asset is not for sale. Any divestment should be limited to a lease arrangement expiring at the end of the valuation period. And include payment terms for expanded extraction that takes place during the period.

A retrospective analysis of the financial performance of the Broken Hill silver, lead, zinc operations would be instructive to show that limitation of an NPV based sale of resources. If 15%, or 30% of Broken Hill had been sold in 1930 (45 years from start up, the same time Hamersley has been in operation) based on the NPV of the operations in 1930, what would have been given away in Australian value from 1960 to say, 1980 when production started to decline? And what value would not have been captured from expansions during the period from 1930 to 1960?

Developed and operating long life resource deposits should not be sold to anyone, sovereign or otherwise.

Thank you.

Peter Matters