



Natural Resources

Balancing cost reduction with risks

BDO's 2015 Executive Mining ERM Round Table

October 2015

Volatile pricing, currency valuation and economic uncertainty pose both apparent and hidden risks that affect how mining companies do business. Mining companies are under increasing pressure to trim costs, and take bigger risks to mitigate the erosion of their profit margins. These were the key trends we explored with mining executives who attended BDO's fourth annual Mining Executive Enterprise Risk Management (ERM) Round Table in Toronto in the summer of 2015. The round table consisted of operating mining companies headquartered in Canada, and whose operations spread across the globe.

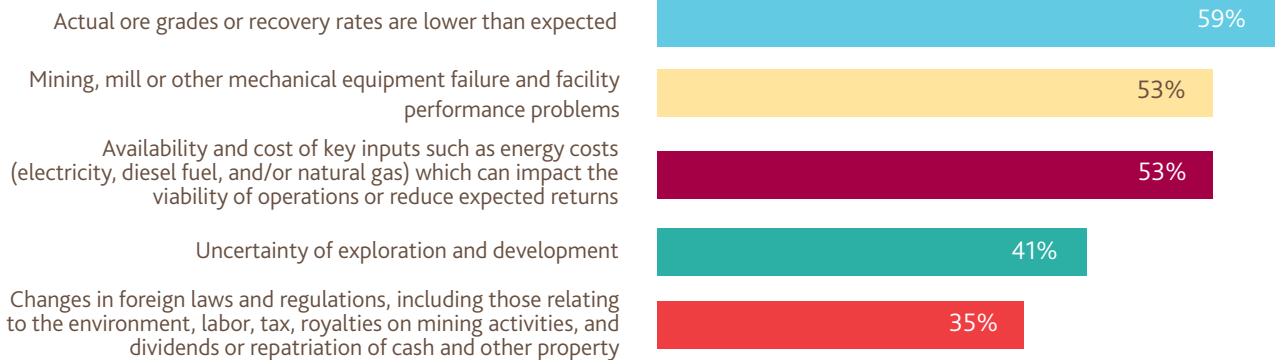


We asked participants a fundamental question: How do mining companies reduce the cost of operation without taking risks that could cost them the company?

The risks, both operational and financial, are significant. There are also political and legal risks that challenge companies doing business in certain jurisdictions.

Prior to the round table, BDO requested that invited participants complete a survey to better understand the make-up of their ERM programs. BDO used the survey results to help facilitate discussions and provide insight into how other participants were managing their ERM programs.

Top operational risks



Top financial risks



Commodity prices



Tightening of credit markets



Changes in interest rates



Increasing cost of insurance



Increasing liabilities for hazards that may be uninsurable

Many risks are within an organization's control. Round table participants, however, spent a significant portion of the session discussing a number of risks that were, in many ways, beyond their control. From an operational perspective, the risks discussed included political instability, changes in foreign laws and regulations, and unexpected geological problems, including natural disasters. In terms of financial risks, the price of gold, access to capital and currency fluctuation were top of mind.

Cost Reduction Amid Volatility Is a Balancing Act

Round table participants agreed that to remain competitive in a highly volatile environment, they need to find the right balance between cost-cutting and risk management.

Mining companies need to identify the risks that matter and their impact not only to the organization, but also to corporate objectives. In our survey, only 21% of organizations were fully aware of the key risks across the enterprise, their impact on the organization and their impact on corporate objectives. At the other end of the spectrum, 14% had an understanding of the most critical risks but did not formally assess the actions required to manage them, nor did they have a plan to address them.

With all of the key risks identified across the enterprise, as well as their impact on the organization and corporate objectives, participants agreed that they could then make informed decisions that would enable them to both manage the risks that truly matter and reduce costs.

Key risks

21%

Percentage of respondents that are fully aware of key risks across the enterprise, their impact to the organization and their impact on corporate objectives.

14%

Percentage of respondents that have an understanding of the most critical risks but do not formally assess the actions required to manage them.

Three Steps to Risk-Managed Cost Reduction

There are three fundamental steps mining organizations can take to reduce operational costs without taking risks that could undermine their survival:

- 1. Know your organization's risk appetite.** Understand the maximum cost reductions which can be made while still re-maining competitive and identify the associated risks with such reductions. Knowing how much risk you are willing to accept will enable you to make smart decisions that balance the risks and the costs.
- 2. Develop meaningful mitigation strategies.** For actions that reduce costs but may pose a medium to high risk to the organization, develop a direct and responsive mitigation strategy. Having a mitigation plan when implementing a cost reduction strategy, allows executives to have an appropriate plan of action in place to respond quickly when unforeseen circumstances arise.
- 3. Add or maximize the value of internal assessments.** Mining companies with existing internal audit or assessment functions, either in-house or outsourced, should seek to maximize the value they can provide. Mining companies without such a function may wish to consider adding it. Internal assessments can help to identify and implement risk mitigation strategies, as well as implement controls to measure the success of these strategies. Internal Auditors can also serve as the eyes and ears of the organization, alerting management to key risks as they arise, and monitoring third party vendors for appropriate practices.

The Right Balance Leads to Opportunity and Profitability

For round table participants the primary objective is to find a balance between cost reduction and risk management that leads to profitability. Mining companies that achieve this balance will increase their opportunities to acquire slower-moving companies, or position themselves to be acquired for maximum value. Those that are unable to find the right balance may face the unwanted options of being acquired at a reduced value, or ceasing to exist.

BDO Canada LLP's Advisory Services Practice ("BDO") hosts yearly roundtables for mining company executives that focus on the emerging issue of enterprise risk management. In the summer of 2015, select member of BDO's team hosted its fourth annual Mining Executive ERM Round Table for 25 mining company executives in Toronto. With topics focusing on the latest trends around industry-specific operational and financial risks, the round table provided participants with a forum to share their issues, ideas and leading practices to manage and mitigate our mining clients' most pressing enterprise risks. For more information about attending a future BDO roundtable event or to obtain a PDF copy of this article, please contact Carlo Mariglia or Stefan Piech.



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