

# Bloomberg

---

## Rio Tinto Cuts Debt Costs As Yields Drop to Record Low: Australia Credit

By Sarah McDonald and James Paton - Sep 15, 2011

[Rio Tinto](#) Group, the world's second-biggest mining company, took advantage of near record-low yields to cut debt costs as company bond sales in the U.S. this month swell to \$40 billion while Australia's market stays shut.

Rio Tinto, with 45 percent of its \$89 billion of gross assets in Australia and [New Zealand](#), sold \$2 billion of notes due in 2016, 2021 and 2040 on Sept. 14 with coupons as low as 2.25 percent, according to data compiled by Bloomberg. U.S. industrial corporate notes yield an average 3.5 percent, or 2.4 percentage points less than Australian counterparts, Bank of America Merrill Lynch indexes show.

"The three big attractions of the U.S. market are size, tenor and pricing," said [Mark Mitchell](#), head of credit at Sydney-based Kapstream Capital, which manages A\$4.2 billion. "Companies such as Rio Tinto can generally issue longer-dated paper, in bigger size and at a tighter spread in the U.S. market as compared to Australia."

Rio Tinto will spend a further \$833 million expanding in the Pilbara region in Western Australia, it said yesterday, amid a flurry of mining investment that's forecast to reach A\$82.1 billion in the 12 months ending June 30 next year as demand for commodities from [China](#) and India stokes prices. The funding required for the expansion isn't swelling Australia's bond market, which hasn't seen an offering from a mining firm since 2004, Bloomberg data show.

### Westfield, SP AusNet

The proceeds of the sale will be used for general corporate purposes, Karen Halbert, a Melbourne-based spokeswoman for Rio, said by phone yesterday.

U.S. corporate bond sales have totaled \$41.6 billion in September while a A\$15 million (\$15.3 million) issue for IMB Ltd. was the only Australian offering by a borrower without government backing, Bloomberg data show. Investors are demanding 194 basis points of extra yield compared to [government bonds](#) to hold [U.S. dollar](#) industrial corporate securities, according to a Merrill Lynch index. The equivalent Australian spread is 230 basis points, the indexes show.

The largest non-financial corporate sale in Australia this year was Westfield Retail Trust's offering of A\$900 million of 7 percent October 2016 notes, while SP AusNet's 10-year securities had the longest tenor, Bloomberg data show.

### 'Cheap' Financing

Rio Tinto, based in [London](#) and rated A- by [Standard & Poor's](#), sold \$500 million of five-year, 2.25 percent notes that were priced to yield 148 basis points more than similar-maturity Treasuries and \$1.15 billion of 10-year, 3.75 percent debt that was priced with a 178 basis-point spread on Sept. 14. The mining company also issued \$350 million of 5.2 percent bonds due November 2040 at a spread of 178 basis points, Bloomberg data show.

“That’s a very cheap form of financing,” said Brad Newcombe, a director at FIIG Securities Ltd., [Australia](#)’s largest specialist fixed-income brokerage. “It’s a great deal for them, and it’s cheaper to hit the U.S. markets than Australia.”

A U.S. sovereign debt rally has helped push yields on investment-grade corporate bonds to an average 3.75 percent, compared with an all-time low of 3.45 percent on Aug. 4, according to the Bank of America Merrill Lynch U.S. Corporate Master index.

The weighted average coupon on Rio Tinto’s outstanding bonds is 5.8 percent, according to data compiled by Bloomberg. Investors have poured more than \$32 billion into U.S. bond funds this year as of Sept. 7, according to EPFR Global, a Cambridge, Massachusetts-based research company.

### [Iron Ore](#) Production

Rio Tinto will invest \$833 million in power and fuel supply projects to help increase iron ore production capacity in [Western Australia](#) by 50 percent in the five years through 2015, according to a statement yesterday. Rio said it will install two gas-fired turbines as part of a new power station near the West Angelas mine site and build a turbine at the Yurralyi Maya power station near Dampier.

The company aims to expand its annual iron ore production capacity in the Pilbara region to 283 million metric tons in 2013 from 225 million tons, it said. Rio also plans to boost capacity to 333 million tons a year in 2015.

Rio Tinto’s bond sale is taking advantage of the low rates “currently on offer,” said Colin Tan, credit analyst at Deutsche Bank AG in Sydney. “The strong demand for the issue partly reflects the pricing but also suggests there’s cash on the sidelines waiting to be invested in investment-grade corporates with strong balance sheets.”

### [Europe](#)’s Debt Crisis

[Reserve Bank](#) of Australia Governor [Glenn Stevens](#) raised [interest rates](#) seven times beginning in October 2009, to 4.75 percent in November 2010 to help control inflation.

Since then, bond yields have plummeted as Europe’s debt crisis caused turmoil in global markets while at home, [consumer confidence](#) dropped and unemployment rose.

Australia’s benchmark 10-year yield rose 6 basis points to 4.15 percent yesterday, and has fallen from 5.55 percent since the start of the year. The notes yield 218 basis points more than similar-maturity Treasuries.

Bond investors are estimating Australian consumer prices will rise at an annual 2.48 percent pace over the coming five years, according to the gap between indexed government debt and bonds that aren't linked to inflation.

Rio Tinto, facing rising wages, higher energy bills and currency gains in Australia and [Canada](#), said last month that underlying first-half profit rose 35 percent to \$7.8 billion, below the \$8.3 billion mean estimate of nine analysts compiled by Bloomberg.

## **Aussie Dollar**

Australia's dollar has surged 9.2 percent against the greenback in the past year, and bought \$1.0248 as of 6:17 p.m. in Sydney yesterday.

Concern the global economic recovery is stalling has boosted the perceived risk of Australian corporate bonds.

The Markit iTraxx Australia index of credit-default swaps rose to 194.8 basis points on Sept. 12, the most since July 2009, according to data from CMA, which is owned by CME Group Inc. and compiles prices quoted by dealers in the privately negotiated market.

The gauge surged to 443.3 in March 2009 amid the credit freeze following the collapse of Lehman Brothers Holdings Inc. The index was at 185 basis points on Sept. 14, according to CMA.

Contracts on Rio Tinto have surged 55 basis points this quarter to 154.1 on Sept. 14, according to CMA. A gauge of default-swaps on 29 miners rose 62 basis points to 209.5.

## **'Limited Interest'**

Australia's second-quarter mineral and energy commodity export earnings rose 12 percent from the previous three months, led by surging demand for coal, the nation's commodity forecaster said yesterday. For the year to June 30, resources and energy exports surged 27 percent to a record A\$175 billion, the [Bureau of Resources and Energy Economics](#) said.

China, the world's biggest buyer of iron ore, boosted purchases 8.3 percent in August to the highest in five months as demand and prices rose.

Rio Tinto has never sold bonds in the Australian currency, according to data compiled by Bloomberg. [BHP Billiton Ltd. \(BHP\)](#) last issued in Australian dollars in 2001, the data show. Mitsubishi Development Pty., a unit of Mitsubishi Corp., sold A\$150 million of three-year notes in August 2004 in the most recent sale by a mining company in the Australian debt markets, according to Bloomberg data.

"It would be good to see more issuers here and Rio would provide a diversifying exposure," said [John Sorrell](#), head of credit at Tyndall Investment Management Australia Ltd. in Sydney, which manages about A\$14 billion of fixed-income assets. "While I think they would find healthy appetite from investors, they have shown limited interest to use it."

To contact the reporter on this story: Sarah McDonald in Sydney at [smcdonald23@bloomberg.net](mailto:smcdonald23@bloomberg.net); James Paton in Sydney [jpaton4@bloomberg.net](mailto:jpaton4@bloomberg.net).

To contact the editor responsible for this story: Shelley Smith at [ssmith118@bloomberg.net](mailto:ssmith118@bloomberg.net); Amit Prakash at [aprakash1@bloomberg.net](mailto:aprakash1@bloomberg.net).

---

©2011 BLOOMBERG L.P. ALL RIGHTS RESERVED.