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Resource Boom Spurs Big Deal

Glencore, Xstrata in Talks to Form $80 Billion Mining Giant

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In a world ravenous for natural resources, two of the world's most powerful raw-materials companies are in talks to combine into an $80 billion colossus that would play a powerful role in an industry that supplies auto makers, chocolatiers and power companies.

Glencore International AG and Xstrata PLC, both Swiss companies, said Thursday they are in talks for an all-share merger of equals. Though they cautioned that the talks may not lead to a deal, people familiar with the matter said the goal is to announce a deal by the time Xstrata reports its annual results Tuesday. The current plan calls for Xstrata Chief Executive Mick Davis to serve as CEO of the combined entity, while current Glencore CEO Ivan Glasenberg would be his deputy.

Merger talks between Xstrata and Glencore are underway but their respective bosses will have to figure out what the deal means for each company. Andrea Hotter and Dana Cimilluca have been following the story.

The combination would be unique in the industry, melding a big miner with a trader of raw materials. Though the two companies aren't household names in the U.S., they are significant players in supply chains that make products for untold numbers of consumers around the world.

The mining sector, which has been noticeably quiet compared to its prerecession mega mergers, may be poised for another round of deals. Part of the reason remains strong demand for natural resources in rapidly growing economies like China. But mining companies are also seeking heft to secure financing for capital-intensive mining operations. It costs $800,000 to buy the claw on a mining excavator and $1 billion to build a rail line in Mozambique.

Xstrata PLC and Glencore International AG are in talks for a merger that would create a giant mining company and dramatically alter the industry's landscape. Dow Jones's Andrea Hotter has been examining the proposed deal.

Roughly 70% of Xstrata's mining assets are in two commodities - coal and copper - that are fueling skyscrapers, cities and automobile production.

The proposed tie-up follows an unruly year for commodity prices, which started high and ended low. Copper was hammered by diminished hopes for China's building boom. But it is back up again. While China's growth rate is slowing, its economy is still expected by Western analysts to grow more than 8% this year and double in size every 11 years.

Copper prices have risen to more than $8,000 per ton, despite the current economic clouds, from less than $2,000 in 2000. And the new combined entity would be perfectly poised to cash in on this copper boom, with only Chile's national company Codelco producing more.

The consolidation game is already on. Last month, rival Rio Tinto PLC ramped up its stake in Canadian miner Ivanhoe to 51%. Ivanhoe's major project is the Oyu Tolgoi copper mine in Mongolia, expected to start producing and shipping to China in 2013.

A Glencore-Xstrata deal would give the new entity more leverage to acquire midsize players. Analysts say possible targets include Fortescue Metals Group, an Australian iron ore producer; Freeport-McMoRan Copper & Gold Inc., a U.S. copper and gold concern; or Anglo American Corp., a South African mining conglomerate.

While Xstrata is a large player in mining, Glencore owns a handful of mining assets and runs a lucrative trading operation that matches up buyers and sellers for everything from nickel to sugar and oil. Mr. Glasenberg, the Glencore CEO and the deal's principal proponent, has said the ability to run a bigger, more efficient and powerful trading operation by putting the two businesses together is a big motivation for the deal.

A merger still could be messy. Power-sharing structures in deals billed as mergers of equals are notoriously prone to failure. Messrs. Glasenberg and Davis, both South Africans, have known each other since school days, and Xstrata is already 34% owned by Glencore. But both men have strong personalities, and they have been known to clash in the past.

Also, regulators around the world could cast a wary eye toward the potential deal given the possibility that it could produce a company with considerable sway over key industrial commodities, creating ripple effects on everything from power and electrical wiring to cars and trucks - and at a time when the prices for many raw materials are high.

Glencore, already a behemoth, could now have even more leverage to push up prices. "It will be reviewed all over the world," said Dave Anderson, a partner in the Brussels office of law firm BLP LLP. "That said, these guys know each other, and have been talking for years, so they'll have assessed the antitrust issues already."

Mining companies Xstrata PLC and Glencore International AG explore are discussing a plan that would put Xstrata Chief Executive Mick Davis in charge of the combined entity, Dana Cimilluca reports on Markets Hub.

People close to the proposed deal played down antitrust concerns, arguing that the companies have different and complementary businesses. Still, antitrust regulators on both sides of the Atlantic have been flexing their muscles lately, most recently moving to block the proposed tie-up between Deutsche Börse AG and NYSE Euronext.

In a sign that the deal may win investor support, shares of Glencore and Xstrata rose on the news in London, with Glencore up 6.5% and Xstrata climbing 10.4%. Xstrata put out a brief statement confirming it had been approached by Glencore after the talks were reported by Bloomberg. The two companies declined to comment further. Sir John Bond, Xstrata's chairman and a seasoned British executive, is expected to take that role at the combined company, the people familiar with the matter said.

Glencore was founded in 1974 by Marc Rich. The former fugitive commodities trader, pardoned by President Bill Clinton in his last days in office, sold the business to his lieutenants in 1994. Mr. Glasenberg took over as CEO eight years later. He and his partners then built Glencore into one of the world's largest private companies, with 2010 sales of $145 billion, before taking it public last May. The IPO brought vast wealth to Glencore partners, including Mr. Glasenberg.

Previous deal talks, however, ran into opposition from Xstrata's Mr. Davis, who has been under pressure from Xstrata shareholders wary of a deal that short changes them and of joining a complex and opaque partnership. Glencore's IPO largely was meant to address such concerns.

Faced with big capital costs, a dearth of attractive deposits to pursue, and booming Asian demand for the world's natural resources, many top miners have scrambled in recent years to strike merger deals.

The steel sector provides an example of how powerful mining companies can squeeze their customers. The world's 10 largest steel companies hold a combined market share of around 28%, while their top three raw materials suppliers control roughly 35% of iron ore, the main ingredient in steel.

The world's largest steelmaker, ArcelorMittal, earned $2.6 billion in the first six months of 2011. In contrast, BHP Billiton, the world's most valuable miner, earned $13.1 billion during that same period.

The consolidation of other metals, like copper in the case of Glencore-Xstrata, could make life more difficult for building companies that need the finished materials for pipes, and for makers of heavy-duty cable wiring.

"We are moving toward a consolidation of the mining world," said Michael Locker, an analyst with New York-based Locker Associates. "A lot of metals, like iron ore, are already pretty well consolidated. Now we're going to see it for other metals, like copper."

Xstrata ranks as the world's fourth-biggest copper producer, churning out 907,000 metric tons in 2010, while Glencore is eighth, at 542,000 metric tons.

Combined, they leap into second place, ahead of Freeport, which at 1.44 million metric tons was behind only Codelco, at 1.76 million metric tons.

The deal would accelerate creeping momentum for deals in the mining sector. In 2011, the total deal value rose 43% to $162.4 billion, while the total number of deals fell 10% to 1,008.

Faced with huge capital costs, big miners are keen to combine to share equipment and labor costs.

Big miners want to get even bigger so they can buy smaller firms with good deposits and infrastructure. Smaller mining companies are increasingly vulnerable because of a lack of access to credit.