

**We invest in winners.** That means we invest in strong companies that create value for their shareholders with sustainable business models, solid balance sheets and high margins. We keep the risks low and invest when our position is fuelled by a positive event. We refer to that as the combination of value and event.

### Rio Tinto plc

The origins of the British-Australian mining group Rio Tinto are in the copper deposits near Minas de Riotinto in southern Spain, which were already known during the Bronze Age and that were later mined by the Phoenicians and Romans. In 1873, the year Rio Tinto was founded, the Rothschild family and other investors bought the money-losing government mines. Today, Rio Tinto extracts iron ore, copper, bauxite and diamonds, and is one of the largest multinational mining companies.

At this time, business could not be better. Free cash flows climbed to USD 9.4 billion in 2017. No wonder, one might think in view of rising commodity prices. This is the time to make profits, as losses will follow in the next crisis. It is correct that the mining industry experienced acquisition fever until the last financial crisis, and that it produced heavily until prices collapsed and exposed losses in the billions. In 2007, Rio Tinto took over Canadian aluminium group Alcan for USD 38 billion. Just a year later, a hostile takeover by BHP Billiton, which valued Rio Tinto at USD 170 billion, failed. After that, the share price lost more than 80%. It has recovered in the meantime. The market capitalisation is USD 100 billion. Rio Tinto is unlikely to let a similar destruction of capital happen again. After a tough restructuring process, Jean-Sébastien Jacques, a Frenchman with a British passport,

is now guarding the group's capital. One will not find goodwill and debt in the balance sheet. For Jacques, profitability is more important than size. Coal mines and other marginal segments were sold. Each project must meet the demanding yield targets and must be a fit for the new concept of rational capital allocation. This means that up to 60% of profits are distributed to shareholders annually through dividends and share buy-backs. At the same time, Rio Tinto possesses considerable earnings leverage. Production costs in the most important segment, iron ore, which was responsible for 70% of profits in the past financial year, are only USD 14 per tonne after the restructuring process. The current market price is USD 67. In addition, investments in mining automation and digitisation are also paying off. Thanks to increasing productivity, additional cash flows of USD 1.5 billion are supposed to be generated annually by 2021. Jacques is also open to big innovations. Together with Apple and Alcoa, Rio Tinto is working make the manufacture of aluminium more environmentally friendly. The new method is supposed to produce oxygen and replace all greenhouse gases that are currently produced by the traditional melting process. Exports expect that the process will be revolutionary for the industry and that it will lead to massive reductions in emissions of environmentally-damaging carbon dioxide. This is the kind of development we are happy to support.

Sincerely yours



J. Henrik Muhle



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