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Cat's Divesture And Exit Does Not Bode Well For The Underground Mining Industry (Part-1)

Investopedia explains," A divestiture is the partial or full disposal of a business unit through sale, exchange, closure, or bankruptcy. A divestiture most commonly results from a management decision to cease operating a business unit because it is not any longer part of a company's core competency". There is no particular difference between the technicalities of the terms exit and divesture. It is not uncommon to find a company exiting completely after divesting to another party at a particular time, only to buy it back at an opportune time. Investopedia also explains exit or exit strategy as "An exit strategy is a contingency plan that is executed by an investor, trader, venture capitalist, or business owner to liquidate a position in a financial asset or dispose of tangible business assets once predetermined criteria for either has been met or exceeded. An exit strategy may be executed to exit a non-performing investment or close an unprofitable business. In this case, the purpose of the exit strategy is to limit losses."

As recent as 27th/28th February, 2022, announcement of Caterpillar divesting or exiting underground mining is not particularly good news for the underground mining industry. Caterpillar has been making some major strategic moves of late to focus on its core surface mining and underground hard rock mining equipment products, technologies, and systems. This has included a licensing and IP agreement with India's Gainwell Technologies, first for Gainwell to manufacture surface highwall miners in India, then more recently extending these agreements to include underground medium and high seam continuous miners and other room and pillar products, including face haulers, roof support carriers, scoops/multi utility vehicles and feeder breakers. On February 23, a similar deal was announced with Simmons Equipment Co in Virginia, US, for low seam room and pillar lines. In addition, Caterpillar in 2020 had confirmed it was closing its Luenen, Germany underground coal longwall (and plow) mining equipment factory with production moved to Asia.

The insider industry news is that Caterpillar is set to effectively withdraw completely from underground coal and soft rock mining through the divestment

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of its longwall business to Germany's Hauhinco Maschinenfabrik GmbH & Co KG, based in Sprockhövel, North Rhine-Westphalia.

There is a history of cooperation between Hauhinco and Caterpillar – notably Hauhinco working with the Caterpillar facility in Luenen to design complete water hydraulic systems for Caterpillar underground longwall mining systems. Hauhinco, a company with over 111 years of history, has a focus in mining in designing customer-specific high pressure emulsion pump stations for roof supports in longwalls as well as water spray pump stations supplying the shearer water spray or the coal plow water spray and the cooling systems for the drive motors with the necessary pressure and volumetric flow rate.It has been known that Caterpillar has entered into a preliminary agreement with Hauhinco to divest the longwall product line. Subject to the negotiation of a final agreement, the deal is expected to be completed in Q3, 2022. Caterpillar and Hauhinco will work together to ensure a smooth transition to minimise any impacts to customers and dealers." On the reasoning behind the move, the company stated: "To stay focused on Caterpillar core products and services, the company has made the decision to exit the longwall product line." Caterpillar's remaining longwall business includes hydraulic roof supports, high-horsepower shearers, automated plow systems and armored face conveyors with intelligent drive technology controlled and supported by advanced longwall automation.

Another Development

Tazewell, Virginia-based Simmons Equipment Co. and Caterpillar have signed an exclusive Intellectual Property (IP) license agreement on Feb 24, 2022, which grants Simmons global rights to manufacture certain soft rock (coal) mining equipment formerly produced by Cat. The agreement expands on Simmons Equipment's existing portfolio of soft rock mining equipment and reflects a continued commitment to providing innovative solutions to the global mining market. The portfolio of equipment includes the CM210 Continuous Miner, CM220 Continuous Miner, Continuous Haulage Product Line, FH110 Battery Hauler, FB85 Feeder Breaker, FB140 Feeder Breaker, RB120 Roof Bolter and the complete battery Shield Hauler Product Line (SH620, SH630, SH650, and SH680). The agreement also grants Simmons Equipment nonexclusive rights to supply aftermarket spare parts and support existing Caterpillar room-and-pillar equipment.

The Issues Prompting Exits

Technology Companies have a keen eye on offering not just products, but technology driven services that can generate an ongoing revenue stream. Examples include technology that can optimize machine maintenance and consulting services related to a manufacturer's products. So unless, a manufacturer does not see defensible business in the service of equipment and spares, it would look other way. Rapidly changing technology and the opportunities presented by digitalization are expected to continue to drive divestment: 79% in the sector expect a rise in technology driven divestments, while 70% believe sector convergence will make them more likely to divest in the next year. Funds from divestment can be used to invest not only in the new technologies but in a workforce with skills to employ them effectively. Early opportunistic

Figure 1. Cat Longwall fleet.

Figure 2. Cat's hauler line.

deals still account for a third of all divestments in the sector. The following points drive a manufacturing company to exit or divest.

1. Manufacturing capacity issues
2. Cash flow and/or access to credit
3. Idle stuck capital
4. Excessive loan interest and servicing
5. Market structure and working business model
6. Size or competitiveness of target market
7. Process and equipment bottlenecks
8. Customer satisfaction practice unviable at the current scale
9. Work for product quality is not satisfied by return
10. Focusing on new product and business segment development
11. Supply chain issues
12. Depleting management talent and engagement

What Could Have Prompted Cat

A business exit strategy is an entrepreneur's strategic plan to sell his or her ownership in a company to investors or another company. An exit strategy gives a business owner a way to reduce or liquidate his stake in a business and, if the business is successful, make a substantial profit. If the business is not successful, an exit strategy (or "exit plan") enables the entrepreneur to limit losses. An exit strategy may also be used by an investor such as a venture capitalist in order to plan for a cash-out of an investment.

- A business exit strategy is a plan that a founder or owner of a business makes to sell their company, or share in a company, to other investors or other firms.
- Initial Public Offerings (IPOs), strategic acquisitions, and management buyouts are among the more common exit strategies an owner might pursue.
- If the business is making money, an exit strategy lets the owner of the business cut their stake or completely get out of the business while making a profit.
- If the business is struggling, implementing an exit strategy or "exit plan" can allow the entrepreneur to limit losses.

Stuck in the Middle

The 'middle' of a market is a place where you are not in a position to ask some high margin premium neither can survive on some low margin premium. It is considered bad if you are stuck in some important way. The inability to respond flexibly and appropriately to new competitive conditions is the grave threat. The 'middle' seems to be what every executive wants to avoid these days. There is ample research on business strategy that suggests the middle is to be avoided for fear of being stuck in it. The conventional view is to see the 'middle' as the problem.

Where Cat Could Have Seen it in the Middle

1. There are not many customers to buy its offerings at a price that suits it.
2. Neither, it can service the lower end customers.
3. The situation is not going to change soon.
4. It sees the situation is unsustainable for its business.

Firms that are stuck in the middle tend to have mediocre returns, and tend to fail during the periodic industry shakeouts. The general advice in the industry circle is, 'find what you are good at and stick to it,' which is often a sound advice. This advice can be however, contested. What is bad today can be good tomorrow-but a CEO tries to maximize the present as the board and the shareholders prod him or her to doing so. The middle may not be all that bad or that it may be entirely sensible for managers to test the middle for the sake of discovering possible new segments of demand in the future; but today business is restless to consider it.

(To be continued)

CEO and Corporate TM Cat's divesture and exit does not bode well for the underground mining industry (Part-2)

Hesitations to divest

Executives generally wait for one or more of the following six concerns to turn good before pursuing a divestiture: misperceptions of asset value, underestimating buyer interest, concerns about damage to the rest of the business, concerns about timing, fear of sunk costs, and emotional attachment to the asset (Mckinsey, 2020).

Business Exit Strategy and Liquidity

Selling ownership through a strategic acquisition, for example, can offer the greatest amount of liquidity in the

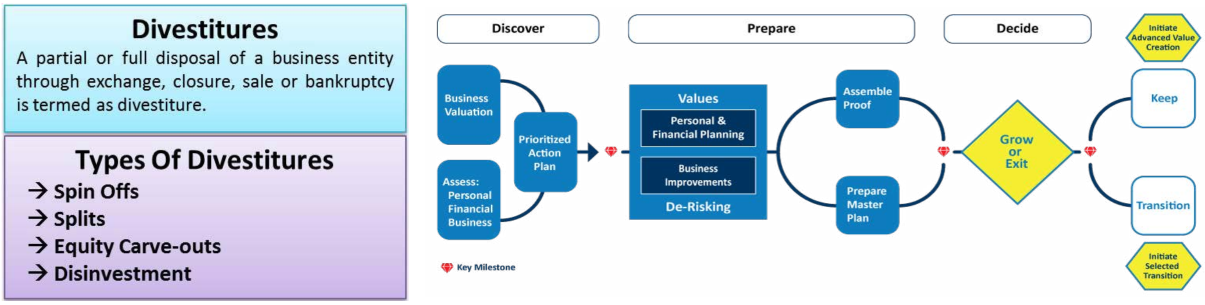

Figure 3. Divesture and exit strategy.

shortest time frame, depending on how the acquisition is structured. The appeal of a given exit strategy will depend on market conditions.

Fragmentation and Market Uncertainty

Sometimes, owners of successful businesses decide to cash out because of uncertainty about fragmentation (big orders becoming small, multiple agents, buyer side management change, etc.) and future market developments. If manufacturer were selling few big orders, large number of small orders will not interest it. Government policies can adversely affect a business. In each of these situations, it may make sense for the entrepreneur to pre-emptively plan and exit the business if it sees that the things are not irreversible at least in the short run.

Business Failure

If the manufacturer continues losing money after having tried a variety of approaches to stabilize the business, it may sometimes be best to call it quits. Quitting might be a wise decision if it finds no reversal of fortune in the operating years and still have no traction; customers still respond to your sales pitch with a blank stare.

Bankruptcy

Bankruptcy is another example of an exit strategy that is often considered in a liquidity crisis or other financial struggles for a company; however, it is usually less preferable and offers a less profitable outcome for business owners. Exit strategies can also be used to prepare for the end of a contract. It can be due to poor performance, changes in company strategy or hierarchy, or the end of an existing contract. Such strategies can be after achieving a

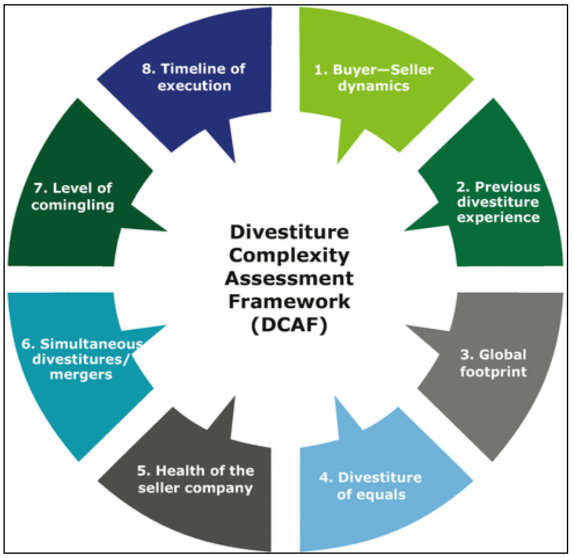

Figure 4. Divesture as a process.

pre-established goal or to mitigate loss, either way, taking their remaining value out of the company. Simultaneously, the operations of the business will slow down until it is too small to operate. Often, small business owners who want to reduce their workload slowly towards retirement will choose the gradual liquidation strategy.

Sale to a Business, the Open Market, or Through an IPO

A business sale to another organization requires unique positioning to make it an appealing acquisition to the other company. Corporations that are looking to acquire a new business segment will be looking for synergies between the brands or operations, a chance to reduce competition, or as a move to increase their market share. Selling to the open market is another exit strategy and is often used when a company is highly sought after, and the demand for it can drive prices up – higher than that of a sale to a business. Finally, an IPO (Initial Public Offering) can provide an exit for private company owners who are looking for large profits and want to see their business continue to grow in the future through equity financing.

Why Underground Mining Should Sit Up and Notice

First of all, it is not a good news for an industry to know that a major manufacturer is losing interest in it. The following are some of the reasons why the industry should get involved:

1. Is the industry's operating and acquisition models conductive for competitive business that the company is in? If not, what can be done about it.
2. A big manufacturing company uses leverages of various new and emerging technologies that the industry can learn from.
3. Underground mining will usher in new green and more efficient technologies; the manufacturer can be a good and mature technology partner.
4. Quality manpower and systems the manufacturer employs need cost of keeping them; are the industry giving those realizable values?
5. Industry tends to depend on the local small scale suppliers for services and spares, etc. They may be more cost effective in the short term; but industry should know what all they are missing: new technology, sound practice, expert advice, standard and assured items-to name a few.
6. It takes two to tango; underground mining should rather form alliance with large manufacturers rather than taking them as one time suppliers.
7. Get into a communication. Spread your demands on the table and listen to the other side-both ways-and make things work for both.

Long Term Implications for Global Underground Mining

1. Underground mining particularly long wall mining can face a service problem as Cat's network would be weakened.
2. The market will go to oligopoly where few OEMs and suppliers will rule the roost.
3. Smaller OEMs and service providers would only sell outdated and substandard technology.
4. Technology adoption for underground mining will be severely hit; it might get lot slower.
5. The underground mining OEM market is going to the hand of considerably smaller companies who will not have resources and preparedness to develop and align with new technology. As a result, technology development would halt.
6. It is a wakeup call not only for the underground mining industry but also the regulators, testing, and standardization agencies as well as the scientific and academic community.
7. In short, neglecting the concerns for mining OEMs can hurt the community without bias.
8. The industry should start a line of communication with the OEMs to come to a common ground before it is too late.

Final Words: Collaboration is the Key

Many mining companies have a deeply ingrained, conventional view of their sector and the environment in which they operate. But while it has served them in the past, it's less likely to work in the future. Miners can no longer afford to ignore the role of the community that they need for support, read manufacturers here – an ecosystem that is growing and becoming more complex every day.

Sustainability, collaboration and sharing common cause and interest will be the key to success. Otherwise, miners are largely left to themselves. Fosters a high degree of collaboration will help building trust and understanding concerns. As with only a handful of global players in the sector, an inevitable sense of mutual self-interest comes to dominate. There's a tendency for production to become over-controlled and prices to be managed. Trust deficit challenges between the company and the manufactures are a regular event, contrasting with needing just the opposite.

(Concluded)