

# Southern Copper Corporation **SCCO** [NYSE] | ★★★

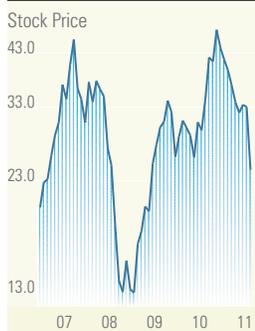
| Last Price | Fair Value | Consider Buy | Consider Sell | Uncertainty | Economic Moat™ | Stewardship | Morningstar Credit Rating | Industry |
|------------|------------|--------------|---------------|-------------|----------------|-------------|---------------------------|----------|
| 26.09 USD  | 25.00 USD  | 12.50 USD    | 43.80 USD     | Very High   | Narrow         | —           | BBB+                      | Copper   |

## Buenavista Ramp-Up Boosts Southern Copper's Output, Management Seems Cautiously Optimistic on Peru

by Daniel Rohr, CFA  
Senior Securities Analyst  
Analysts covering this company do not own its stock.

Pricing data through October 07, 2011.  
Rating updated as of October 07, 2011.

Currency amounts expressed with "\$" are in U.S. dollars (USD) unless otherwise denoted.



### Analyst Note Aug. 01, 2011

Stronger copper prices and the ramp up of the massive Buenavista copper mine in Mexico to full production translated into a sharp increase in Southern Copper's sales (up 54% from the second quarter of 2010) and operating income (up 85%). Operating cash costs after by-product credits came in at \$0.37/lb (an enviable result by industry standards), an increase from \$0.24/lb in the first quarter, as Buenavista generates less by-product metal than some of the company's other mines.

Cash costs before by-product credits held steady on a sequential basis (\$1.68/lb from \$1.66/lb in the first quarter). While this result suggests very little unit cost inflation, we'd conjecture that the steady cost profile was a function of better fixed cost leverage at Buenavista and superior ore grades at Cuajone in Peru, which masked the effects of higher raw material costs and stronger local currencies. We hope to see additional granularity on this topic offered in Southern Copper's Tuesday earnings call.

On the topic of Peru--and what the election of Humala might mean for Southern Copper--the press release signaled cautious optimism (see June 7, 2011 note for our thoughts on the matter). Southern Copper has big plans for the country, aiming to boost production from 355,000 tons per year (tpy) to 647,000 tpy through an array of projects, including the greenfield Tia Maria mine and brownfield expansions at Toquepala and Cuajone. Management indicated that the company is now confident that "the new government will guarantee social stability, the rule of law, and a stable and competitive tax regime," echoing what we've heard from other miners with Peruvian assets and in line with our assessment of the situation. Again, we hope to obtain additional color on Southern Copper's earnings call.

**Thesis** Apr. 15, 2011

Southern Copper assumed its present size and shape in 2005, when Mexican conglomerate Grupo Mexico combined the operations of Southern Peru Copper (in which it had purchased a majority stake in 2004) with those of Minera Mexico (key assets of which it had acquired via government auction in 1988-90). At present, Grupo Mexico owns 80% of Southern Copper's outstanding shares. In its current form, Southern Copper ranks as the world's largest copper miner by reserves (132 billion pounds of proven and probable reserves as of year-end 2010), among the largest by annual output (1.1 billion pounds in 2010), and, thanks to an enviable portfolio of world-class open-pit mines, among the lowest cost. Three variables are likely to dictate Southern Copper's long-term fortunes: the price of copper, the success of expansion projects in Peru and Mexico, and management's ability to maintain amicable labor relations.

Copper prices will be the biggest driver of Southern Copper's earnings power. Following a period of sub-\$1.00 per pound copper prices that stretched back to the mid-1990s, surging emerging market demand (particularly China) kicked off a historic price runup beginning in late 2003. Rising demand outstripped the industry's ability to expand mine output on a cost-effective basis, pushing copper prices past \$2.00 in 2005 and above \$3.00 in 2006. The runup continued more or less unabated until the dark days of late 2008, when copper prices plummeted more than 60% in a matter of months, to an average of \$1.37 in December. To the surprise of most industry players, copper's recovery in 2009 was nearly as dramatic. By November 2009, prices had recovered above \$3.00 and haven't looked back.

The multi-billion-dollar question for Southern Copper is whether the \$3.00-plus prices that prevailed for most of the past few years represent a true "new normal" that will persist for the foreseeable future. Based on prevailing share prices, the market seems to think so, in effect, pricing in strong future copper demand growth driven by China and other emerging markets and a continued inability for the supply side to keep pace. For our part,

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| Close Competitors                  | Currency(Mil) | Market Cap | TTM Sales | Oper Income | Net Income |
|------------------------------------|---------------|------------|-----------|-------------|------------|
| <b>Southern Copper Corporation</b> | USD           | 22,057     | 6,160     | 3,216       | 1,994      |
| <b>First Quantum Minerals Ltd.</b> | USD           | —          | —         | —           | —          |

Morningstar data as of October 07, 2011.

we're a bit less sanguine on long-term copper prices, and by extension, Southern Copper's valuation. While we have little quarrel with the conventional wisdom regarding copper's long-term demand outlook (the risks inherent to a Chinese fixed asset investment bubble notwithstanding), we think the market underestimates the sheer scale of the eventual supply side response to recent sky-high copper prices. Granted, at present, supply is severely constrained: while miners would love to goose output, they can't do so at the drop of a hat. At present, there's no slack left in the system. Barring a setback in emerging market growth, we expect the relatively inelastic short-term supply situation will keep copper at elevated levels in 2011 and most of 2012. Yet beginning in the second half of 2012, we expect to see a reversal in copper's fortunes. Enticed by today's record copper prices and cheap capital, producers are gearing up for a massive increase in copper output--a surge in supply that, owing to the time it takes to expand an existing mine (much less develop a greenfield operation) will only manifest years after the wheels are set in motion. Importantly, the vast majority of the new supply is very inframarginal, meaning cash costs are well below the industry's long-term marginal cost of production, which we estimate at roughly \$2.00/lb in 2011 dollars. The upshot of this is that, in contrast to new oil supplies, which tend to be more marginal in nature, new copper supplies will have the effect of shifting out the supply curve, which should bring copper prices closer to the industry's long-term marginal cost.

Whether copper remains above \$3.00 for the foreseeable

future or returns to more modest levels, we expect Southern Copper to remain solidly profitable thanks to the low-cost profile of its large and long-lived Mexican and Peruvian open-pit mines. From 2008 through 2010, Southern Copper's consolidated cash costs (including byproduct credits) averaged a mere \$0.25 per pound against an average copper price of \$2.96. By way of comparison, fellow copper giant Freeport McMoRan's consolidated cash costs averaged \$0.83 over the same period. We expect Southern Copper will maintain its overall cost edge, but investors can expect unit costs to vary according to molybdenum and zinc price levels (steel demand will be a primary driver), energy prices (in 2010, energy inputs accounted for 36% of total production costs), and mine sequencing.

Southern Copper also has an attractive growth profile. The return of Cananea to normal production levels (roughly 400 million pounds per year) and completion of two major projects in Peru (nearly 500 million pounds per year) should put the company on pace to nearly double 2010 volumes within a few years.

## Valuation, Growth and Profitability

Our fair value estimate of Southern Copper shares is \$25. Not surprisingly, our copper price forecast is the most critical assumption in our model. We expect copper prices to remain strong in 2011 and most of 2012, reflecting a combination of short-term supply inelasticity, emerging market demand growth, and a continued recovery in OECD demand. Beginning in the second half of 2012, we expect copper prices to trend lower, reaching a "midcycle" price of \$2.50/lb in 2014. This relatively bearish forecast is predicated on the belief that the eventual supply side response to today's heady mix of record copper prices and incredibly cheap capital will be stronger than most expect and will be sufficient to push prices closer to the industry's long-term marginal cost of production, which we

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estimate at \$2.00 per pound in 2011 dollars, far below the elevated prices at which copper trades today.

In addition to our copper price forecast, other key valuation drivers for Southern Copper include the price of molybdenum and volume and cost expectations for the company's expansion projects. Our valuation is also sensitive to the discount rate we assign to future cash flows. We use a 12% cost of equity—a higher-than-average discount rate, but in our mind reasonable because of commodity price volatility, country-specific risk, and the fact that Grupo Mexico, which owns a controlling stake in Southern Copper, may not always act in the best interest of minority shareholders. This discount rate results in a terminal EV/EBITDA multiple of 6.7 times. Were we to employ a 10% cost of equity, which is closer to the average across Morningstar's entire coverage universe (but in our opinion not indicative of Southern Copper's risk profile), our fair value estimate would leap to \$32 per share and an associated terminal EV/EBITDA multiple of 8.3 times.

## Risk

Southern Copper bears risk associated with copper's often volatile price, but is the only major producer we cover that undertakes significant hedging activities to dampen the associated cash flow volatility. As of Dec. 31, 2010, the company had hedged 28% of 2011 production at \$4.00/lb, plus an additional 31% through zero-cost collars, with an average floor of \$3.02/lb and cap of \$4.84/lb. Explaining the rationale for the hedging strategy, management noted that while it expects the copper market to run a deficit in 2011 (4%-5% demand growth accompanied by 1%-2% mine supply growth), it considers the recent runup in copper prices to be an "overreaction" exacerbated by investment demand.

Under Mexican and Peruvian laws, mineral resources are

owned by the state, with mining concessions awarded to firms like Southern Copper. A favorable political climate and amicable government relations are therefore critical to Southern Copper, but are by no means a sure thing. Lima has an unfortunate history of price controls, currency controls, investment controls, and asset expropriation, at times making for an inhospitable climate for foreign investors like Southern Copper. In recent years, however, circumstances in Peru have improved. Inflation, for instance, fell from a high of 7,649.7% in 1990 to 5.8% in 2008, 2.9% in 2009, and 1.5% in 2010.

Another source of country-specific risk is the labor unrest that has often bedeviled Southern Copper and its copper mining peers in Latin America. Southern Copper's low-leverage balance sheet proved crucial amid the financial crisis. This conservative capital structure will prove valuable as the firm navigates the ups and downs of highly cyclical copper prices.

## Bulls Say

- Southern Copper's low-leverage balance sheet proved crucial amid the financial crisis. This conservative capital structure will prove valuable as the firm navigates the ups and downs of highly cyclical copper prices.
- Southern Copper's Mexican and Peruvian mines are low cost, a dependable source of free cash flow in nearly any copper price environment.
- Southern Copper boasts a massive, long-lived reserve base of 132 billion pounds at a long-run assumed copper price of merely \$1.80.

## Bears Say

- Labor unrest has been a near-constant headache for Southern Copper. Management estimates the Cananea strike depressed operating income by \$1.1 billion in

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2008 alone.

- Grupo Mexico has a dominant ownership stake in Southern Copper and could take actions that run counter to the interests of minority shareholders.
- Southern Copper's profitability depends on favorable copper prices, which have proved to be highly volatile.

## Financial Overview

**Financial Health:** Southern Copper is in robust financial health. The company ended 2010 with \$2.2 billion in cash against \$2.8 billion in debt, with minimal maturities until 2015 (when a modest \$200 million maturity comes due). Despite significant capital expenditures slated for 2011 (management has guided \$1.7 billion), we expect Southern Copper to produce ample free cash flows for the year, thanks to strong prevailing copper prices. Even under a weaker copper price scenario, the company should have little difficulty generating the cash necessary to meet its contractual obligations. In the nervous years of 2008 and 2009, Southern Copper generated an average \$876 million in annual free cash flow.

## Company Overview

**Profile:** Southern Copper is one of the world's largest copper producers. The firm's 132 billion pounds of reserves at year-end 2010 (assuming \$1.80/lb copper prices) ranked as the world's largest. In 2010, Southern Copper produced 1.1 billion pounds of copper as well as a material amount of molybdenum and zinc, although these metals constitute a much smaller share of total revenue. Mexican conglomerate Grupo Mexico owns 80% of Southern Copper's outstanding shares.

**Management:** Oscar Gonzalez Rocha became CEO in 2004, replacing Larrea family scion German Larrea Mota-Velasco, who remains as chairman. Rocha retains

the title of president, which he has held since 1999. Gonzalez and Larrea have long histories with Southern Copper and its related companies, sitting on several boards and holding key executive posts in many of the related firms. Larrea is CEO and chairman of Grupo Mexico, which now owns 80% of Southern Copper's outstanding shares. Given Grupo Mexico's huge ownership stake and control of the board, minority shareholders have little influence on corporate actions. We note, however, that in recent years, Southern Copper has proved to be a much better steward of shareholder value than many of its peers that are 100% publicly owned. Conservative balance sheet management enabled Southern Copper to buy back a sizable quantity of its shares at dirt-cheap prices in late 2008. Meanwhile, many more leveraged miners were scrambling to tap the markets for what proved to be very expensive capital. We also note that Southern Copper offers a higher dividend payout than many mining companies (perhaps a consequence of Larrea family control). The company paid out an average of 80% of net income from 2005 through 2010--a total of \$7.9 billion.

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## Analyst Notes

Aug. 01, 2011

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Jul. 21, 2011

### Newly-Released Copper Demand Data Is Open to Interpretation: Is Chinese Demand Really Dropping?

Copper supply and demand data released by the International Copper Study Group (ICSG) on Thursday paints a decidedly less bullish picture for copper than that espoused by most market commentators. But quirks in the ICSG data set could be rendering the message more bearish for the red metal than it really is.

According to the ICSG data for April (ICSG reports with a significant lag, but it's the best available picture of actual supply and demand conditions), global mine production increased 2.1% and global apparent consumption was up 1.2% in the first four months of 2011. Year-to-date, ICSG estimates a seasonally-adjusted surplus of 46,000 tonnes, meaning the world has produced more copper than it has consumed.

Set against the 6.9% post-slump copper consumption surge we saw in 2010 and the 2.5% compound annual growth rate from 2000 to 2010, the relatively weak YTD consumption growth portrayed in the ICSG data might seem downright bearish for copper prices and casts doubt on the sustainability of prevailing copper prices, which remain near record highs.

Digging a bit deeper into the ICSG data set, the most striking number is the 7% YTD decline in apparent Chinese consumption. If sustained for the remainder of the year, this would mark a major reversal for a country where consumption grew at a 15% annual rate during the last decade. Put lightly, that would be bad news for copper miners (China comprises about 40% of global demand), which are staking massive capital expenditures on

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## Analyst Notes (continued)

continued growth in Chinese copper consumption.

Yet there is likely more than meets the eye in the Chinese numbers. ICSG estimates Chinese consumption by summing domestic production, net imports, and reported inventory changes. Unfortunately, a nontrivial share of Chinese inventories go unreported. In our view, it seems likely that the YTD decline in apparent consumption is largely attributable to an inventory drawdown at these "nonreporters," as opposed to a sharp reversal in a decade-long bull trend.

That said, in light of Thursday's China PMI "flash" reading from HSBC, which, at 48.9 marked the first sub-50 reading

in many months and the lowest level in 28 months, it seems likely that 2011 will mark a slowdown in China's copper consumption growth, if not an outright drop. Of course, the bigger risk to the copper market is that China sees a reversal in the hitherto nonstop growth in fixed-asset investment and real estate development--two big drivers of copper consumption. At present, we do not believe share prices of copper producers adequately compensate investors for this risk or the risk that prevailing copper prices engender a stronger supply-side response than many seem to expect (see our Dec. 20, 2010, note on the latter subject).

Jun. 07, 2011

### Humala's Election No Boon for Southern Copper, But No Disaster Either

The victory of left-leaning Nationalist Party candidate Ollanta Humala in Peru's June 5 presidential election triggered a sharp reversal in Southern Copper's shares, which fell 11% Monday on the heels of a 7% bump last Thursday after the release of poll numbers that had shown rival candidate Keiko Fujimori, perceived as the more business-friendly candidate, holding a narrow lead. The drop in Southern Copper's share price is somewhat understandable given Humala's repeated campaign promises to increase government involvement in Peru's natural resource sector and to hike mining royalties, his stated admiration of Venezuelan leader Hugo Chavez, and his 2000 move (as an army officer) to temporarily seize one of Southern Copper's mines. Indeed, with Peruvian assets responsible for roughly 60% of Southern Copper's consolidated revenues and 66% of segment operating income in 2010, any adverse developments in Peru would have serious negative implications for Southern Copper's underlying value. That said, for a variety of reasons, we think Monday's share price reversal represents a bit of an overreaction and we've opted to maintain our \$25 per share

fair value estimate.

For starters, it'd be an error to draw a straight line between the fiery rhetoric and ideological purity that defines most political campaigns and the laws and regulations that ultimately find their way into implementation. Notably, in recent months Humala has indicated that were he to ascend to the country's highest post he would seek to follow the more benign political path established by former Brazilian President Luiz Inacio Lula da Silva, rather than that of Venezuela's "expropriator-in-chief" Chavez. To boot, news reports have Humala swearing on the Bible that he would refrain from altering the framework that has made Peru the fastest growing economy in South America during the last decade.

Even if one were to believe the midcampaign strategic shift was wholly attributable to electoral expediency and that Humala will return to his "Chav-esque" roots once in office, he lacks the political and institutional power to implement the kind of odious policies we've seen Chavez undertake in

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## Analyst Notes (continued)

Venezuela. Humala's party controls only 47 of the 130 seats in Congress and given the divisive quality of the election and the slim margin of victory, the newly-elected president may find it difficult to pass any particularly extreme measure. He won't find friends in the media either. In contrast to the mostly cowed or state-controlled Venezuelan media, Peru's media had been largely opposed to Humala in the election. All told, we think outright expropriation is highly unlikely.

This is not to say we expect smooth sailing for Southern Copper. In all likelihood, Southern Copper and fellow Peruvian operators such as Freeport-McMoRan and Xstrata are likely to face higher royalty rates going forward. But judging by campaign promises made by Fujimori and the general popularity of such a move, a royalty hike was probably in the cards regardless of the electoral outcome. Put in perspective, the existing royalty regime, established by 2004 legislation, sets royalties at 1% to 3% of sales. For Southern Copper's Toquepala and Cujone mines, this translated to an average \$55 million in total annual royalties during the last two years, a relative pittance compared to the \$1.4 billion in average annual operating income those operations generated. While we expect higher royalty rates in the coming years, we don't expect such a move to materially damage Southern Copper's underlying value: something at or a few percentage points above neighboring Chile's 4% seems likely.

In addition to royalties, we expect the new government to

review other means of extracting cash from the wildly profitable mining sector. While we think a punitive windfall profits tax is relatively unlikely, a return to some sort of "regional development contribution" mechanism (aimed at ensuring profits generated in a poor region are reinvested locally) is a strong possibility. Under the old five-year law, which expired in 2010, Southern Copper had paid roughly \$14 million annually in regional development contributions--again a relatively small number that, even if increased substantially, would not represent a big blow to Southern Copper's finances.

Perhaps the biggest risk to Southern Copper's shares stems not from the portion of sales or profits it shares with the government, but from whether the government approves the company's various high-NPV capital projects, including the stalled Tia Maria copper mine (see our April 20 note). In the case of Tia Maria, we expect some sort of accommodation will be reached, perhaps entailing a special program akin to what we saw in the regional development contribution mechanism.

All told, while Humala's June 5 victory is surely no boon to Southern Copper, we doubt it is the disaster some believe it to be. We think the 12% cost of equity used in our Southern Copper valuation (quite a bit higher than the norm for Morningstar's coverage universe) adequately captures the country-specific risk associated with operations in Peru.

Apr. 20, 2011

### Southern Copper Management Cautious on Copper's Near-Term Outlook, Optimistic on Tia Maria

Higher copper prices (up 34% to \$4.38 per pound) and the restart of the benighted Buenavista mine (formerly known as Cananea) in Mexico contributed to 31% top-line expansion in Southern Copper's first quarter. Consolidated cash costs, while higher sequentially, remained very

impressive on an absolute basis, coming in at \$0.24 per pound after byproducts, by far the lowest of any copper miner we cover. Barring a big drop in copper prices, we should see sequential sales growth in the second quarter as Buenavista reaches full capacity (about 400 million

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## Analyst Notes (continued)

pounds per year) and the Cujajone mine in Peru intersects higher ore grades.

Southern Copper remains the only major copper producer we cover to hedge a significant share of its planned production. The company reported it had hedged 32% of its remaining 2011 production at \$4.08 per pound and

implemented zero-cost collars (cap \$4.84, floor \$3.02) on another 30%. For 2012, collars are now in place for 13% of planned output. Management said today's prices "imply an acute scarcity of physical material that we were not seeing at the end of the fourth quarter of 2010 and we still don

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**Sales USD Mil** 6,160 **Mkt Cap USD Mil** 22,057 **Industry** Copper **Sector** Basic Materials

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**Morningstar Rating** ★★ ★ **Last Price** 26.09 **Fair Value** 25.00 **Uncertainty** Very High **Economic Moat™** Narrow **Stewardship Grade** —  
per share prices in USD



| Growth Rates Compound Annual |       |       |      |       |  |
|------------------------------|-------|-------|------|-------|--|
| Grade: C                     | 1 Yr  | 3 Yr  | 5 Yr | 10 Yr |  |
| Revenue %                    | 37.9  | -5.4  | 4.6  | 21.9  |  |
| Operating Income %           | 75.3  | -9.4  | 4.5  | 33.1  |  |
| Earnings/Share %             | 67.9  | -10.0 | 2.9  | 25.2  |  |
| Dividends %                  | 280.1 | -9.5  | 9.6  | 40.4  |  |
| Book Value/Share %           | 0.4   | 1.7   | 4.0  | 6.3   |  |
| Stock Total Return %         | -26.2 | 33.6  | 17.5 | 36.9  |  |
| +/- Industry                 | 0.3   | 5.9   | 4.6  | 7.4   |  |
| +/- Market                   | -26.0 | 28.5  | 20.6 | 36.1  |  |

| Profitability Analysis |         |          |      |        |
|------------------------|---------|----------|------|--------|
| Grade: C               | Current | 5 Yr Avg | Ind  | Mkt    |
| Return on Equity %     | 51.0    | 44.4     | 44.4 | 24.6   |
| Return on Assets %     | 26.2    | 25.7     | 20.5 | 9.6    |
| Fixed Asset Turns      | 1.5     | 1.4      | 1.3  | 7.3    |
| Inventory Turns        | 4.7     | 4.7      | 3.4  | 15.2   |
| Revenue/Employee USD K | 553.7   | 403.0*   | —    | 1005.9 |
| Gross Margin %         | 59.6    | 58.3     | 54.1 | 39.2   |
| Operating Margin %     | 52.2    | 49.8     | 50.0 | 16.1   |
| Net Margin %           | 32.4    | 31.6     | 26.3 | 10.9   |
| Free Cash Flow/Rev %   | 22.4    | 27.5     | 23.8 | 0.1    |
| R&D/Rev %              | —       | —        | —    | 10.0   |

| Financial Position  |               |               |
|---------------------|---------------|---------------|
| Grade: B            | 12-10 USD Mil | 06-11 USD Mil |
| Cash                | 2193          | 1454          |
| Inventories         | 505           | 609           |
| Receivables         | 748           | 880           |
| Current Assets      | 3703          | 3272          |
| Fixed Assets        | 4095          | 4130          |
| Intangibles         | 112           | 111           |
| Total Assets        | 8128          | 7794          |
| Payables            | 830           | 469           |
| Short-Term Debt     | 10            | 10            |
| Current Liabilities | 1139          | 698           |
| Long-Term Debt      | 2750          | 2740          |
| Total Liabilities   | 4238          | 3793          |
| Total Equity        | 3890          | 4001          |

| Valuation Analysis   |         |          |     |      |
|----------------------|---------|----------|-----|------|
|                      | Current | 5 Yr Avg | Ind | Mkt  |
| Price/Earnings       | 11.1    | 17.7     | 7.1 | 12.8 |
| Forward P/E          | 7.8     | —        | —   | 12.4 |
| Price/Cash Flow      | 12.3    | 15.6     | 5.9 | 6.5  |
| Price/Free Cash Flow | 16.1    | 22.6     | 7.9 | 15.3 |
| Dividend Yield %     | 8.4     | —        | 4.9 | 2.2  |
| Price/Book           | 5.5     | 6.9      | 2.9 | 1.6  |
| Price/Sales          | 3.6     | 5.3      | 1.9 | 1.1  |
| PEG Ratio            | 0.5     | —        | —   | 1.6  |

| 2001  | 2002 | 2003  | 2004 | 2005 | 2006  | 2007  | 2008  | 2009  | 2010  | YTD   | Stock Performance  |
|-------|------|-------|------|------|-------|-------|-------|-------|-------|-------|--------------------|
| -4.4  | 24.3 | 231.4 | 5.2  | 55.4 | 76.2  | 107.7 | -48.6 | 107.7 | 53.2  | -42.9 | Total Return %     |
| 8.6   | 47.7 | 205.0 | -3.8 | 52.4 | 62.6  | 104.2 | -10.1 | 84.3  | 40.4  | -34.8 | +/- Market         |
| -32.8 | -0.7 | 55.0  | 7.7  | 6.8  | 30.0  | 6.1   | 16.4  | -53.2 | -0.6  | 0.8   | +/- Industry       |
| 3.0   | 3.1  | 1.2   | 5.1  | 9.5  | 9.5   | 6.5   | 12.1  | 1.3   | 3.5   | 8.4   | Dividend Yield %   |
| 956   | 1152 | 3774  | 3778 | 9861 | 15868 | 30957 | 13988 | 27974 | 41429 | 22057 | Market Cap USD Mil |

| 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | TTM  | Financials               |
|------|------|------|------|------|------|------|------|------|------|------|--------------------------|
| 658  | 665  | 798  | 1716 | 4113 | 5460 | 6086 | 4851 | 3734 | 5150 | 6160 | Revenue USD Mil          |
| 29.9 | 32.3 | 39.8 | 60.3 | 59.6 | 62.6 | 64.5 | 54.3 | 51.2 | 59.2 | 59.6 | Gross Margin %           |
| 89   | 119  | 217  | 927  | 2095 | 3054 | 3497 | 2202 | 1485 | 2604 | 3216 | Oper Income USD Mil      |
| 13.6 | 17.9 | 27.2 | 54.0 | 50.9 | 55.9 | 57.5 | 45.4 | 39.8 | 50.6 | 52.2 | Operating Margin %       |
| 47   | 61   | 122  | 597  | 1400 | 2038 | 2216 | 1407 | 929  | 1554 | 1994 | Net Income USD Mil       |
| 0.10 | 0.13 | 0.25 | 1.24 | 1.59 | 2.31 | 2.51 | 1.60 | 1.09 | 1.83 | 2.35 | Earnings Per Share USD   |
| 0.06 | 0.07 | 0.09 | 0.40 | 1.06 | 1.71 | 2.27 | 1.94 | 0.44 | 1.68 | 1.94 | Dividends USD            |
| 480  | 480  | 480  | 480  | 883  | 883  | 883  | 879  | 851  | 850  | 850  | Shares Mil               |
| 2.52 | 2.59 | 2.74 | 3.58 | 3.77 | 4.15 | 4.36 | 3.88 | 4.56 | 4.58 | 4.73 | Book Value Per Share USD |
| 198  | 142  | 191  | 717  | 1644 | 2059 | 2703 | 1721 | 963  | 1921 | 1804 | Oper Cash Flow USD Mil   |
| -161 | -77  | -50  | -172 | -471 | -456 | -316 | -517 | -415 | -409 | -424 | Cap Spending USD Mil     |
| 37   | 65   | 141  | 546  | 1174 | 1604 | 2388 | 1204 | 548  | 1512 | 1379 | Free Cash Flow USD Mil   |

| 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | TTM  | Profitability      |
|------|------|------|------|------|------|------|------|------|------|------|--------------------|
| 2.6  | 3.4  | 6.6  | 26.4 | 33.8 | 33.8 | 34.2 | 22.8 | 15.7 | 21.9 | 26.2 | Return on Assets % |
| 3.9  | 4.9  | 9.6  | 39.3 | 55.5 | 58.3 | 59.0 | 38.9 | 25.6 | 40.0 | 51.0 | Return on Equity % |
| 7.1  | 9.1  | 15.3 | 34.8 | 34.0 | 37.3 | 36.4 | 29.0 | 24.9 | 30.2 | 32.4 | Net Margin %       |
| 0.37 | 0.37 | 0.43 | 0.76 | 0.99 | 0.91 | 0.94 | 0.79 | 0.63 | 0.73 | 0.81 | Asset Turnover     |
| 1.5  | 1.4  | 1.5  | 1.5  | 1.7  | 1.7  | 1.7  | 1.7  | 1.6  | 2.1  | 2.0  | Financial Leverage |

| 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 06-11 | Financial Health        |
|------|------|------|------|------|------|------|------|------|------|-------|-------------------------|
| 206  | 210  | 289  | 552  | 919  | 1583 | 1708 | 816  | 1176 | 2564 | 2574  | Working Capital USD Mil |
| 273  | 299  | 289  | 257  | 1162 | 1518 | 1290 | 1280 | 1270 | 2750 | 2740  | Long-Term Debt USD Mil  |
| 1209 | 1241 | 1315 | 1721 | 3326 | 3667 | 3848 | 3381 | 3876 | 3890 | 4001  | Total Equity USD Mil    |
| 0.23 | 0.24 | 0.22 | 0.15 | 0.35 | 0.41 | 0.34 | 0.38 | 0.33 | 0.71 | 0.68  | Debt/Equity             |

| 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | TTM  | Valuation       |
|------|------|------|------|------|------|------|------|------|------|------|-----------------|
| 19.6 | 16.8 | 31.3 | 6.3  | 7.0  | 7.8  | 14.0 | 10.0 | 30.2 | 26.7 | 11.1 | Price/Earnings  |
| 1.5  | 1.7  | 4.7  | 2.2  | 1.3  | 2.9  | 5.1  | 2.9  | 7.5  | 8.1  | 3.6  | P/E vs. Market  |
| 0.8  | 0.9  | 2.9  | 2.2  | 3.0  | 4.3  | 8.1  | 4.1  | 7.2  | 10.7 | 5.5  | Price/Sales     |
| 4.8  | 8.1  | 19.8 | 5.3  | 3.3  | 7.7  | 11.4 | 8.2  | 29.1 | 21.6 | 12.3 | Price/Cash Flow |

| Quarterly Results      |        |        |        |        |  |
|------------------------|--------|--------|--------|--------|--|
| Revenue USD Mil        | Sep 10 | Dec 10 | Mar 11 | Jun 11 |  |
| Most Recent Period     | 1257.9 | 1499.0 | 1602.0 | 1801.5 |  |
| Prior Year Period      | 1151.8 | 1136.0 | 1219.4 | 1173.2 |  |
| Rev Growth %           | Sep 10 | Dec 10 | Mar 11 | Jun 11 |  |
| Most Recent Period     | 9.2    | 31.9   | 31.4   | 53.5   |  |
| Prior Year Period      | -20.0  | 152.6  | 96.0   | 42.3   |  |
| Earnings Per Share USD | Sep 10 | Dec 10 | Mar 11 | Jun 11 |  |
| Most Recent Period     | 0.43   | 0.58   | 0.56   | 0.78   |  |
| Prior Year Period      | 0.37   | 0.42   | 0.45   | 0.37   |  |

| Industry Peers by Market Cap |                 |             |      |      |
|------------------------------|-----------------|-------------|------|------|
|                              | Mkt Cap USD Mil | Rev USD Mil | P/E  | ROE% |
| Southern Copper Corp         | 22057           | 6160        | 11.1 | 51.0 |
| First Quantum Minera         | —               | —           | —    | —    |

| Major Fund Holders |  | % of shares |
|--------------------|--|-------------|
|                    |  | —           |
|                    |  | —           |
|                    |  | —           |

\*3Yr Avg data is displayed in place of 5Yr Avg TTM data based on rolling quarterly data if available; otherwise most recent annual data shown.  
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## Morningstar's Approach to Rating Stocks

### Our Key Investing Concepts

- ▶ Economic Moat™ Rating
- ▶ Discounted Cash Flow
- ▶ Discount Rate
- ▶ Fair Value
- ▶ Uncertainty
- ▶ Margin of Safety
- ▶ Consider Buying/Consider Selling
- ▶ Stewardship Grades

At Morningstar, we evaluate stocks as pieces of a business, not as pieces of paper. We think that purchasing shares of superior businesses at discounts to their intrinsic value and allowing them to compound their value over long periods of time is the surest way to create wealth in the stock market.

We rate stocks 1 through 5 stars, with 5 the best and 1 the worst. Our star rating is based on our analyst's estimate of how much a company's business is worth per share. Our analysts arrive at this "fair value estimate" by forecasting how much excess cash--or "free cash flow"--the firm will generate in the future, and then adjusting the total for timing and risk. Cash generated next year is worth more than cash generated several years down the road, and cash from a stable and consistently profitable business is worth more than cash from a cyclical or unsteady business.

Stocks trading at meaningful discounts to our fair value estimates will receive high star ratings. For high-quality businesses, we require a smaller discount than for mediocre ones, for a simple reason: We have more confidence in our cash-flow forecasts for strong companies, and thus in our value estimates. If a stock's market price is significantly above our fair value estimate, it will receive a low star rating, no matter how wonderful we think the business is. Even the best company is a bad deal if an investor overpays for its shares.

Our fair value estimates don't change very often, but market prices do. So, a stock may gain or lose stars based

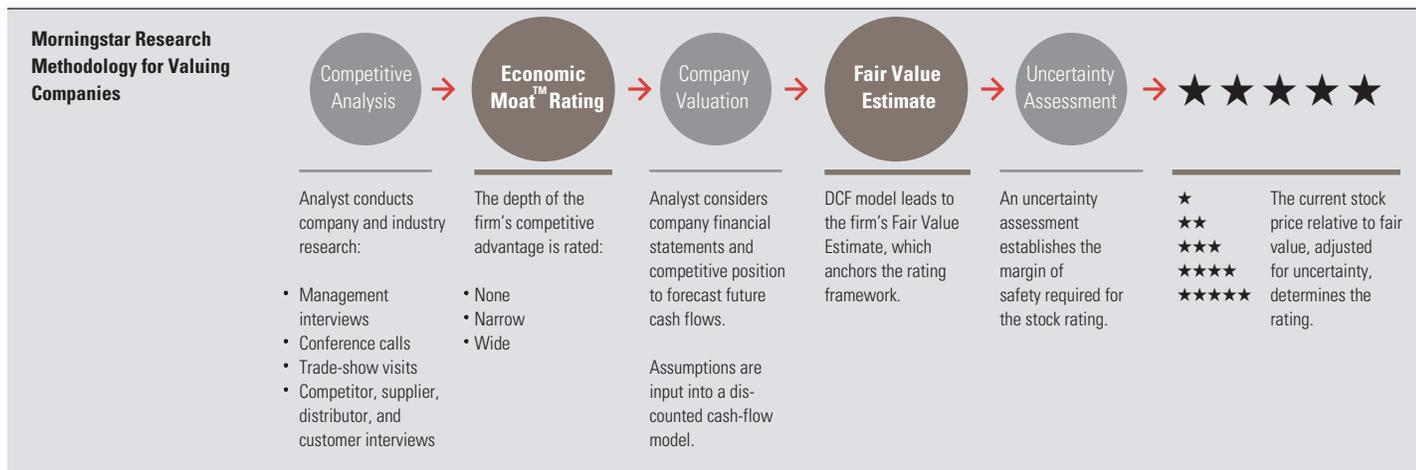
just on movement in the share price. If we think a stock's fair value is \$50, and the shares decline to \$40 without much change in the value of the business, the star rating will go up. Our estimate of what the business is worth hasn't changed, but the shares are more attractive as an investment at \$40 than they were at \$50.

Because we focus on the long-term value of businesses, rather than short-term movements in stock prices, at times we may appear out of step with the overall stock market. When stocks are high, relatively few will receive our highest rating of 5 stars. But when the market tumbles, many more will likely garner 5 stars. Although you might expect to see more 5-star stocks as the market rises, we find assets more attractive when they're cheap.

We calculate our star ratings nightly after the markets close, and issue them the following business day, which is why the rating date on our reports will always be the previous business day. We update the text of our reports as new information becomes available, usually about once or twice per quarter. That is why you'll see two dates on every Morningstar stock report. Of course, we monitor market events and all of our stocks every business day, so our ratings always reflect our analyst's current opinion.

### Economic Moat™ Rating

The Economic Moat™ Rating is our assessment of a firm's ability to earn returns consistently above its cost of capital in the future, usually by virtue of some competitive advantage. Competition tends to drive down such



## Morningstar's Approach to Rating Stocks (continued)

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economic profits, but companies that can earn them for an extended time by creating a competitive advantage possess an Economic Moat. We see these companies as superior investments.

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### Discounted Cash Flow

This is a method for valuing companies that involves projecting the amount of cash a business will generate in the future, subtracting the amount of cash that the company will need to reinvest in its business, and using the result to calculate the worth of the firm. We use this technique to value nearly all of the companies we cover.

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### Discount Rate

We use this number to adjust the value of our forecasted cash flows for the risk that they may not materialize. For a profitable company in a steady line of business, we'll use a lower discount rate, also known as "cost of capital," than for a firm in a cyclical business with fierce competition, since there's less risk clouding the firm's future.

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### Fair Value

This is the output of our discounted cash-flow valuation models, and is our per-share estimate of a company's intrinsic worth. We adjust our fair values for off-balance sheet liabilities or assets that a firm might have--for example, we deduct from a company's fair value if it has issued a lot of stock options or has an under-funded pension plan. Our fair value estimate differs from a "target price" in two ways. First, it's an estimate of what the business is worth, whereas a price target typically reflects what other investors may pay for the stock. Second, it's a long-term estimate, whereas price targets generally focus on the next two to 12 months.

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### Uncertainty

To generate the Morningstar Uncertainty Rating, analysts consider factors such as sales predictability, operating leverage, and financial leverage. Analysts then classify their ability to bound the fair value estimate for the stock into one of several uncertainty levels: Low, Medium, High,

Very High, or Extreme. The greater the level of uncertainty, the greater the discount to fair value required before a stock can earn 5 stars, and the greater the premium to fair value before a stock earns a 1-star rating.

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### Margin of Safety

This is the discount to fair value we would require before recommending a stock. We think it's always prudent to buy stocks for less than they're worth. The margin of safety is like an insurance policy that protects investors from bad news or overly optimistic fair value estimates. We require larger margins of safety for less predictable stocks, and smaller margins of safety for more predictable stocks.

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### Consider Buying/Consider Selling

The consider buying price is the price at which a stock would be rated 5 stars, and thus the point at which we would consider the stock an extremely attractive purchase. Conversely, consider selling is the price at which a stock would have a 1 star rating, at which point we'd consider the stock overvalued, with low expected returns relative to its risk.

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### Stewardship Grades

We evaluate the commitment to shareholders demonstrated by each firm's board and management team by assessing transparency, shareholder friendliness, incentives, and ownership. We aim to identify firms that provide investors with insufficient or potentially misleading financial information, seek to limit the power of minority shareholders, allow management to abuse its position, or which have management incentives that are not aligned with the interests of long-term shareholders. The grades are assigned on an absolute scale--not relative to peers--and can be interpreted as follows: A means "Excellent," B means "Good," C means "Fair," D means "Poor," and F means "Very Poor."

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