A challenging year for the African mining sector in 2017 - what does 2018 hold?

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Mining Newsletter

Commodity trends of 2017 - will these change in 2018?

There was a strong, consistent focus on thermal and coking coal, gold, copper and the platinum group metals. Interest in chrome, iron ore and manganese picked up, particularly in the last half of 2017. The strongest emphasis has however been on the so-called *"battery metals"* which is driven by new demand for these metals used in the manufacture of batteries for the ever-increasing production of electric vehicles. The trends and patterns seen in 2017 are likely to remain the same in 2018, particularly in relation to *"battery metals"*. However, another trend has emerged. Bitcoin mining is catching on in a big way, with significant investment in the *"mining rigs"* used for Bitcoin mining. The general view is that there is a window of opportunity with high levels of optimism, primarily because the regulatory and tax regimes have not yet come fully to grips with Bitcoin mining, and there are still margins to be made. Countries which can provide a steady, constant supply of electricity needed to run the hardware and cool it down, will have an advantage.

What is the current state of the African Mining Sector and will it continue in 2018?

2017 was a complex year for many African countries with every single aspect of both personal and business life being disrupted by political, socio-economic and regulatory change and uncertainty. Many of the changes were anticipated and expected, some were predicted, and some may have caught people by surprise.

Change and uncertainty has been particularly prevalent in the African mining and natural resources sector, a key barometer for the state of business, which remain critical to many African economies and which, if managed properly, can continue to contribute significantly to growth and development, to the benefit of all Africans. The mining and natural resources sector's position as a key contributor and as a potential significant driver for growth and development has been hampered by significant challenges faced by the sector, across Africa, in 2017.

A good example is the changes to Mining Laws in Tanzania which have impacted significantly, on foreign investment in Tanzania. Closer to home, the publication of the Reviewed Broad-Based Black Economic Empowerment Charter for the South African Mining and Minerals Industry 2016, on 15 June 2017 ("Mining Charter 3") and the immediate, widespread and generally negative response to Mining Charter 3 has had a negative impact on the industry. In addition to the losses sustained by mining stocks, Mining Charter 3 has also been blamed by a number of stakeholders for the high number of job losses in the mining and natural resources sector in 2017 or that it was at least, a significant contributing factor. While there may be some merit in these arguments, it would be far too simplistic to attribute the job losses to Mining Charter 3 only – there are many contributing factors such as regulatory and policy uncertainty which is broader than just Mining Charter 3, external investor perceptions of political stability, corruption and nepotism, and the significant increases in the costs of mining operations. Feasibility studies for new investment and investment in expansion projects now, are of necessity, include pricing the risk associated with policy and regulatory uncertainty, and this costing has resulted in cautious decisions on new investment.

Given the current status, it is likely that the African mining and natural resources sector will continue to face similar challenges in 2018.

Which commodities will experience the biggest changes and developments?

The commodities that are likely to be most affected in 2018 fall into two categories, namely the commodities that are driven by economic and other development, such as the commodities that are used for the production of steel and related products, and those commodities which will be driven by broader global developments such as the fourth industrial revolution, more commonly referred to as Industry 4.0, the Internet of Things, and Artificial Intelligence. The so-called "battery metals" are integral to this latter category of commodities.

Commodities, such as gold, that are now extracted from ever-increasing depths, will need to progress levels of mechanisation, and move towards full automation, for various reasons, including costs, and health and safety. All commodities will, in general, be required to review mining methodologies, in the interests of health and safety. The health and safety figures for 2017, in South Africa, have been particularly poor, and South Africa, at the very least, will need to take significant strides to improve health and safety. Similar concerns have been raised in various African countries.

With regards to commodity prices, what do you foresee?

The percentage fluctuations that were seen in 2017 in commodities such as gold, platinum, iron ore, etc., are likely to be the same. There may however be an increase in commodity prices for those commodities that are integral to the successful implementation of the Internet of Things, Artificial Intelligence, and of course, electric vehicles.

What are your views on the regulatory environment and its impact on African mining in 2018?

The regulatory environments across Africa remain of concern, with two very good examples being Tanzania and South Africa, and the impact that political decisions have had on the strong mining and natural resources sectors in both these countries.

The core component of regulatory uncertainty are consistent, transparent, practically implementable policies. The primary concerns therefore relate to policy uncertainty because without certainty in this regard, implementation through the regulatory structures and mechanisms becomes challenging. Given the current status of policies in various African jurisdictions, it is likely that, unless there are dramatic changes which drive policy certainty, the African mining industry is likely to face similar challenges in 2018.

What impact will the Revised Mining Charter have on commodities? And why?

The publication of Mining Charter 3 had an immediate, widespread and generally negative response. Unlike in respect of the two previous versions of the Mining Charter, the response were more widespread, with criticism coming from a broad spectrum of stakeholders which initially included the Chamber of Mines, which represented the majority of mining companies, trade unions, and other interested and affected parties. In November 2017 the High Court of South Africa granted a request by the Centre for Applied Legal Studies and Lawyers for Human Rights, which represent various community organisations, to join the Chamber of Mines application for a review of Mining Charter 3.

It was estimated that mining stocks lost approximately R50 billion in value, following the publication of Mining Charter 3 on 15 June 2017.

In addition to Mining Charter 3, Minister Zwane published his intention to issue a notice placing a moratorium on all applications for new prospecting and mining rights, renewals of prospecting and mining rights, and Ministerial Consents in terms of Section 11 of the Mineral and Petroleum Resources Development Act (in summary where a right or an interest in a right is to be transferred or there is a change of control, Ministerial Consent is required).

Although Minister Zwane did not issue the notice, after being challenged again, by amongst others Chamber of Mines, the intention to issue the notice, following closely on discussions regarding Mining Charter 3, created high levels of uncertainty, which impacted on investment decisions, at that time.

Since then, investors have considered their position, and in several instances, new investments have been made despite the uncertainty, by investors who have expressed the view that they have become risk tolerant. One the High Court of South Africa delivers its findings in relation to the Chamber of Mines court cases, this may provide some stability, provided the parties do not challenge the decision.

Mining Charter 3 is simply one of the factors that must be taken into account in identifying risk investment profile, and applies equally to all commodities.

What is also important to note, is that Mining Charter 3 does not only impact on South African mining companies, but also on South African and foreign suppliers of goods and services, and it is possibly, in this regard, where commodities that are marginal, may be impacted.

In the event that Mining Charter 3 comes into force and effect in its current format or in a substantially similar format, compliance will require significant commercial activity in relation to ownership, goods, services, and employment equity representation at all levels within mining companies.

There is likely to be a high level of vendor-financed transactions, to give effect to Mining Charter 3.

In terms of investments, what are your predictions for the African mining industry?

Africa remains full of opportunities and as a result, investment will continue. What has changed over the last eighteen to twenty-four months, has been which investors are investing in Africa. While the traditional investment jurisdictions, such as Canada, the United Kingdom, and the United States have continued to invest, there are numerous newer investors from countries such as China, Singapore, Korea, and Japan. Several of these investments are driven by trading companies that want to control the full value chain from extraction through to market, to provide levels of certainty which are not necessarily available without that level of control.

The investors that have taken up these opportunities have adopted a more realistic view on investment risk and return. This does not mean that their decisions are reckless – in most cases the decisions are based on careful consideration of the in-country risk profile which then allows them to put in place appropriate protection mechanisms, consistent with their risk appetite.

Which commodity will be most attractive and be a more investable option?

Any of the so-called *"battery metals"* will remain attractive and investable in 2018. There are talks that silver may pick up again in 2018.

Longer term investment is likely to remain in commodities such as gold, platinum group metals, copper, manganese and chrome.

It is likely that, for the foreseeable future, fossil fuels will remain the primary source of energy and investment in these commodities is likely to remain at current levels, throughout 2018.

Which commodity still brings risks to mind in terms of possible investments?

Iron ore unfortunately remains a potential risk in 2018. The existing mining companies have had to cut costs, dramatically, and restructure to survive within the new realty of iron ore prices. This however also means that it becomes extremely difficult for smaller operators and smaller mines, to be established. With current iron ore prices, any increase in costs could have a dramatic impact on the feasibility of these operations.

Chrome also remains extremely volatile, and robust investment strategies are required.

What do you predict with regards to international opportunities?

Africa remains an important investment destination, because of its variety and scope of resources. In relation to particular countries, recent developments in Zimbabwe are likely to refocus attention to Zimbabwe. Mozambique, Namibia, Zambia, Botswana, Ghana, Mali and Guinea, remain active investment destinations.

Looking further abroad, opportunities are still available in the United States, Australia, and the Far East. However, in these countries, mining is relatively mature, which means that the costs are high, in mature regulatory frameworks, making it extremely difficult for new entrants.

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