Advisors in resilience

Africa's Mineral & Beneficiation Policy Monitor

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Eunomix™ is a pioneering advisory firm at the nexus of strategy, risk management and socioeconomic development. The firm specialises in resource rich countries, with a focus on Africa. Serving businesses and governments, it helps deliver sustainable outcomes in the face of systemic uncertainty, competition for resources and growing demands for shared prosperity.

Eunomix produces monthly briefs monitoring and reporting on political and policy issues of relevance to clients. Current monitors cover South Africa and Zimbabwe's general policy environments as well as energy issues.

This new monitor, will be issued on a quarterly basis, and dedicated to tracking trends in beneficiation and mineral rent policy, legislation and regulation in Africa. It aims to provide a 'live' overview of the continent-wide movement to derive greater local value from the mining industry, with all the implications this entails for economic development, investment climate and the growth of the mining sector. This monitor represents a natural extension of Eunomix's extensive work on the topic.

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1. Overview and analysis

1.1. Great expectations

Following the commodity super-cycle of the past decade, which generated large returns for the mining industry, governments have been seeking to significantly increase returns from mining. This is certainly true for Africa, which remains the least developed and most prospective region in the world. Seeing the wealth mining has created for many countries in the developed world and realising the potential for their own, and feeling that they insufficiently gained from the boom years, many African nations have been adjusting and reviewing their mining policy and legislations. Unified regional policy initiatives like the African Mining Vision have sought to guide and support this process.

In parallel local populations, especially around mining operations, have developed higher expectations for both governments and mining companies to deliver greater, tangible local returns.

The policy adjustments deployed over the past few years have sought to increase the 'local take' through a variety of measures. These mainly encompass:

- Introducing greater automaticity, transparency and disclosure of requirements on mining regulation, licensing and government-companies' contracts;

- Increasing direct taxes and royalties, and introducing measures to combat practices that decrease local tax receipts;
- Restricting foreign ownership and requiring meaningful percentages of the ownership of mining companies to be 'indigenised'/localised;
- Mandating local socioeconomic development and environmental investment in support of communities directly affected by mining; and
- Making some form of local beneficiation compulsory in support of industrialisation, mainly through the imposition of export levies, restrictions or bans on unrefined/unprocessed ores and minerals.

The requirement for a 'better deal' out of mining represents a necessary and legitimate aspiration, and one that is supported by the record profits registered by the mining industry globally during its best decade ever. Many of the measures imposed by governments address critical issues, notably around the macroeconomic impact of mining (Dutch disease, for instance), the fiscal leakages that result from questionable tax practices, and the negative legacies of mines long after they have shut down, among many others.

1.2. The rock and the hard place

At the same time, the mining boom has dissolved into what looks like a new commodity bear of low prices, loss making industry, and tumbling investment in prospection and mining. Market fundamentals are not looking good.

In a sector that is highly capital intensive and requires long development cycles, finding the balance between social and capital returns is a difficult exercise even at the best of times. In downturns it is simply perilous. For all actors the stakes are high:

- Not enough benefits for governments, employees and communities will lead to potentially damaging income losses (fiscal revenues, wages, etc.), the wasting of mineral rents, and huge associated socioeconomic opportunity costs;
- Conversely, too much pressure on mining companies will lead to no less damaging loss of investments, mine closures, and the sterilisation of mineral rents, also with huge associated socioeconomic opportunity costs.

For some time now, analysts have warned of slowed growth in resource rich countries – especially those with less competitive mining taxes, legislation and policy environments – as investors face limited capital resources and become increasingly risk averse.

Governments have clearly been struggling to adapt to this challenge and balance their conflicting obligations in a fast moving environment:

- Recently, countries such as Botswana, Zambia, and Zimbabwe have started to soften some of their policies in response to market pressures;
- Others, such as the Democratic Republic of Congo (DRC), South Africa and Tanzania continue to seek ways of increasing their share of mining benefits.

The section below explores some of these developments.

2. Recent policy developments

2.1. Softening stances

- **Zambia**: in an unexpected about-turn, in April 2015 Zambia backtracked on the royalty and tax increases it had implemented in January 2015 – a development that had been received with much surprise as Zambia had been considered a success story in investment climate reform, and had been rewarded with much investment and improved production in its copper sector:
  - In January, Zambia implemented major changes to taxes applicable to miners. Royalty rates on open-pit mining increased to 20% from 6%, and to 8% from 6% for underground mining; a new 30% corporate processing and smelting tax was introduced as well as a 30% tax for tolling income.
  - However, in the face of underwhelming commodity prices, industry players applied pressure on the Zambian government to review the policy.
  - As a result, recently elected President Edgar Lungu directed his Mines Minister Christopher Yaluma and Finance Minister Alexander Chikwanda to consider options to resolve the impasse.

  - In April, the Zambian government introduced amendments to the mining tax regime and reduced royalties and taxes to a more sustainable level – reducing the gross royalty on open pit mines from 20% to 9% along with the reintroduction of a 30% corporate income tax and a 15% variable profits tax.
  - Zambia's attempt at receiving a larger proportion of mineral rents was perhaps hasty in light of recent economic realities. From the onset, Zambia's chamber of mines had concurred that the January tax changes would disrupt the government's objective of increasing revenues. Fitch Ratings Ltd. had forecasted that growth would be so negatively affected that the local economy would expand at the slowest pace in 13 years in 2015. While Zambia's review has been widely welcomed and will help avoid further loss of earnings, it has been a costly exercise. The now relaxed rules mean that the government owes US$600-million in value added tax (VAT) refunds to mining firms such as Glencore and Vedanta Resources. As a result, Zambia's Mopani Copper Mines (MCM), majority owned by Glencore, announced that it would delay the construction of a planned copper processing plant until the government refunds US$300-million in VAT.

- **Zimbabwe**: in a similar move Zimbabwe's government has recently taken steps to lighten the burden on the struggling local mining industry:
  - In April, the country suspended a 15% tax on diamond sales. Zimbabwe's diamonds have traditionally been easily extractable through open cast mining. However, as those sources deplete, miners have warned that the tides are changing as they lack the technology and expertise to access the deeper diamonds.
  - In May, Zimbabwe lifted a 15% tax on un-beneficiated exports, allowing platinum miners to resume exports of concentrates.
  - In June, Zimbabwe lifted a ban on chrome ore exports, revised royalty fees for chrome ore from 2% to 5%, removed a 20% export tax and lowered power tariffs for chrome producers. Mines Minister Walter Chidakwa acknowledged that the four-year ban had failed to stimulate the local industry amidst outdated equipment, weakening prices and unsustainable energy tariffs.
  - Following these developments, in July, Chidakwa announced that Zimbabwe would be overhauling its mining legislative regime, replacing it with one that would be fairer to investors and would bring a 'win-win outcome'. The two-piece legislation will reportedly be simpler and offer tax incentives for those willing to beneficiate locally.
  - These recent policy decisions, in a country that has played a pioneering role in pushing for beneficiation, are indicative of how governments across Africa are struggling to retain mining investment while seeking to derive greater socioeconomic benefits from the sector. However, the recent lessons learned in Zimbabwe might result in it paving the way for the rest of the continent.

- **Botswana:** in a characteristically pragmatic move, Botswana has deferred payment of royalties for copper mining companies:
  - Botswana deferred copper mining companies' payment of 3% royalties for a year. The government has warned that following a review in a year's time, a decision on payments would be made depending on market recovery.
  - The country, which has become one of Africa's most developed nations on the back of its diamond resources, has admitted to finding diamond beneficiation challenging.
  - In June, Diamond Hub executive Mmetla Masire said that a number of the diamond cutting and polishing factories were downsizing or liquidating owing to a narrowing price margin between rough diamonds and polished diamonds.
  - Masire acknowledged that Botswana had not fully appreciated the complexities of beneficiation and that it now had to find a better middle ground.
  - Botswana's softening stance may represent a recognition that 'getting a better deal' is not simply a matter of raising taxes or imposing downstream beneficiation, and will demand a careful balancing act requiring flexibility in the face of changing markets and a sustainable policy and tax regime.

2.2. Stuck in the (uncomfortable) middle

- **South Africa's** Mineral and Petroleum Resources Development Act (MPRDA) is in the hands of parliament, after President Jacob Zuma referred it back to the National Assembly for reconsideration in January, as he believed that the Bill would not pass constitutional muster:
  - Parliament can only revisit the constitutional issues referred to it by the president. While the items deemed unconstitutional have not been published, analysts have speculated which clauses may have been cause for concern.
  - These include a clause that would give government the right to a free stake of up to 20% in any new oil and gas projects, with a right to acquire an additional 80% at an 'agreed price'. Another clause would give discretionary powers to the minister of mineral resources over deciding what minerals are strategic. Other issues that are contentious in terms of international trade law include the export restrictions on strategic or designated minerals, where the minister can compel mining companies to supply minerals for local manufacturing at what do not appear to be full market value prices.
  - As a result of the MPRDA's delay, the Department of Trade and Industry's (DTI) Mineral Beneficiation Action Plan (MBAP) has not been published yet. The main objective of the MBAP is to break down the objectives of the 'beneficiation strategy' into incremental and achievable targets.
  - It is clear that the government is intent on increasing its share of mining benefits – mainly through downstream beneficiation – however, there remains a lack of clarity on how this will be achieved. While the legislative uncertainty has been a source of concern, many also prefer a delayed process if it will ensure a better regulatory regime. It is important to note that this discussion is taking place at a difficult time for the governing party, the African National Congress (ANC), which has seen reduced electoral support, is being pressured from the political left, and is dealing with a declining mining industry and lower commodity prices.
- In the **DRC** the government has recently announced it would re-open talks on the new mining code:
  - In March, the mines ministry submitted a draft version of the new mining code to parliament; the review process is ongoing.
  - A number of provisions have caused some anxiety in the mining industry. These include the inclusion of more provisions governing the interaction with local communities, an increase of the state's free carry participation from 5% to 35%, an increase of royalties (a draft in April 2013 mentioned royalties on copper at 6%, other sources have mentioned 4%, against a current rate of 2%); and an increase of taxes (including an increase of the corporate income tax from 30% to 35%).
  - Responding to the industry's concerns, the President of the National Assembly, Aubin Minaku, communicated to the Congolese Business Federation (FEC) that he considered additional consultation with industry representatives "an indispensable imperative." Additionally, Moise Katumbi – the governor of the copper rich Katanga province – has openly warned against significant tax hikes amid the recent decline in copper prices.
  - It is worth noting that the discussion around the new mining code has been ongoing since 2012 but has seen consistent delays due to political instability and the industry's negative response to it. Furthermore, President Joseph Kabila is reportedly seeking an unconstitutional third mandate at next year's elections, and is attempting to delay the elections. Reopening the debate on the mining code may be one way for Kabila to achieve this, and he might attempt passing the legislation just before the elections are due.

2.3. Hardening stances

- **Tanzania's** mining sector is set to continue to struggle as a result of its high taxes and royalties:
  - Over the last decade, Tanzania has enjoyed a steady average annual GDP growth of between 5% and 7%. The contribution of the mineral sector to the GDP stands at 3.5%, a number which the Tanzanian government would like to see grow in the coming decade.
  - In 2008, UNCTAD's World Investment Report showed that foreign direct investment (FDI) had significantly increased, ranking Tanzania as one of the top non-oil African countries in terms of FDI receipts. This was fuelled by the 'opening up' and development of the

country’s mining sector. Mineral resources, particularly gold, have contributed to the country’s rising GDP.

- In 2010, Tanzania introduced a new mining code, following many local complaints that the sector was doing little to alleviate poverty. The code raised taxes and royalties and included a free carry interest and state equity participation, making Tanzania’s mining legislation one of the least competitive in the region.
- As a result, earlier this year the BMI report, ‘New Market Research Report Tanzania Mining Report Q1 2015’, forecasted that Tanzania’s relatively burdensome mining code combined with the global gold price plunge would discourage investment and affect the growth of Tanzania’s mining sector up to 2018.
- In addition to the mining code, the government further weakened investor confidence through retroactive application of the new royalty rates (which continue to be contested), and slow administrative processes. A number of other aspects are undermining the government’s growth ambitions, including infrastructure bottlenecks, significant electricity supply challenges, high dependence on external aid and the fact that the new growth sectors tend to act as enclave economies with little employment generation. This comparatively uncompetitive investment and operating environment is unlikely to see improvement until after next year's national elections.

END OF REPORT

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