Crisis point

South Africa's government must reassess policy priorities and resolve regulatory issues

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The Arnot power station

Photo: Gerhard Roux

South Africa is Africa's mining giant. In 2010, the country's mineral rent stood at an impressive US$16.6 billion in the dollar value of the year 2000.

The Democratic Republic of the Congo (DRC) and Zambia, Africa's other large mining economies, generated resource rent of around US$1.4 billion each in 2010, less than a tenth of South Africa's. Altogether, South Africa's rent accounted for 65% of Africa's total.

Giving jobs to more than 500,000 people directly, the sector contributed more than US$35 billion in exports of primary minerals, and constituted the largest source of foreign exchange to the country. A further US$11 billion of primary minerals were sold locally for processing. The industry's local expenditures are high, standing at more than US$50 billion in 2011, and are responsible for another 800,000 jobs throughout the economy.

Growing crisis

Yet, beyond the impressive statistics, the country's mining economy has been confronted with a growing crisis over the past few years, one which some analysts now call a crisis of survival.

Last year, dozens of miners were killed by police during a violent strike that saw others brutally hacked to death. The then African National Congress (ANC) Youth League leader Julius Malema also made threats of nationalisation.

While both the ruling ANC and the government have taken great pains to stabilise the situation and reassure investors, notably through a commitment against nationalisation, the damage has already been done. Investments, production and profits have been under pressure despite bumper commodity prices until 2012.

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Until 2007 the country was the world's leading gold producer. The combination of policy uncertainty, regulatory heavy-handedness (notably on safety), electricity supply constraints, rapidly rising energy and labour costs (and now labour instability), and declining grades, have led South Africa to drop to sixth place. A dismal performance.

Platinum group metals (PGMs), another leading source of mineral rents and employment in the country, have been battered by labour unrest, with production having declined in 2012-2013, forcing the main producers to undergo profound restructuring in an oversupplied market.

However, this restructuring has been threatened by the possibility of further labour unrest and by a government intent on preventing job losses. The government is mooting regulation allowing the minister of mineral resources to set aside a share of production for local transformation (so-called beneficiation) at determined prices.

The ANC and government believe that the country's large share of PGMs, which is more than 80% of global reserves, provide it with a monopoly, which would allow it to dictate pricing conditions.

Coal is also under pressure. Considered a strategic asset since the country relies on it to fuel electricity production under monopoly by parastatal Eskom, the sector has also been targeted for Black Economic Empowerment (BEE), a policy that seeks to advance the rise of a Black capitalist class.

BEE has often served to promote the politically connected elite, and is contributing to supply constraints due to a lack of capital and technical capacity – together with regulatory and pricing uncertainty. The country now faces what some have called a "supply cliff", which threatens the government's entire electricity production strategy, despite new coal discoveries in the north of the country.

Downstream difficulties

The situation is also challenging for downstream industries. Rand Refinery, the world's largest gold refinery, is looking to both diversify its products and set up operations overseas as gold production declines and costs increase.

South Africa has recently lost its position as the world's leading ferrochrome producer due to electricity supply constraints, with, power utility Eskom taking the extraordinary step of buying back power from businesses that has been sold through long-term agreements.

The result has been the loss of over 100,000t of production over the past few years. All of this contradicts government policy that seeks to encourage industry to beneficiate more.

Fast-rising input costs are not new, but have been let loose and led to unrealistic expectations by labour unions that compete against one another for members. Electricity policy often works at cross-purposes to the government's mining policy. Critical transport projects are costly and slow to come about.

In this context, the government needs urgently to reassess its policy priorities and resolve regulatory uncertainty by eliminating administrative discretion, improving licensing procedures, opening the energy and infrastructure markets to private operators, and addressing unrealistic labour expectations. If it does not, South Africa's mining industry faces a future of steady decline. ▼

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