The impacts of 15 years of mineral policy on the performance of South Africa's mining industry and how to manage country/political risk and drive positive mineral development strategy

27 June 2019

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Eunomix, advisors in resilience

Eunomix is a trailblazing consultancy delivering resilient solutions in the face of uncertainty and disruption. Our offering enhances risk management, strategy and responsible growth.

We are experts on emergent nations and markets, with proficiency in resource-rich countries and fragile states, and a deep focus on Africa. Blending economics and political science with strategy, risk management and communications, we have extensively worked in mining and extractives, infrastructure and transportation, and manufacturing.

- We assist corporates manage exposure to country risk and investment climate, and deliver opportunity in a responsible manner toward shared value. Our work is focused on corporate strategy, scenario planning, enterprise resilience and risk management.
- We work with governments toward sustainable investment, growth and empowering socioeconomic development. We support investment climate improvement, develop growth strategies and special economic zones, conduct sectors and clusters development, and help investment projects come to fruition.

Founded in 2009 Eunomix, has become a reputed advisor and a trusted voice, providing advances in analysis and action through innovative and rigorous approaches.

Beyond consulting, we seek to contribute to the quest for resilient and sustainable societies through research and engagement. **Eunomix Research** is a specialised division dedicated to contributing to public policy and corporate practices that impact the growth and development of countries and their communities. Eunomix Research does this by conducting and distributing research that has public value, is original and of the highest standard.

Claude Baissac is a recognised specialist in strategy, risk management and economic policy.

He has over 20 years of executive and consulting work with corporates, governments and international organisations.

He is the CEO of Eunomix.

1 | Policy and the performance of mining in South Africa

- Last year Neal Froneman commissioned Eunomix to conduct an independent analysis of how mineral policies drive the operational, performance and investment decisions of mining producers.
- Specifically how government and producers, but also other key stakeholders such as labour unions and communities, may engage productively on setting the objectives of mineral policy and on measuring and monitoring the effectiveness of such policy in a dynamic domestic and international context.
- Conducted with the purpose of supporting deliberations on the Mining Charter. It was submitted to the South African Department of Mineral Resources as part of the process of public consultations that concluded at the end of August.


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Mineral policy impact on South Africa's mining sector

An economic analysis

31 August 2018

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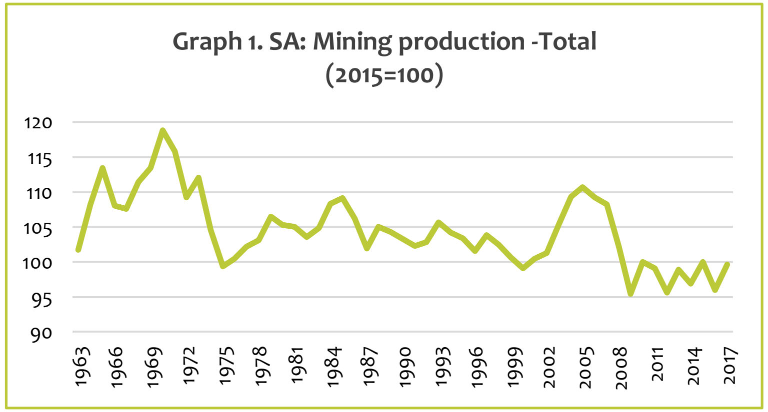
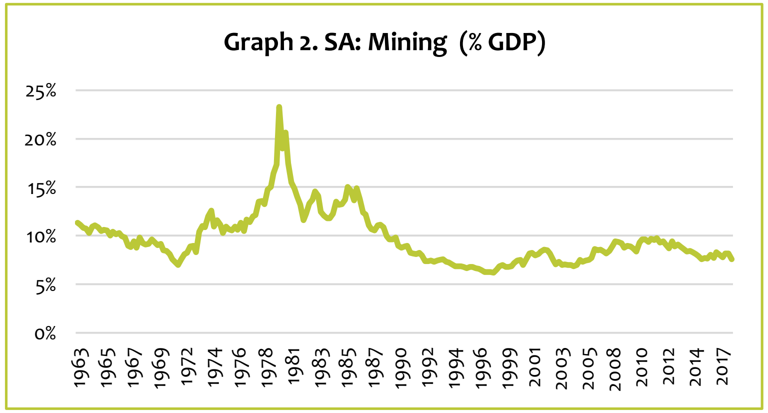
Download the report at:

https://www.eunomix.com/our-work.php

<u>Political events such as the Charter change the market, exacerbating external impacts of commodity prices:</u>

- Pre-2002, mining tends to focus on production, and less on long-term investment
- This reverses after the 2002 iteration of the Charter, when the market was shocked, but recovers somewhat after the 2010 iteration
- The fragility of the economy increases after every iteration of the Charter, a strong political effect, but is more pronounced after the 2002 iteration
- This is reinforced by a worsening relationship with labour and a "flip-flopping" perception of government effectiveness and regulatory quality, including when measured against the political capital metricmacro economically inefficient
- This also implies a higher state burden to "spend out of the problem", as seen in reversing correlations for the budget deficit and subsidy responsibilities





Policy interventions change the market in inefficient ways:

- Operational and financial performance are precursors to investment, and interventions that constrain operations are macro economically inefficient
- Correlations with exports, FDI, employment, investor and consumer sentiment, and the commodity indices generally switch correlational relationships and in many cases weaken
- Rents'/returns correlations generally turn from overwhelmingly positive to mixed, especially GFCF, budget deficit, etc. – the economy is more fragile, macroeconomic events exacerbate negative sentiment, and interventions constraining operations become macro economically inefficient
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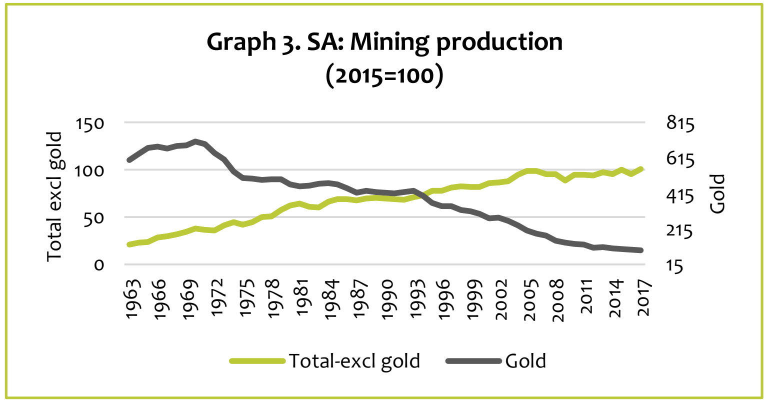

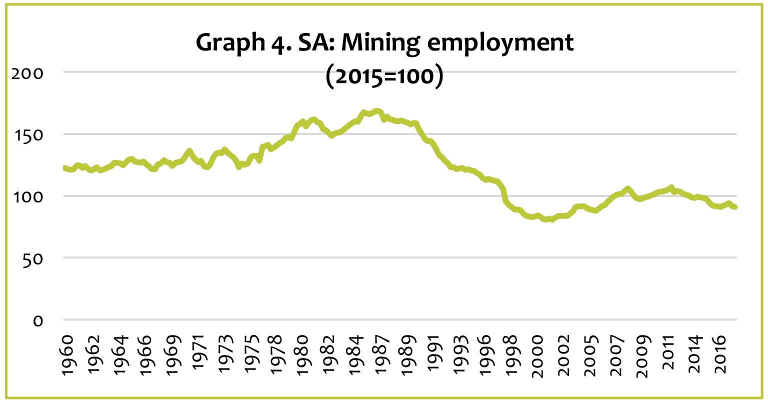

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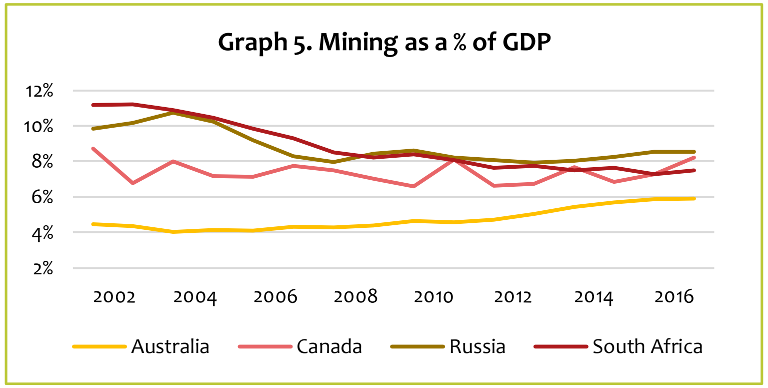
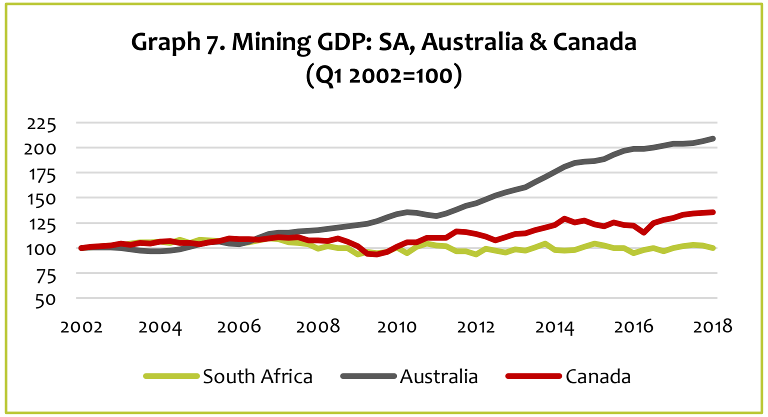
Policy interventions appear to fail to achieve on their main objectives:

- A primary mandate of the Mining Charter is to use a strong industry as a redistributional foundation for national transformation and development
- From the rejection of Hypothesis 2, inefficient distribution of resources is harmful to industries that function in certain market environments
- The mining industry is currently not as strong an industry as currently politically believed, with many externalities that are negatively affecting future operation expectations
- This in return has a negative impact on the breadth and depth of the industry's transformation and contribution to national development

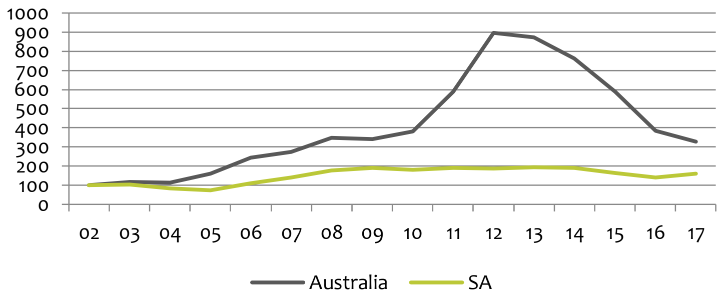




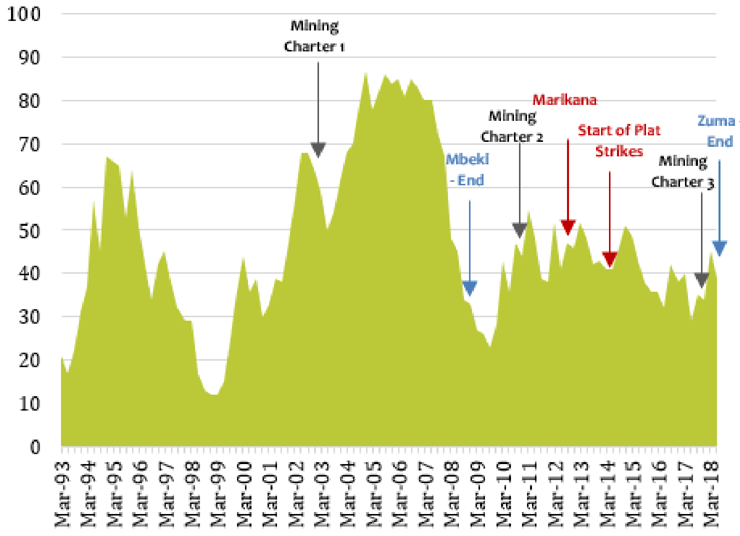
Implications:

- Our research results indicate a strong likelihood that policy interventions as currently in place will lead to the continuous decline of the South African mining industry. As a result South Africa will remain an underperforming international mining jurisdiction, well below its potential.
- Crucially, these interventions will also fail to achieve their transformational mandate as the role of mining continues to decline, and its overall impact on the economy and national socioeconomic wellbeing decreases.
- Our projections of the future performance of the South African mining industry, conducted as part of our research, confirms this. Excluding the possible future impact of the planned Mining Charter, we anticipate no improvement in this performance. Looking at the critical employment contribution of mining, we expect a near-term loss of over 40 000 direct jobs, with the negative attendant socioeconomic consequences that this would bring.

Graph 8. Mining investment: SA vs Australia (2002=100)



Graph 9. BER Business Confidence Index



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South Africa’s performance and trajectory

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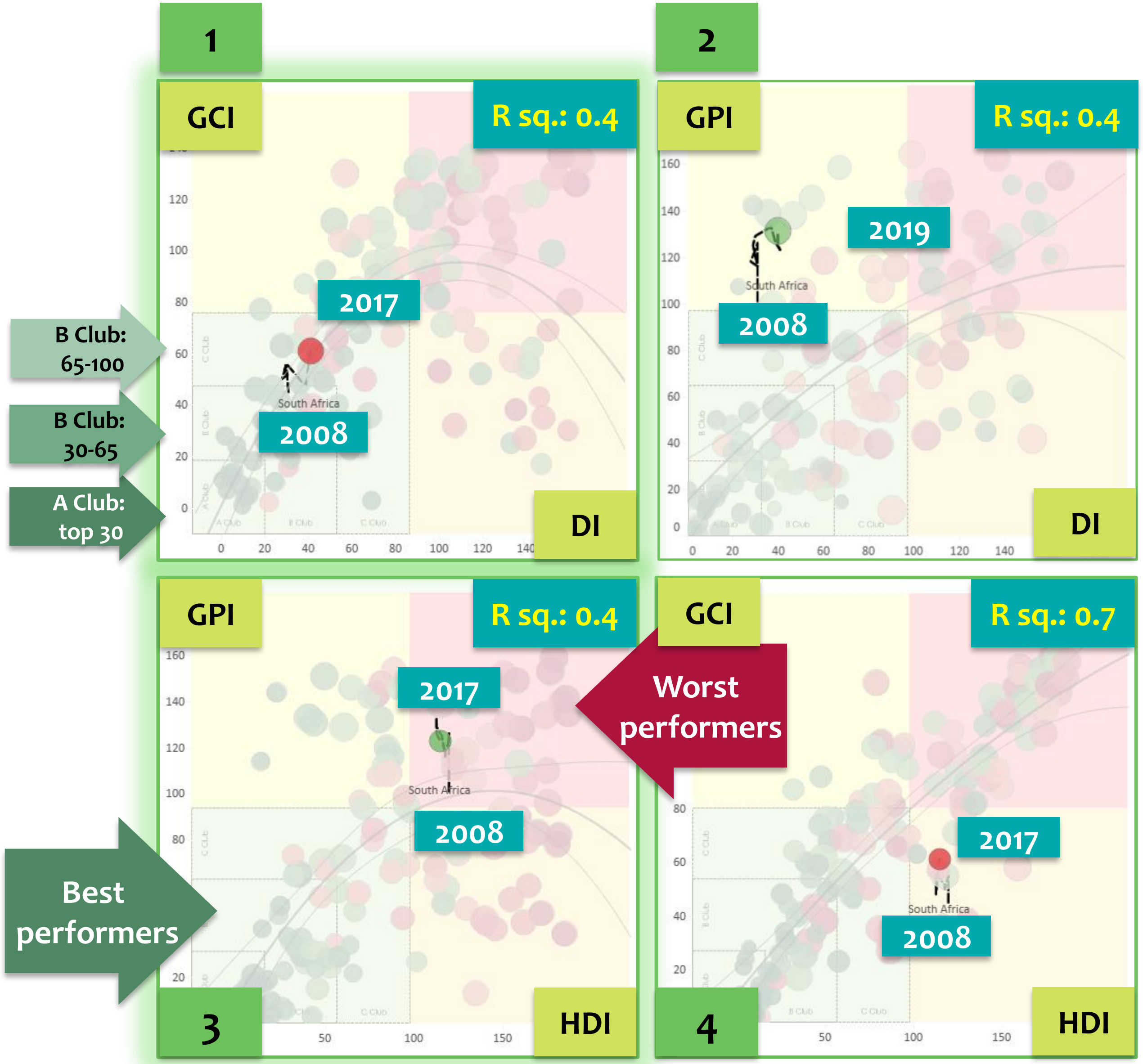
South Africa in the indexes – 2008 to 2019

South Africa belongs at once to better performing and worst performing country groupings, but as declined in all performance indicators

- In 2008 SA among the more competitive and democratic countries – Chart 1
- Concurrently been a poor performer in security and welfare – Chart 4
- Since 2008, it has experienced decline in ranking in all but its HDI ranking, where it has stagnated
- Has led to significant changes in the country's neighbourhood. This is a crucial demonstrator of declining performance:
  - In 2008, it was close to Cyprus, India, Portugal and Slovenia
  - In 2017 it was close to Botswana, Colombia, Jamaica, Latvia and the Philippines



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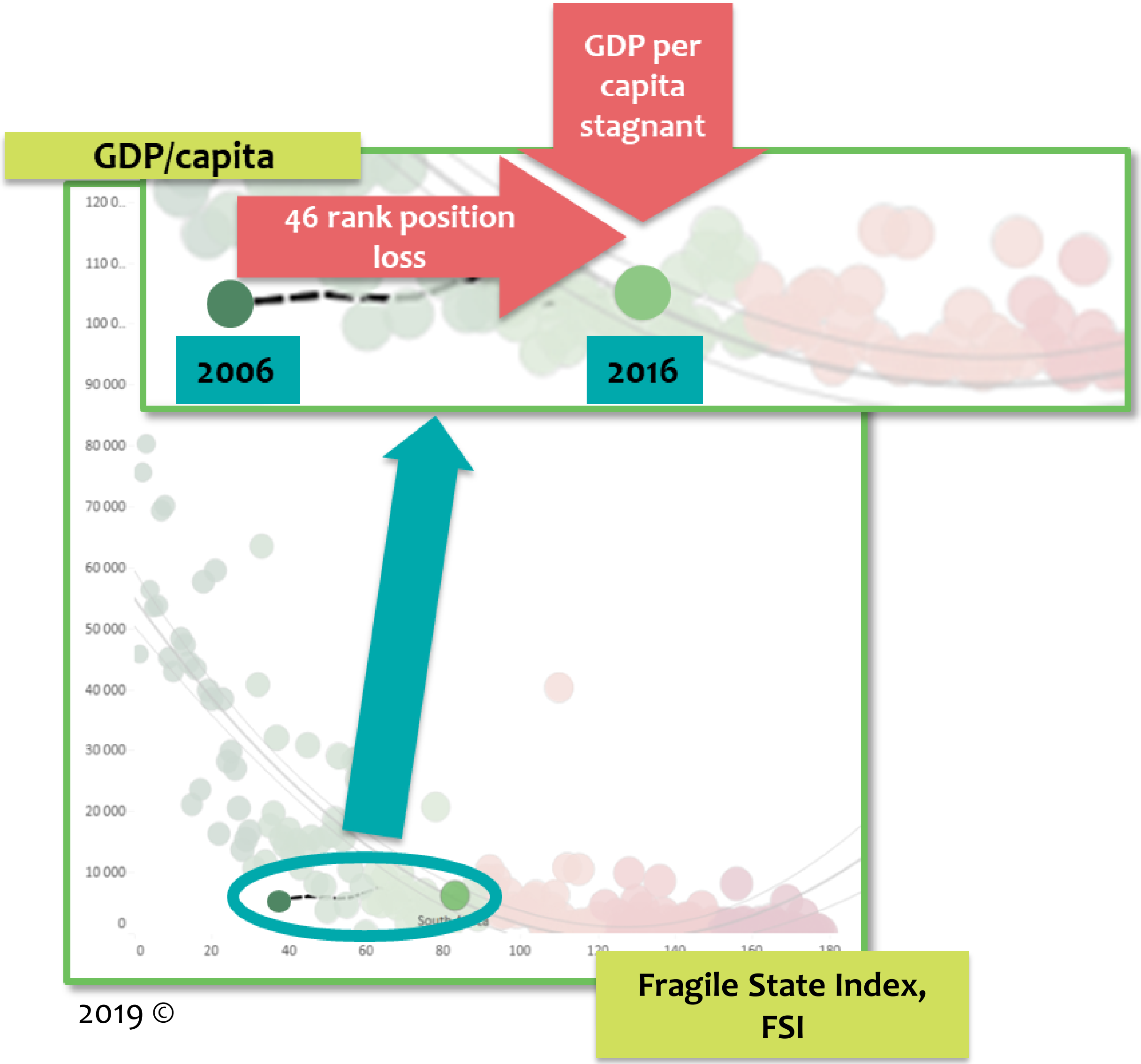
South Africa's exposure to the fragility/GDP per capita "law"

South Africa saw a wide decline in its Fragile States Index ranking, losing 46 positions. This is one of the world's top 10 worst rank losses over the period 2006-2016

- In 2006, SA ranked above average on FSI at 37/178 countries. GDP/C stood at USD5,500
- In 2017 ranked average at 83/178. GDP/C rose marginally to USD 6,200
- This rank loss is not much lower than that of conflict-afflicted countries like Mali, Ukraine, and Venezuela. Of non-conflict affected countries, Brazil and India fared similarly



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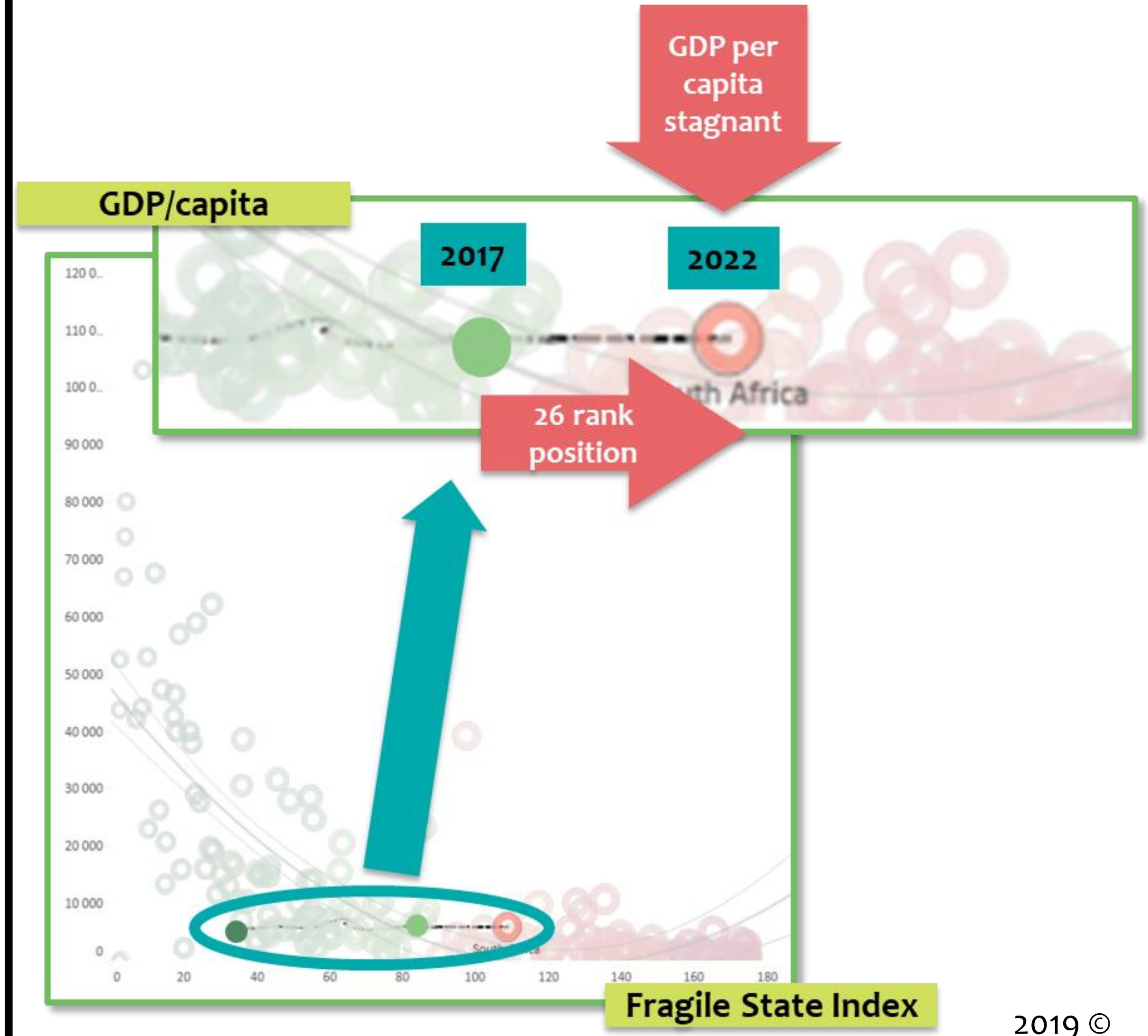
The fragility/GDP per capita forecast confirms

Our forecast shows that if trends remain constant, South Africa will lose 26 rank positions between 2017 and 2022, with no gains in GDP per capita

- This would add to the 46 rank positions lost between 2006 and 2017, with total rank loss amounting to 72
- This would represent a loss similar to those of conflict-afflicted countries like Iraq and Syria – declines in these countries are usually over a short period of time
- In that case, SA would perform worse than the average on FSI/GDP-C
- The country would be a fragile state, highly vulnerable to internal and external shocks

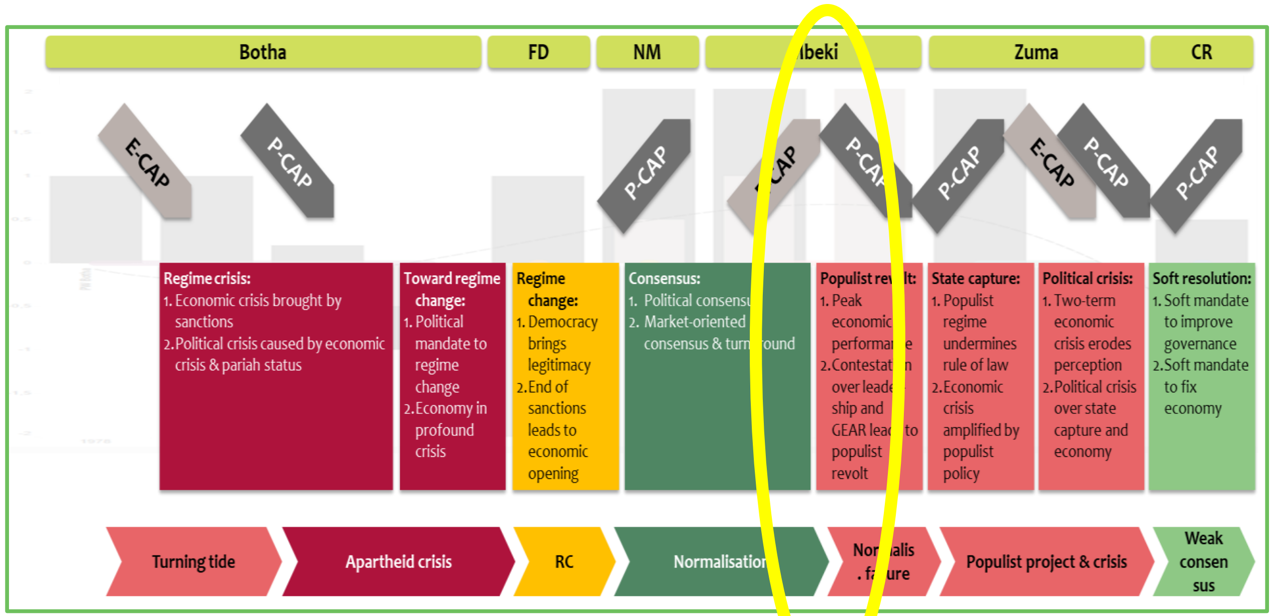


Our scenario for Ramaphosa: if Mandela and Mbeki couldn't do it…

The odds are against Ramaphosa being able to accumulate enough capital to ensure himself against an upset similar to that encountered by Mbeki

- Top scoring scenario is No6, where Ramaphosa gains 0.5 Polcap and Ecocap in 2019 from his 2018 scores, but trends in the post-1994 forecast for both Polcap and Ecocap. His second term is ended in 2024 or 2029 following his/his chosen successor at the ANC elective conference. The 2nd scoring scenario forecasts that he does not increase his capitals in 2019. He is then extremely vulnerable in 2024

The best economic term, which followed 2 terms of economic gains and represented the longest period of growth since the 1970s could not prevent a populist upset. This is a red flag for Ramaphosa, who lacks conditions present in the 1990s



3 Implications

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