

The state of mining in South Africa

Opportunity lost or light at the end of the tunnel?



How does South Africa, once the world's most attractive mining destination, lose its spot on the podium? Could the answer lie in the midst of South Africa's threatening call for nationalisation; the severe labour unrest; poor maintenance of infrastructure; the high levels of perceived corruption at government level and an increasingly tricky Broad-Based Black Economic Empowerment (BBBEE) .. Are the recent downgrades from Ratings agencies and, local mining companies moving their operations off-shore to what are perceived to be more stable operating environments evidence of a mining industry in decline?

Cost of Labour

The 2012 labour unrest, wildcat strikes and poorly orchestrated wage negotiations put South Africa on the map as not only having a highly volatile labour force in the mining sector, but also pinned the country as having a Gordian knot type situation between unions and government. Jurgen Beier, Canadian

Mining Leader for Deloitte says, "labour costs in South Africa continue to be problematic. Even before Marikana, South African labour costs were viewed as being high, largely based on poor productivity and less automation in relation to other leading mining countries."

One of the reasons South Africa was perceived to be an attractive destination in the past was due to the low cost of labour. Organised labour has consequently become more demanding in their remuneration expectations and the country now faces a situation where semi-skilled mining workers earn a higher base income than the majority of University educated graduates. Taking into account the severe health and safety risks, remote and isolated locations and the need to subdue the nationalisation debate, perhaps the higher wage demands can be justified?

Role of Infrastructure

Delegates who participated in the Deloitte

Insomnia Index at the 2012 *Investing in African Mining Indaba*, listed infrastructure as one of the top three challenges when considering doing business in Africa. Although an estimated R4-trillion will be spent over the next 15 years on the South African National Infrastructure plan, the question is how much confidence does the international market have that this investment will be correctly allocated? Recent downgrades by Ratings agencies Fitch and Moody's do not instil the confidence that is required for mining companies, who are forced by the nature of their business models to make long-term investment commitments, to consider South Africa as an attractive investment destination. Glenn Ives, North American Mining Leader at Deloitte says, "South Africa is joining the rest of Africa more rapidly than expected, partly because of the decline in its infrastructure." As South Africa continues to strive to meet its infrastructural demand and reduce its infrastructural deficit, Africa's infrastructure services remain nearly twice as expensive as other developing economies, reflecting both a lack of scale in production and high costs as a result of the lack of competition¹.

Opportunity Lost?

South Africa contains the world's highest *in situ* value of resources², yet global investor appetite continues to be satisfied in other developing countries, where the relative cost, stability and prospects seems more favourable. South Africa also contains the world's largest majorities of commodities like platinum, manganese and chromite. However,

¹ Agence Française de Développement and World Bank: *Africa's Infrastructure: A Time for Transformation*

² Chamber of Mines, Facts & Figures 2010

there is no disputing that South Africa has failed to capitalise on the commodity boom or super cycle, largely as a result of the continued interruption in social, economic, and political development, despite often enjoying what can only be described as 'monopolistic' powers in these commodities in comparison to other countries. It begs the question as to whether South Africa will continue to be perceived by the international mining community as not only the leading mining investment destination but also as the gateway to Africa. As other countries like Ghana – and their attractive growth rates, Botswana – with their continually improving ease of doing business and socio-political stability ; and Mozambique – with their recently acquired coal and gas reserves, continue to put pressure on South Africa as the African mining destination of choice.

Investment Awry

The increasing involvement of the state in the mining industry is a global trend. South Africa has seen its fair share of state involvement with calls for nationalisation and further taxation of the industry. Even the more expensive and mining friendly South America countries have increased their level of state intervention through the introduction of export controls; tighter controls on the issueing of licenses and permits and increased taxes and royalties. Yet South America is forecast to have some of the highest projected mining investment over the next 20 years as a region.³ It seems that international mining investment is not deterred by state intervention, given the projected investment in countries that currently have higher levels of

³ Deloitte: *Tracking the Trends 2013*

government intervention. How is it that South Africa's reputation in the mining industry has taken a turn for the worse? It seems that mining investment is not deterred by state interventions, but by prolonged uncertainty. This is even further exacerbated by the fact that the mining industry has been selected as the most prominent vehicle to deliver governments' socio-economic agenda. This has resulted in significantly higher socio-economic expectations of miners and communities. Combine this with the challenge of sourcing funding for large capital projects, and very quickly the hurdle rate for new investments become insurmountable. Despite funding being considered to be the greatest challenge to capital project expansion in Sub Saharan Africa, South Africa has the lowest estimated average % project cost overrun. It seems that South Africa is perceived internationally as a country that is 'unstable', from a regulatory and labour perspective and that the threat of nationalization cannot be ignored. The combination of these factors will only increase the already high cost of mining in South Africa.

Not all doom and gloom

Whilst South Africa may be considered underwhelming as far its investment potential is concerned, it seems there are a number of positive take-aways that South Africa have to offer the world. Jurgen Beier, Canadian Mining Leader for Deloitte, says "South Africa is still seen by the world at large as a very innovative country and many of the technologies and new mining ideas which originate in South Africa are rapidly adopted

around the world. South Africa contains a large skills base, and is often considered amongst the world's leading countries for mining technology and innovation. As well as being a leading developer of technology and innovation, South African mining professionals are also in high demand because of their capability and experience." Of all the African countries, South Africa's infrastructure is considerably the most highly developed. As infrastructure is highlighted as the biggest challenge to mining investment, it puts South Africa in a highly favourable position. Whilst the South African mining industry faces somewhat of a stormy future, it has weathered storms before and will need to harness all the available innovation and resilience in order to once again become a mining destination of choice.

Where to from here?

How does South Africa go about navigating this storm? The key seems to lie in changing the existing perceptions of both foreign and local investors of the South African mining industry.. Phil Hopwood, Global Mining Leader at Deloitte suggests three of these priorities to be for government to focus on reducing the risks of foreign investment, implementing a more robust regulatory environment and proving competitiveness in productivity.

With robust project management skills, high levels of innovation and deep mining experience, perhaps the role of South Africa in the global mining industry is slowly shifting away from major resource provider to strategic project advisor.

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