



TRENDS IN AFRICAN MINING DISPUTES

An Industry and Valuation Perspective

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19 November 2020

This afternoon's presentation



1. Questions and observations welcome

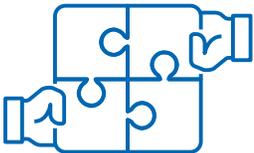
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3. Structure of the presentation

- i. Why is the mining industry so prone to disputes?
- ii. Types of mining disputes
- iii. Regulation issues
- iv. Valuation issues
- v. Outlook





Why is the Mining Industry so Prone to Disputes?

The Mining Sector is...



Cyclical

- Commodity prices are cyclical.
- Cyclical and volatility can lead to the circumstances of partners diverging, increasing the risk of disputes.
- Price cyclicity reflected in the sector's access to capital and strategy (e.g. value vs. growth).



Capital Intensive

- Exploration for minerals tends to be extremely risky – a fact that is often forgotten after minerals have been discovered.
- Large scale investments are required in the early stage of a project's life and once made they are largely to be considered as “sunk costs”.

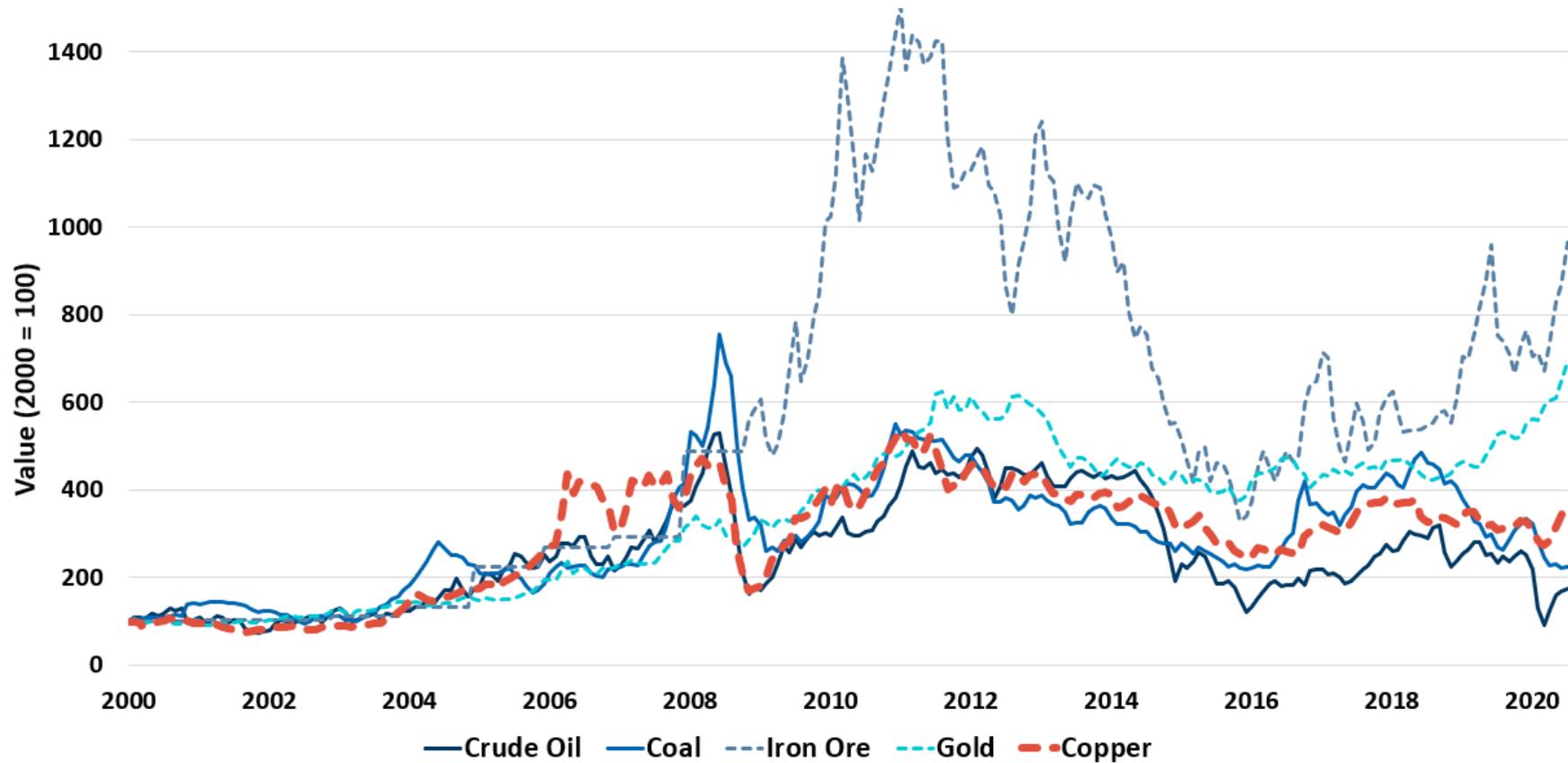


International

- The mining sector is exposed to a range of country and political risks.
- The exposure depends on the countries where minerals are based and the extent of regulation prevalent in that country.

... prone to disputes

The Mining Sector is



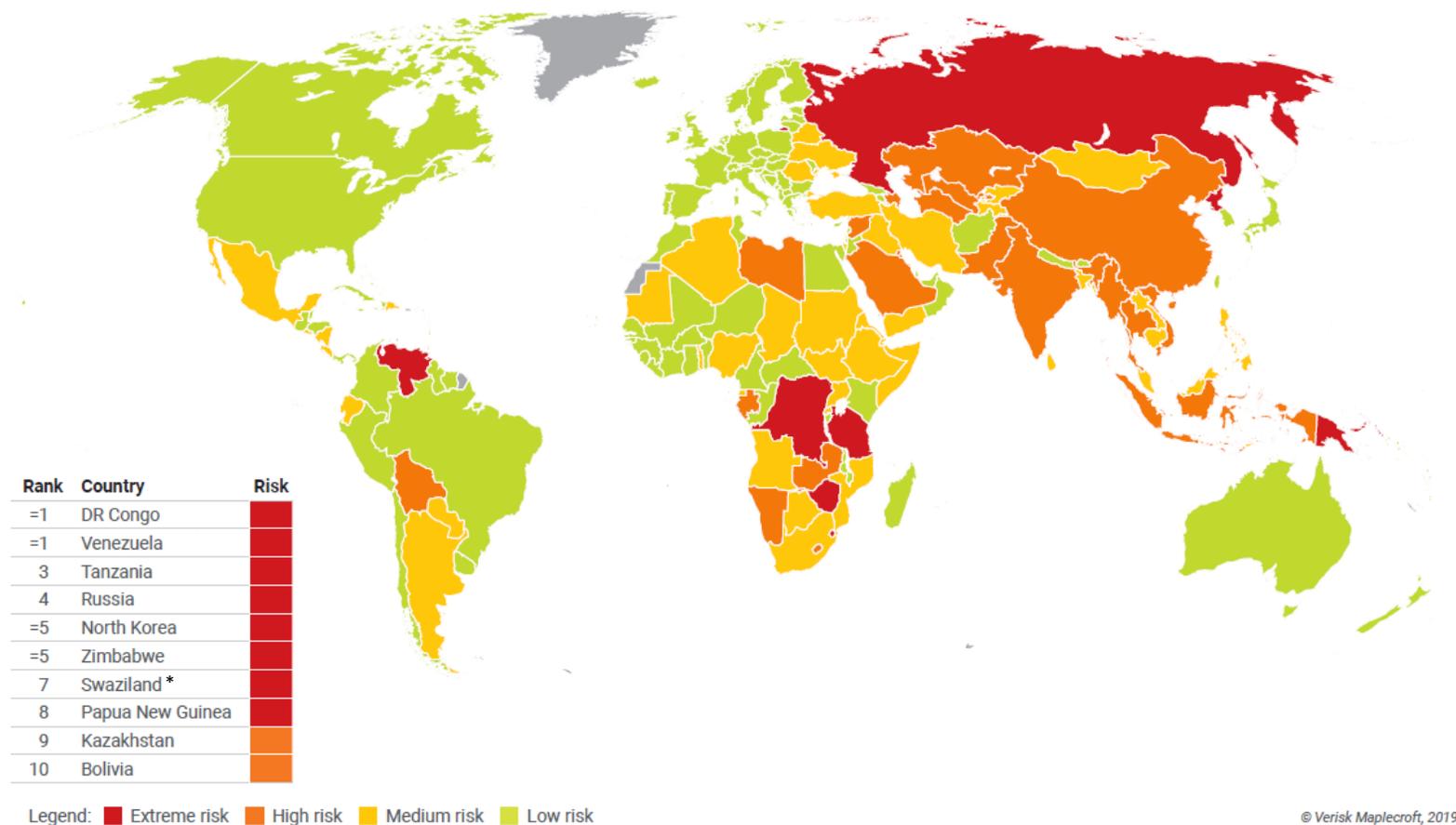
Source: IMF, FTI Analysis

... exposed to significant cyclicality

The mining sector is...



March 2019
Resource Nationalism Index



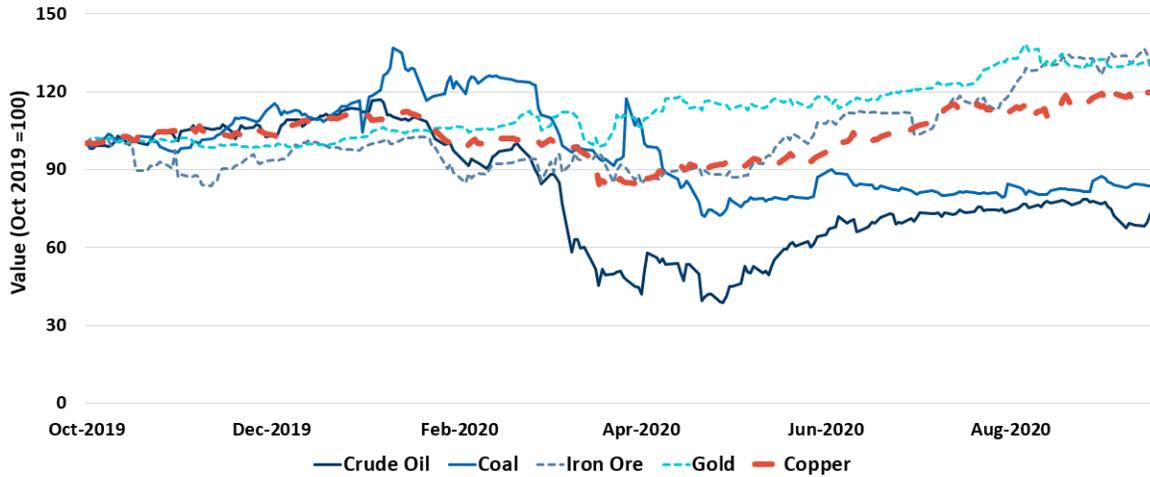
Source: Verisk Maplecroft, 2019

*Eswatini

... exposed to elevated resource nationalism risk

Recent developments in the mining sector

Performance in the past year



Source: S&P CapIQ, FTI Analysis

Zambia Debt Default

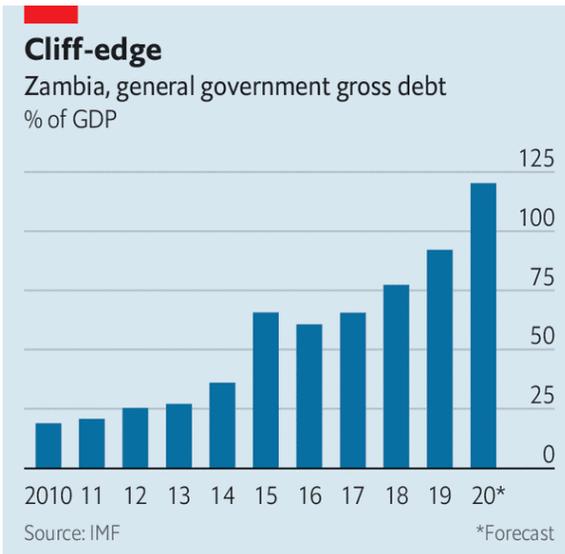


Source: The Africa Report

Vale tailings dam disaster in Brazil



Source: Financial Times



Source: IMF

*Forecast

Source: Economist

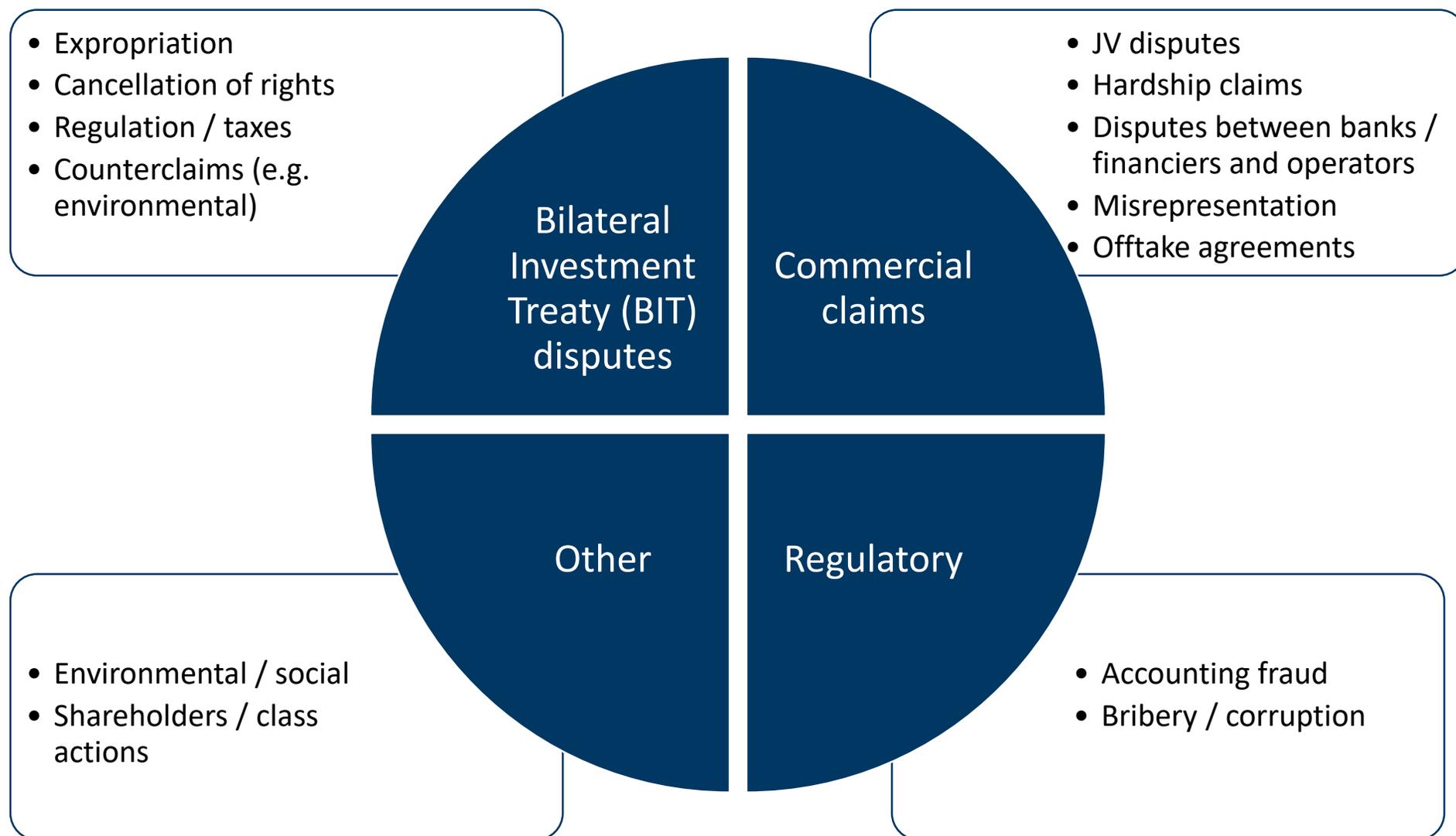


Wrapping up Mining Sector Trends



Types of mining disputes

A wide range of disputes can arise within the mining industry



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1. Number of total shares outstanding as of July 23, 2020, times the closing share price as of July 30, 2020.



Regulatory mining disputes

Mining and regulatory disputes



Regulatory focus

- Impact of Covid-19
- Unprecedented fiscal demands
- Balancing economic recovery
- Increased revenue collection efforts
- Customs declarations, royalties, licence fees and transfer pricing
- Complex matters
- Almost all instances cross-border



Risks, causes and pitfalls

- Lack of administration – especially pre-commissioning of operations
- Use of agents and possible illegal activities between agents and government officials
- Agreements with agents not preventing corrupt activities
- Intermittent functionality (technological) at border posts
- Manual operations at border posts
- Forging of documents
- Corrupt payments
- Incorrect use of import and export tariff codes
- Lack of control – regulatory audits
- Massive assessments – selective and unscientific sampling of documentation
- Could end up in lengthy disputes
- Revoking of licences
- Can manifest itself as life threatening
- Media exposure



Valuation issues

Valuation 101



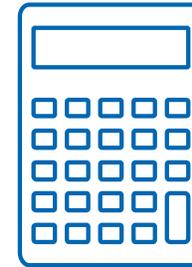
Cost based

- In effect sunk costs
- Recovery of investment



Market based

- Observed transactions in the asset in question
- Observed transactions in similar assets

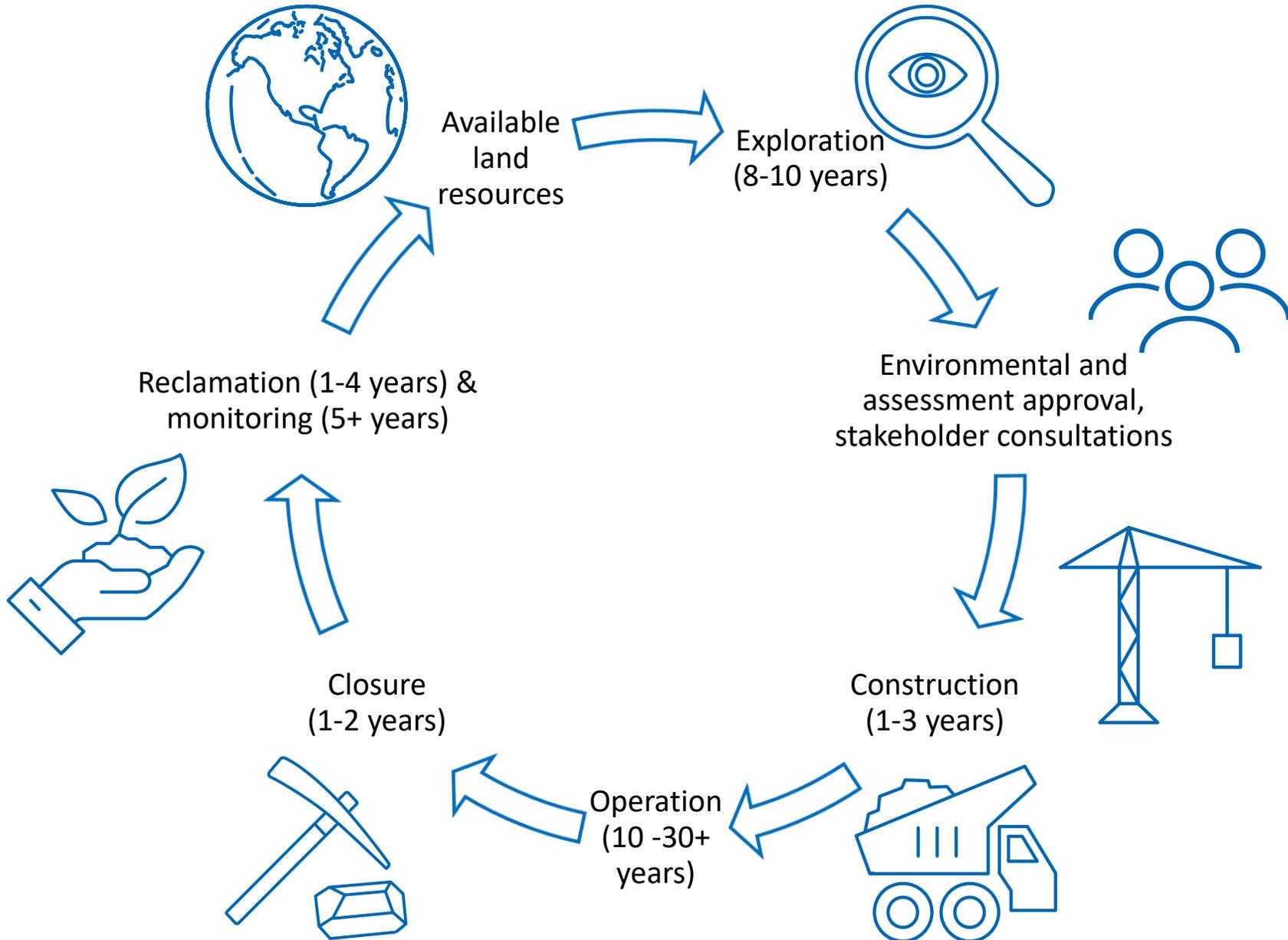


Income based

- Based on finance theory
- Expected cash flows discounted at the opportunity cost of capital (“DCF”)
- Certainty adjusted cashflows (“Modern DCF”), Monte Carlo and real options analysis becoming more prevalent

What makes mining disputes different?

Valuing mining assets requires different methodologies appropriate to their stage of development



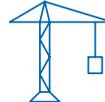
Different stages may require different valuation approaches

E.g. Canadian Institute of Mining, Metallurgy and Petroleum valuation guidelines state that the following approaches should be used for different stages of development

Increasing Information



Decreasing Risk

Valuation Approach	Exploration Properties 	Mineral Resource Properties 	Development Properties 	Production Properties 
Income	✗	?	✓	✓
Market	✓	✓	✓	✓
Cost	✓	?	✗	✗

Industry guidelines provide **possible** approaches



Guidelines not requirements



Standard of value



Judgement required

- Delineation between categories
- Multiple categories
- Data available
- Consistency of data



Track record

Themes, difficulties and points to consider



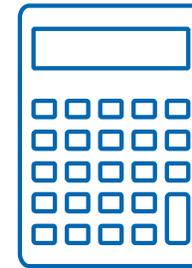
Cost based

- What data is available?
- Project specific costs
- Adjust for risk?



Market based

- Share price not always the best measure of fair market value
- Difficulties in determining comparable transactions
 - Product
 - Scale
 - Point in life cycle
 - Geology
 - Transportation
 - Location
 - Operating parameters
 - Legal hurdles



Income based

- A life of mine or detailed internal forecasts typically required
- Even where financial evidence appears good quality, may require further expertise and input
 - Price
 - Technical
 - Financing
- Optionality?

Some examples

Copper Mesa Mining v Republic of Ecuador (2016) – exploration property

Claimant (Mesa):

- Market-based compensation of USD 70m
- Wasted costs USD 27m in the alternative

Respondent (Ecuador):

- Comparable data not comparable
- Base on share price of Mesa
- Costs fail to reflect the fall in value due to the global financial crisis

Tribunal:

- Methods cannot be *“uncertain, subjective or dependent on contingencies, which cannot fairly be assessed by the Tribunal”*
- Wasted costs awarded (less some deductions to account for claimant’s contribution to loss)

Bear Creek Mining Corp v Republic of Peru (2017) – development property

Claimant (Bear Creek):

- DCF of c. USD 300m
- Feasibility reports + technical expert evidence confirming they were reasonable inputs

Respondent (Peru):

- Insufficiently advanced project for DCF. Not a going concern and lacks history of profits
- “Modern” DCF, share price, wasted costs

Tribunal:

- Despite being in development phase, no guarantee a hypothetical purchaser would gain licences given opposition from community and speculative
- Wasted costs USD 18m

Issues in recent “mega award” Tethyan Copper v. Islamic Republic of Pakistan (2019)

- Claimant assessed damages of USD 8.5 billion (+ interest) using a “Modern DCF” approach
 - Uncertainty addressed in cash flows rather than discount rate
 - Assessed by reference to at-source pricing of risk

- Respondent disagreed with Claimant’s methodology
 - Too uncertain and for long-term price projections, capital and operating costs as well as asymmetric risks, no market based indicator
 - Cost based approach of USD 220 million more appropriate

- Tribunal sided with the Claimant’s methodology
 - Clear that the mine would have been likely to become operational
 - DCF well-established and mode DCF is a variant of that
 - Made certain deductions to arrive at damages of USD 4 billion (+ interest)

- Award recently stayed

Implications of COVID on assessment of damages



Date of assessment more important



Current valuations are likely to be volatile and may quickly become stale



More difficult

- What is the counterfactual scenario?



Valuation uncertainty

- Divergence in forecast views
- Fewer relevant transactions
- Divergence in comparability of companies
- Wider ranges / disclosure?
- How will Courts and Tribunals take this into account?



Thank you

Questions? Now, or later, contact details below



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Johan leads FTI Consulting’s Forensic & Litigation Consulting segment in Johannesburg. He has conducted investigative work in over 70 countries around the world.

He has testified in numerous matters of a civil nature in arbitrations, civil Courts and Criminal Courts. Specific matters of arbitrations were dealt with in Dubai, South Africa, Sweden, Tanzania and South Africa where he assisted as an expert.

He has significant experience conducting investigations, and consulting in litigation matters and financial crimes, in many industries including mining.



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Jim has over 30 years’ experience of valuing mining companies and projects in addition to experience in operations and as a consultant. He has visited and evaluated mining projects in all major mining centres of the world with a focus on the emerging market regions, including West and Central Africa, South America, and Central Asia.

Before joining FTI Consulting, he was a mining equity analyst at Canaccord Adams, Renaissance Capital and RFC Ambrian.



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Henry Pannell is a Chartered Accountant and expert witness. He specialises in providing expert financial advice in international arbitration, domestic litigation (primarily in the UK and South Africa), and competition matters.

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