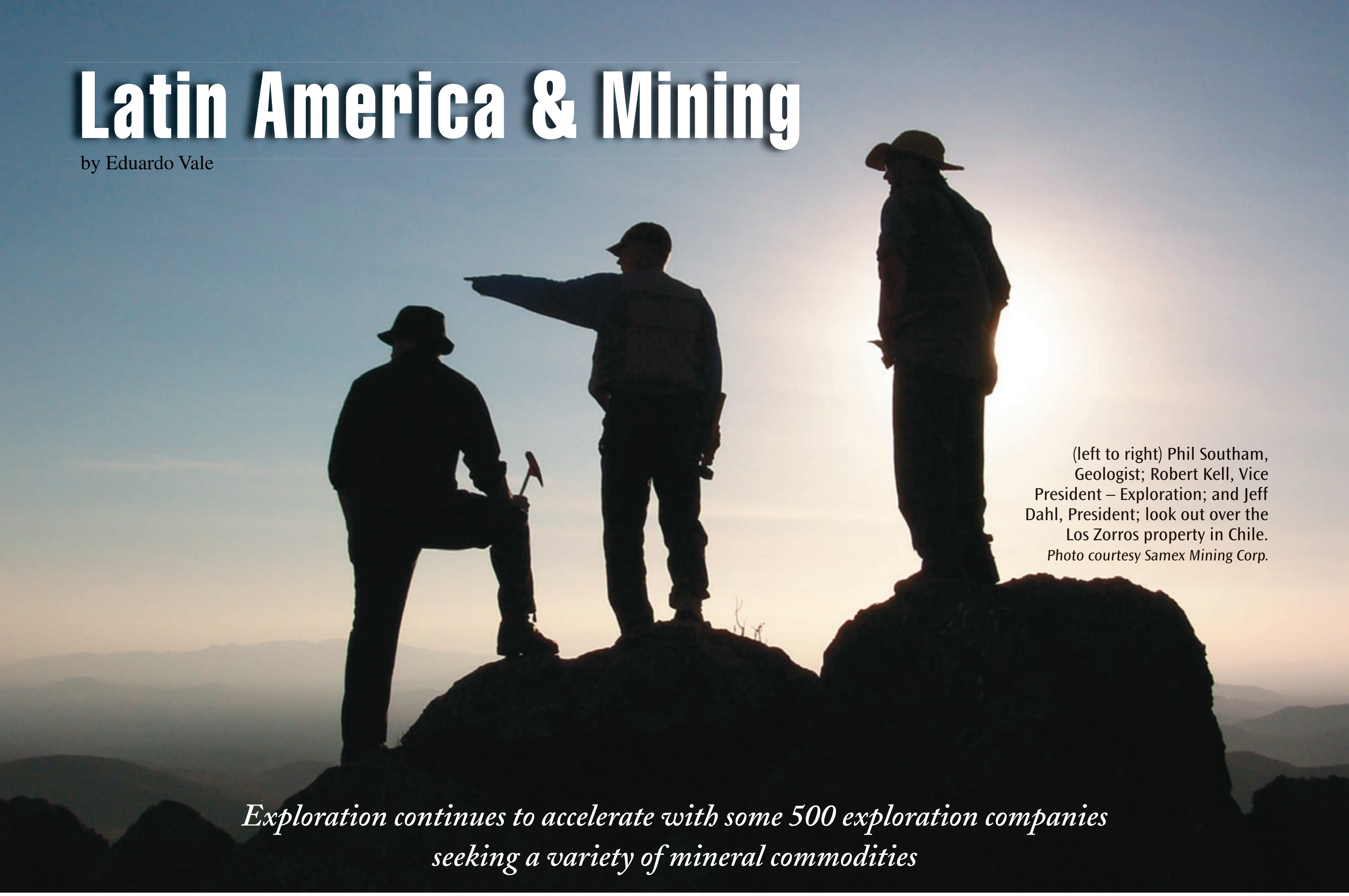
Latin America & Mining

by Eduardo Vale



(left to right) Phil Southam, Geologist; Robert Kell, Vice President – Exploration; and Jeff Dahl, President; look out over the Los Zorros property in Chile.
Photo courtesy Samex Mining Corp.

Exploration continues to accelerate with some 500 exploration companies seeking a variety of mineral commodities

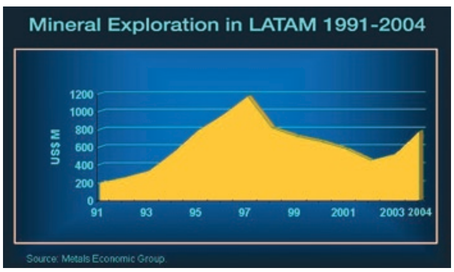
Traditionally, Latin America (LATAM) has been characterized as a region with great potential and opportunities. However, there are so many challenges, major social and economic inequalities and strong political instability that have been exacerbated, on several occasions, by a dubious political sympathy toward foreign investment. In fact, the history of some countries is permeated by cases of conflict with foreign mining companies.

When focusing from a mineral viewpoint, LATAM has long been recognized for its abundant geological wealth and potential despite the scarcity of appropriate geological information over large areas. Its world-class resources and reserves of silver, copper, nickel, niobium, zinc, iron ore, manganese, bauxite, tin and gold, not to mention a comprehensive suite of industrial minerals and fuels, support this statement. However, the remarkable mineral production growth and achieved status as the most prominent region in the current portfolios of mining companies can be traced back to the early 1990s. This period configures noticeable discontinuity in the general investment climate in the region, especially in the mining industry. Parallel to the diminishing attractiveness of the mining business in traditional centres, several Latin American countries began implementing an important set of macroeconomic and sectoral policies aimed to competitively include their economies in the global economy.

At the level of the mining industry, a comprehensive revision was launched of the legal and taxation rules and procedures in place. Despite the differences in intensity and timing, this concerted movement was observed in a large number of countries, such as Argentina, Bolivia, Brazil, Chile, Ecuador, Mexico and Peru, for example. A common trait of consensus set into the renewed national mineral policies was the strategic role given to the mining industry as a vector for achieving higher levels of social and economic development. A good example of this commitment was the mineral policy of Argentina and Chile, conceiving taxation stability regimes for selected projects.

CURRENT MINERAL STATUS

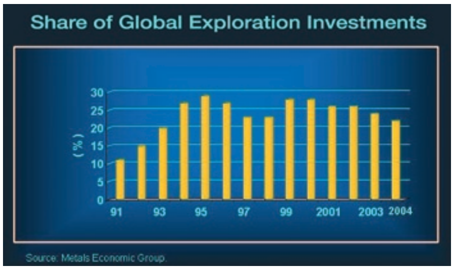
According to research conducted by the Metals Economic Group, in the 1991-2004 period, the accumulated capital allocated to mineral exploration in LATAM was US $8.8 billion, representing about 24% of total global investments. The figure below shows a profile of the behavior of the regional series of exploration investments.



During that period, regional investment jumped from US $200 million in 1991 to US $781 million in 2004, indicating an 11% average growth rate. This accelerated pattern compares with a much lower growth rate - 5% - found for exploration investments at a global level. It is timely to comment that during the 1991-1997 period, the regional growth rate was 34%. As a result, the Latin American share progressed from 11% in 1991 to 29% in 1995 – the highest level recorded – and since then has been oscillating in the 22%-28% range. In 2004, the relative participation of the region was 22%. Despite this drop, LATAM has stayed in the regional leadership with four countries - Brazil, Chile, Mexico and Peru – among the top 10 global jurisdictions in terms of exploration budgets for 2004. These countries represented a combined investment of US $584 million, representing 75% of the regional investments and 23% of the total amount invested by the 10 major countries.

In absolute terms, the regional peak occurred in 1997 with an investment of US $1.2 billion (23%). In the 1997-2002 period, reflecting the impact of an range of forces on the gold market – Bre-X, Central Bank policies, dot.com IPOs, hedging, etc. – there was a considerable reduction (62%) in regional exploration. At a global level, the drop was more intense (66%), with global investments in 2002 at the same level as for 1993: US $1.7 billion. The following figure shows a profile of the relative share of Latin America in global exploration investments.

Nowadays, the number of exploration companies going shopping in Latin American prospective regions



is about 500, a strong sign of its attractiveness. On the other hand, a good reference for the potential of the region is also suggested by the consolidated position of its principal mining countries in the ranking survey prepared annually by The Fraser Institute. The last edition, 2004-2005, embracing 64 jurisdictions, included three Latin American countries – Chile, Mexico and Brazil – among the top 10 for the Current Mineral Potential Index. When considering the Composite Policy and Mineral Potential Index, the region representation now has four countries with the inclusion of Peru. Moreover, for this last index when considering the first 13 jurisdictions, LATAM scored five countries with the inclusion of Argentina.

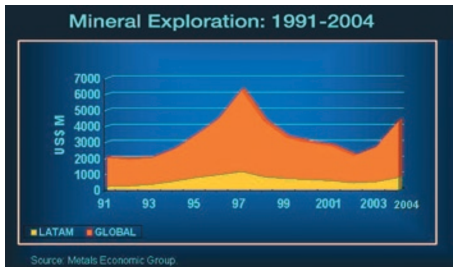
Finally, concerning global mineral and processing investments, traditional research conducted by the Raw Materials Group has been in the forefront in the region since 2000, with an average share of about 30% of global investments. However, the last research estimates total investments for LATAM at US $36 billion, representing about 35% of the global amount.[1]

CHALLENGES, THREATS & OPPORTUNITIES

In general, fundamental macroeconomic challenges are subordinated to a common development agenda in which achieving a minimum rate of sustainable growth, combating poverty and misery and reducing economic and social inequalities while preserving the environment are the key aspects. At an operational level of the mining industry, the improvement in the investment climate is crucial, with policies looking to generating quality geological information, infrastructure development, development of the capital markets, and reinforcement of national entrepreneurship.

In terms of threats, macro economic disarrays and the resurgence of a certain political instability have been degrading the regional business climate. In the context of the mining sector, the following should be mentioned:

Taxation – national projects designed to increase taxation, such as those seen in Chile, Peru and Bolivia (natural gas), are disturbing expectations and may be detrimental to regional competitiveness, ➢



depending on the intensity of the changes made. Concerning taxation level and distribution, the consolidation process at federation levels is different, putting in check taxation stability agreements since regional and local governments want a large slice of the cake. This reality was leveraged by a perception that the current favourable period of windfall returns could last for a few years, not to mention the possible attitude, as that prevailing in Chile, for example, about the low tax revenue from the mining industry.

Opposition to Mining — on another front, there has been gradual opposition to mining projects, inserting the region in the insidious global process of dispute and blocking of mining projects, whatever the relative values and opportunity costs at stake. Several events impacted the image of the industry and raised growing concern about the prospective business climate for mining investments. Emblematic projects such as Tambo Grande and Rio Blanco (Peru), Esquel (Argentina), Bojuru (Brazil) and Cerro San Pedro (Mexico), representing a first wave of investments totaling around US $1.3 billion, characterize the nature of these problems and the magnitude of costs involved.

At national levels, these vectors – taxation and environment – may reduce the attraction of foreign investments and hinder achieving higher levels of potential mineral products most needed for the overall region.

The business mood in any region and sector of activity is increasingly influenced by the relative attractiveness of other producing regions. Despite the aforementioned factors, LATAM, when confronted with the set of opportunities, challenges and threats in Africa, Asia and Eastern Europe, is in a very strong position because of its range of competitive and comparative benefits. A regional cross-country overview can be summarized as follows:

- Extent and diversity of geological environments of interest
- Impressive stretches of primary areas with low to no levels of exploration;
- Centuries-old tradition of the mining industry
- Clear and transparent mineral legal framework in granting exploration permits and mining concessions
- Good flexibility in transferring exploration and exploitation rights
- Large number of national mining companies, specialized suppliers and consulting companies in a network of potential partners, sellers, buyers and customers
- Modern and seasoned institutional frame of specialized government agencies, especially in Argentina, Brazil, Chile and Peru
- A multitude of tax incentives.

These aspects, when evaluated from the expectations of the global mining players and interests, rank LATAM as a top geographical priority for major and junior companies, institutional investors, financiers, suppliers and consulting companies.

[1] ERICSSON, M. Industry Registers Record Investment. E&MJ. Jan/Feb, 2005