



WORLD BANK GROUP
Energy & Extractives

Looking Beyond the Boom: Pre-Competitive Collaboration and the future of mining in Latin America

II EU-Latin American Dialogue in Raw Materials
September 22, 2015

Paulo de Sa

Practice Manager

Energy and Extractives Global Practice

The World Bank



Key Messages

- ▶ Despite the current downturn, Latin America still holds the largest reserves in the world for several key minerals and will continue to attract the interest of mining companies in the foreseeable future.
- ▶ The current downturn provides LATAM countries with an opportunity to deal with some of the challenges that emerged during the boom: poor and uncoordinated infrastructure development, weak-overstretched capacity, limited technical innovation, and growing social demands and environmental concerns.
- ▶ The issues governments are facing are “surprisingly” similar across countries but there is presently limited opportunity to share experiences and good practices and discuss alternative solutions.
- ▶ Collaboration between public and private sectors namely in the areas of infrastructure and innovation hold the key for future success.

Mining in LatAm: Industry at Crossroads

- ▶ Many Latin American countries have deliberately - or by force of circumstances - decided not to develop their mining sectors.
- ▶ In places like Chile, Mexico and Peru, mining has induced greater levels of wealth and prosperity and supported a path towards advanced economies.
- ▶ Mining investment has grown exponentially in Latin America over the past decade. In 2014 the Region received 27% of global exploration spending and was bound to receive up to US\$200 billion in new investment by 2020. However, since 2014, Chile and Peru saw a significant decline in foreign investment as mineral prices declined.
- ▶ Latin America's preeminence in mining cannot be taken for granted. Lower prices, rising costs, declining productivity and increasing social and regulatory pressure in community engagement and environmental sustainability are hampering the sector's profitability and ability to remain globally competitive.

Challenges Affecting the Industry

- ▶ Slowing Demand in China
 - ▶ China's "new normal" will probably translate in annual growth rates of less than 7% but growth will still be robust. Shift from industrial growth to services will cause reduction in the intensity of consumption and a slow down in demand growth rates for minerals.
- ▶ Supply Overcapacity
 - ▶ Majors conserve cash - cost reduction and deferral of exploration and capital expenditures - in order to go down in the cost curve... but still look to increase market share by taking high cost producers out of the market.
 - ▶ Don't underestimate capacity for cost reduction: contractors, low energy (and steel) prices, innovation, reengineering, labor productivity, overheads, currency depreciation...

Low Prices are Here to Stay!

- ▶ Finance is still relatively abundant, in spite of very low returns on equity (capital impairments)
 - ▶ Large companies still have strong positive cash flows.
 - ▶ In the first 8 months of 2015 more money has been raised for mining than in 2014, with a sharp increase in the amount of debt being raised.
 - ▶ Traditional equity investors are still present.
 - ▶ But, increase in US interest rates will increase constraints on project financing
- ▶ **In Summary**
 - ▶ Prices will be capped at least until 2018: we expect that mineral commodity prices will remain low but, because of demand-related factors, not as low and not for as long as they were back in the 1990s.
 - ▶ Price volatility is expected to increase.

The way forward: Collaboration or competition?

- ▶ During high commodity prices mining companies were mainly focused in bringing additional production into the market, forgetting opportunities to improve efficiencies and reduce costs through precompetitive cooperation
- ▶ Mining has the potential to act as a platform for change and economic diversification in Latin America:
 - ▶ Through advances in research and development and technological innovation it can address the challenges that hinder the productivity of the industry and of the countries, such as lack of infrastructure, access to water, and rising energy costs.
 - ▶ Through Supply Linkages Cooperation and Public-Private Partnerships it can drive the growth of a new mining services sector that helps to diversify the economy.
 - ▶ Through policies that foster inclusion it can enhance skills and take a leadership position on issues such as environmental and social sustainability.

Examples of Precompetitive Cooperation

- ▶ **Soft:** safety, environmental management, skills improvement, METS (mining equipment, technology and services) sector, geodata modelling/predictive analytics, community development.
- ▶ **Hard:** multipurpose infrastructure, including power and water - sharing infrastructure can reduce costs and does not reduce competitive advantage.
- ▶ **Future:** local content (suppliers, contractors), R&D and technological innovation, research hubs, industrial parks.
- ▶ **Beyond CSR:** Partnerships with governments in contributions to achieve the SDGs.

How Should Governments Respond?

- ▶ Declining Commodity prices bringing instability into the sector.
- ▶ Global economic risks continue to hinder growth prospects. The global economy remains fragile and prone to policy while slower “new normal” growth in China is increasing volatility.
- ▶ The sharp change in commodity prices creates both benefits and difficulties for policy makers in resource rich countries. The precise effects is country-specific, but the needed adjustments span the spectrum of monetary, financial, fiscal, social, and real sector policies.
- ▶ The most important policy areas are: (a) macroeconomic frameworks; (b) predictability of sector policies; (c) tax regimes; (d) financial spillovers; and (e) diversification strategies.



Policy Actions

- ▶ **Macroeconomic policies** and strong fiscal position to smooth price volatility (to avoid boom and bust cycles), with the effective use of stabilization funds.
- ▶ **Predictability of rules:** policies, regulations and institutions.
- ▶ **Overall enforcement of the rule of law.**
- ▶ **Business climate and trade policies:** reducing barriers to entry, power of oligopolies, improving labor markets, avoiding indiscriminate subsidies...
- ▶ **Don't tax more, tax better and improve tax administration.** Revenue mobilization from general taxation is often plagued by loopholes, exemptions, tax avoidance and evasion, while waste and inefficiency in public expenditures remain prevalent, both at national and subnational levels.
- ▶ **Promote non-tax benefits (linkages) but don't impose (unrealistic) targets.**
- ▶ **Foster interdisciplinary collaboration:** Intergovernmental planning collaboration and administrative approvals .

Potential areas for EU-LATAM Cooperation Where World Bank Can Assist

- ▶ Geodata.
- ▶ Integrated Resource Management and Regional Economic Development.
- ▶ PPPs for Infrastructure (power, water...).
- ▶ Integrated Supply Chain Management: Partnerships with industry and solution providers to foster innovation and develop METS (mining equipment, technology and services) sector.
- ▶ Joint R&D and technological transfer, research hubs, industrial parks.
- ▶ Environmental Management
- ▶ Ban on the use of mercury in artisanal and small scale mining.

The World Bank Group

IBRD

International Bank
for Reconstruction
and Development

Est. 1945

Role: To promote
institutional, legal
and regulatory
reform

Clients: Governments with
per capita income
between \$1,025
and \$6,055.

Products:

- Technical assistance
- Loans
- Policy Advice

IDA

International
Development
Association

Est. 1960

To promote
institutional, legal
and regulatory
reform

Governments of
poorest countries
with per capita
income of less than
\$1,025

- Technical assistance
- Interest Free Loans
- Policy Advice

IFC

International Finance
Corporation

Est. 1956

To promote private
sector development

Private companies
in member
countries

- Equity/Quasi-Equity
- Long-term Loans
- Risk Management
- Advisory Services

MIGA

Multilateral
Investment and
Guarantee Agency

Est. 1988

To reduce political
investment risk

Foreign investors in
member countries

- Political Risk Insurance

← **Shared Mission: To Promote Economic Development and Reduce Poverty** →

THANK YOU !

Pdesa@worldbank.org