LAC eco-political trends and mining risk analysis

Presented at MILA conference in Lima – 2016.10.24
Wherever possible, AMI has verified the accuracy of information provided by third parties, but does not under any circumstances accept responsibility for such inaccuracies should they remain unverified.

It is expected that the reader will use the information provided in this report in conjunction with other information and with sound management practices. AMI therefore will not assume responsibility for commercial loss due to business decisions made based on the use or non-use of the information provided.
About AMI
More than two decades of seeking to understand the region

- **1993**: InfoMex is founded in Mexico City
- **1995**: First studies conducted in South America, name changed to InfoAmericas
- **1997**: Office opened in Sao Paulo
- **1999**: Tendencias launched, the most widely read regional intelligence newsletter
- **2000**: InfoAmericas joins the Global Intelligence Alliance (GIA) as its Latin American member
- **2002**: Five industry practices are introduced
- **2003**: AMI consultants complete their 1,000th client engagement in Latin America
- **2006**: InfoAmericas is sold to Kroll, forming Kroll’s first market intelligence division
- **2007**: Office opened in Miami
- **2011**: Key members of the former InfoAmericas team form AMI, with offices in Miami and Mexico City
- **2015**: AMI launches Sao Paulo affiliate office
- **2015**: 2,000th client engagement completed
We deliver the intelligence
You need information to make smart business decisions

Growth
- Opportunity Benchmarking
- Market Assessment
- Customer Research
- Investment Viability
- Partnering
- Strategic Planning

Risk
- Competition
- Unethical competitors
- Political
- Reputational
- Economic
- Regulatory

Performance
- Market Share
- Best Practices
- Brand Awareness
- Customer Satisfaction
How AMI supports natural resources and infrastructure investors

**Pre-investment phase**

- Politically Exposed Persons DD
- Counterparty risk assessment

**Operating phase**

- Strategic partner due diligence
- Competitive risk monitoring
- Counterparty risk assessment

**Country risk analysis**

- Strategic planning
- Research support

**Reputational Risk**

- Reputational due diligence of companies and individuals

**Political Risk**

- Political and regulatory risk monitoring

**Competitive Risk**

- Competitive risk monitoring

**Economic Risk**

- Opportunity benchmark analysis
Having collaborated together on an ad-hoc basis for over a decade, AMI and Southern Pulse have formalized an operative alliance. Together, our two firms bring to our clients a network of over 300 consultants and investigators across more than 100 cities in 28 Latin American and Caribbean countries.

Complex investigations that delve into local political, competitive and security issues relies on local human intelligence. Since the 1990s, our firms have carefully built a network of reliable and trustworthy affiliates whose relationships penetrate all levels of political and corporate circles.

Since 1993, our combined firms have conducted more than 3,000 market intelligence cases including:

- Competitive intelligence
- Political risk monitoring & analysis
- Due diligence & background checks
- Fraud investigations
- Security risk analysis & monitoring
Leading trends shaping LAC
LAC’s most important commodities are trending low

Low oil prices hurt the currencies and fiscal balances of Venezuela, Ecuador, México y Colombia but are a blessing to the Caribbean and Central America.
Competitiveness matters
With the commodity windfall gone, LAC must compete for investors and decrease waste

Countries that reformed themselves in the past will now reap the relative benefits

2016 GDP growth and Doing business in (World Bank) ranking

Sources—EIU, IMF, World Bank
Mid-2016 marks the bottom of the down-cycle
Over $1 trillion USD of regional GDP disappeared but will recover by 2019

### Latin America Nominal GDP (USD Billions)

<table>
<thead>
<tr>
<th>Year</th>
<th>Brazil</th>
<th>Mexico</th>
<th>Argentina</th>
<th>Colombia</th>
<th>Chile</th>
<th>Peru</th>
<th>Venezuela</th>
<th>ROLA</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>$2,416</td>
<td></td>
<td>$1,304</td>
<td>$599</td>
<td>$377</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2015</td>
<td>$1,772</td>
<td></td>
<td>$1,152</td>
<td>$644</td>
<td>$329</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>$1,720</td>
<td></td>
<td>$1,065</td>
<td>$546</td>
<td>$346</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2017</td>
<td>$1,938</td>
<td></td>
<td>$1,127</td>
<td>$678</td>
<td>$363.18</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2018</td>
<td>$2,104</td>
<td></td>
<td>$1,224</td>
<td>$798</td>
<td>$375.89</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Sources – IMF, AMI analysis
Short term growth driver – undervalued currencies

Falling commodities combined with Brexit triggered currency overselling. Currencies will rise (vis-à-vis the USD) towards their historic average... unless the Fed grows hawkish.

Source – EIU Big Mac index
Long term growth driver – LAC’s demographics
Fewer children, more working women = consumption growth through 2030
100 million millennials are now of working age

Population by age group in Latin America for 2010 and 2020

Sources – ECLAC, AMI analysis
Even more than an economic crisis, this is a fiscal crisis
South American governments have not cut costs in line with the fall in tax revenue

<table>
<thead>
<tr>
<th>Country</th>
<th>Fiscal Deficit/Surplus as % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brazil</td>
<td>-2.3%</td>
</tr>
<tr>
<td>Mexico</td>
<td>-2.6%</td>
</tr>
<tr>
<td>Argentina</td>
<td>-3.5%</td>
</tr>
<tr>
<td>Chile</td>
<td>-1.8%</td>
</tr>
<tr>
<td>Peru</td>
<td>0.6%</td>
</tr>
<tr>
<td>Ecuador</td>
<td>2.3%</td>
</tr>
<tr>
<td>Ecuador</td>
<td>-0.9%</td>
</tr>
<tr>
<td>Ecuador</td>
<td>-5.3%</td>
</tr>
<tr>
<td>Ecuador</td>
<td>-4.9%</td>
</tr>
</tbody>
</table>

Sources – World Bank
Scarcity breeds pragmatism
South American governments are shifting policies towards a pro-business stance

Examples of LAC’s political shift to the right

• Argentines elected a pro-business President who has moved quickly to unwind over a decade of destructive populist policies.
• Brazil’s congress impeached Dilma. President Temer and a center-right cabinet are aggressively pursuing fiscal discipline and economic reform. Federal prosecutors deepen their investigations.
• Peruvians elected a proven technocrat who promises to foster more investment in Peru.
• Venezuelans elected an opposition party dominated congress in their December 2015 elections.
• Bolivians denied Evo Morales the opportunity to run for a fourth consecutive term in office.
• Ecuadorians denied Rafael Correa the option to seek another term in the 2017 elections.
Key jurisdiction analysis
Peru – leading the recovery of LatAm mining investment

PPK’s victory combined with tested mining laws inspires investor confidence

Strengths

• PPK government serious about lowering corruption, more infrastructure and less mining red tape
• Peruvian mining laws encourage investment
• Legislation pending to formalize 70,000 miners
• Established political class supports mining
• Qualified mining labour pool

Weaknesses

• Royalty trickledown is inconsistent or ineffective
• Local communities target their anger re: lack of royalties at the mining companies
• 2012 mandate for special treatment of indigenous can delay permitting
• Over 200 permits per mine on average
• Coca production funds illicit groups

Risk areas

Local political & social risk

Security risk
Chile – maturing democracy = stronger civil society
Miners must contend with non-elected political players and an independent judiciary

**Strengths**

- The most admired mining laws in the region
- Efficient permitting process
- Easy to secure mining rights & defend them
- Established political class supports mining
- Qualified labour force. Professional services support.

**Weaknesses**

- Anti-mining environmentally focus civil society is well organized, allied with indigenous groups and popularly supported
- Most mining assets located in arid regions – water usage is often controversial, even conflictive
- Independent judiciary unafraid to adjudicate mining conflicts

**Risk areas**

- Legal risk
- Local political & social risk
- National political & regulatory risk
Argentina – mining now enjoys strong federal support
The decentralized jurisdictional model now works against Argentina

Strengths

- Macri admin named mining one of four pillars for FDI development. Sec. Meilán promoting aggressively.
- Passed reforms: no more export taxes & royalties, re-permitted open-pit mining
- Wants to legislate cohesive federal-provincial accord
- Similar geological construct as Chile but less developed

Weaknesses

- Strong environmental movements led to recent bans on open-pit mining and some chemical use
- Decentralized mining legal environment
- Some provincial restrictions operate in violation of more liberal federal codes
- Provincial alignment challenging if transfer payments aren’t maintained, or Macri loses political capital

Risk areas

Local political & social risk
Operational & bureaucratic risk
Colombia – mining struggle to compete with other interests

In contrast to hydro-carbons, mining does not enjoy widespread political support

**Strengths**

- Under exploited geology – large proven deposits
- Consistently pro-investment governments
- Improving infrastructure
- March towards peace has dramatically improved security, even if some regions remain vulnerable

**Weaknesses**

- Property title rights can be challenged
- Environmental permitting is slow and sometimes challenged after initial approval
- Uncoordinated agencies cause delays
- Even if peace is rescued, serious security issues continue, especially near Venezuela border
- Total tax burden double that of Peru or Chile
- Informal mining abounds, hurts industry

**Risk areas**

- National political & regulatory risk
- Legal risk
- Security risk
Ecuador – running out of $, Correa tries to befriend mining

Dollarization limits monetary policy. Ecuador needs investment and must limit imports.

Strengths

- Correa admin has changed (again) its stance on mining, seeking to attract new investments
- Useful amendments to tax laws implemented
- Opening 25 concessions to attract $750m

Weaknesses

- Ecuador does not recognize jurisdiction of foreign courts in any legal conflict with the state
- Arbitration must take place in LatAm
- Balance of payments crisis triggers import restrictions, causing delays to miners
- Capital gains tax increases add to burden
- Correa grip on power loosening – may lead to power vacuum and unpredictable investment climate

Risk areas

- National political & regulatory risk
- Legal risk
Guyana – a wild west backdrop, but friendly to mining

Despite a conflictive history as a young democracy, Guyana has always welcomed mining.

**Strengths**

- Granger admin has embraced US, IMF, World Bank
- Supportive of mining – trying to formalize sector
- Elected on anti-corruption, improvements made
- International arbitration the norm. Local courts respect foreign court decisions
- Broad public support for mining, prospector culture

**Weaknesses**

- Poor infrastructure. Mines reached by plane, boat
- Informal mining abounds, hurts sector reputation
- Money laundering infiltrates many local suppliers
- Lack of technical support and equipment operators
- Very strong political party rivalry could politicize future large scale investments.

**Risk areas**

- Operational & bureaucratic risk
- National political & regulatory risk
- Security risk
Mining investor best practices
# Pre-investment phase

Research the entire risk eco-system. Build partnerships to ward off future risks.

## Co-investors

- Include powerful and politically neutral local investor or two investors connected to leading parties.
- Include development bank with loans to government

## Royalties & taxes

- Profit based (vs production based) will create fewer conflicts when prices rise again
- Negotiate guaranteed payments to local community

## Government relations

- Assess attitudes beyond exec branch including senate, house leadership and opposition.
- Build bridges to mining experts in all areas of gov’t

## Local community

- Political risk analysis should include deep dive on local players – political, NGO, labor, religious, community leadership.
- Identify money links to national players
Build-out phase
Use the leverage of monies spent to form political allies, build partnerships, connect locally

Local relations
- Establish local outreach office outside mine in local community
- Build (or support) local committee made up of govt, labor, NGOs, other to administer local royalties

Training
- Work with gov’t to build a mining education / training facility near the mine to enhance long term employability of locals, and foster community support

Procurement
- Get out ahead of local sourcing complaints by hiring locally, and publicizing
- Work with politically connected local suppliers

Government relations
- Invite political leaders from all branches, including opposition to visit the mine along with press.
- Set expectations re: future tax flows
## Operating phase

Utilize intelligence & influential partnerships to anticipate and mitigate risk

### Intel program

- Monitor locally and nationally
- Focus on anticipating problems so they can be proactively mitigated
- Align with gov’t & community relations budgets
- Control your IT assets

### Industry cooperation

- Work with other formal miners to foster industry wide best practices
- Cooperate on efforts to educate politicians, journalists, NGOs and public

### Advisory board

- Develop advisory board that includes powerful local business leaders, influential civil leaders, local mining experts
- Use board to build bridges

### Gov’t & community relations

- Build program and budget around the mitigation of perceived threats – adjust over time
- Energy sector = best practices
About AMI

AMI is Latin America’s leading independent market intelligence consultancy

Our founding partners helped pioneer the field of market intelligence in Latin America

Our consultants have advised over ½ of the region’s 100 largest strategic investors over a span of two decades

AMI consultants have conducted close to 2,000 client engagements in Latin America since 1993

Our consultants have worked in every market in Latin America

Our holistic approach to market intelligence is unique. We combine market research, competitive intelligence, political analysis and economic forecasting in our studies. Few others do the same in Latin America

AMI is an affiliate of the Global Intelligence Alliance (GIA), the world’s leading independent Market Intelligence network with 26 representative offices spread across six continents.

John Price, MD
+1 (305) 441-9300
jprice@americasmi.com