Developing a different roadmap for the future?

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"The single biggest problem in communication is the illusion that it has taken place" – George Bernard Shaw

The conversation on the future of the mining sector reflects three related fault-lines in our society: the tension and mistrust between the ruling party and big business; the unsettling dichotomy of wealth and poverty; and a deeply-held view by the majority of South Africans that the mining industry epitomises white control in the economy. There is a sense amongst those in the ruling party that the industry is not doing enough to contribute to social and economic change.

The perceived slow pace of transformation in the mining industry and the fact that despite possessing a significant base of mineral wealth, South Africa is still plagued by unacceptably high rates of unemployment, keeps the industry in the spotlight. Genuine questions are raised about the juxtaposition of acute levels of inequality with high levels of wealth in one country. This foregrounds much of the debate on the future of the mining sector.

Even before the ANC Youth League raised the nationalisation debate, there were tensions between the industry and the ruling party in the period leading up to the change in the old order mining rights to new order mining rights under the custodianship of the state.

These tensions surfaced again in the context of the mining industry's representations on the Mining Charter before the Minerals Resources Portfolio Committee in 2011. There were

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seriously divergent views between the Chamber and the government regarding the performance of the industry in meeting the requirements of the Charter.

The National Mineworkers Union and the South African Mineral Development Association (SAMDA) also expressed views that showed frustration with the pace of change in the mining sector.

Until a healthy space is created for various social actors to talk candidly about the current challenges in the sector and pull their minds together to consider alternative and better scenarios for the future, it will always be difficult to move forward.

Tensions between the mining industry and the political establishment are certainly not new, but have reached a new high post-apartheid.

Monopoly capitalism under the English dominance of the mining sector created a similarly tense environment between the mining industry and the political elite of the Nationalist Party.

Gold and diamond mining existed as a politically ungovernable enclave – a liberated zone of sort - within a political order that felt threatened by its existence. The sector bred populist nationalism amongst the Afrikaners in ways that are not too dissimilar to the simmering tide of African populist nationalism under the ANC.

Adrian Fourie, the Minister of Mines under Barry Hertzog, was particularly hostile towards the mining industry, especially when production was cut back under the pressure of the

Great Depression in the early 1930s. In his anger he threatened nationalisation, pointing out that:

> We have had a spectacle in South Africa that there is one man who is chairman of all producing companies… He alone is the centre of the whole diamond industry …It is necessary for the government to take this great industry under its protection and that the interests of the public in general should not be lost sight of.

Fourie was clearly incensed by rising unemployment and socio-economic implications of supply curtailment. Sometime later it was Nico Diederichs, finance minister under John Vorster's government, who strongly, signalled his government's intention to nationalise mines. He considered mining magnates as selfish, exploitative, and trampling over the interests of the Afrikaners.

The English-dominated mining industry at the time buckled under pressure and acted. It was forced to facilitate the formation of large-scale Afrikaner capital, and participated in an exclusively racial form of economic empowerment, leaving in the cold the majority of the people.

The sometimes ambivalent, but generally genial, liaisons between the ruling Afrikaner elite and the English economic elite is something that would later generate a much deeper sense of resentment by the black majority in South Africa.

Often times when it is said that the there is more that the mining industry can do this is expressed the backdrop of an ugly history. The expectation is therefore that the industry should show more stamina to change the course of South Africa's political economy in ways that would break a new ground for inclusive and shared prosperity.

Increasingly economic empowerment and social inclusion are viewed as cornerstone of a more enduring nation-building project. It is no longer just the idealism of it that cuts it. Its substance has to be borne out in the changing material condition of the majority of the population and their increased economic participation.

Business leadership and the mining industry in particular, have a pivotal role to play towards the achievement of this end. If we do not act right today, we will give room to populist nationalists who would cast all caution to the wind and undermine economic stability in the future. This is where the meeting point of our diverse interests: we all want a stable future; but this will not be possible if the stranglehold of inequality and unemployment is not broken.

We may thus find ourselves in a position where we are no longer able to stem the cauldron of social discontent induced by economic exclusion and a deep sense of resentment over relative deprivation.

The danger, of course, is that such a climate could be manipulated by populist politicians for their own narrow ends. Long-term stability is possible through social cohesion grounded primarily on social and economic inclusion of the previously marginalised.

This is not to suggest that the mining industry is not contributing anything presently, but given the weight of history, more could yet be done.

The Mining Sector's Contribution to the South African Economy

Indeed, the mining sector is the biggest single contributor to the gross domestic product (GDP). It is also a significant contributor to the tax base and foreign exchange earnings.

According to a report generated by Citi Bank in June 2011, in the previous year the industry's contribution to the economy amounted to some $49 billion (R360bn), equivalent of 9% of the country's GDP. The sector is also responsible for employment of approximately 500 000 people. The industry is an important contributor to the growth of South Africa's economy and to sustaining livelihoods through employment.

While, understandably, the industry is deeply unhappy at being cast as uncaring about transformation, and is justifiably worried about nationalisation and radical pronouncements on tax, the magnitude of developmental challenges in South Africa requires more than what we have seen thus far.

There are two developments that have served to neutralise the debate on nationalisation for now: the expulsion of Julius Malema from the ANC and the release of the SIMS Report, which takes some sting off the debate while also stoking controversy over the resource-rent tax.

State Intervention in Mining: Summary of the ANC SIMS Report

The State Intervention in the Mineral Sector (SIMS) report is comprehensive and draws on a benchmark study of 13 countries. Significantly, the SIMS Report rejects nationalisation as not feasible given South Africa's budget deficit constraints and long-term fiscal challenges. It strongly prefers a resource rent tax.

It should be noted that even before the ANC research team undertook its work in 2011, Enoch Godongwana then deputy Minister of Economic Development and the chair of the SIMS working group, made bold proclamations that South Africa should go the route of super-profit tax. He made these remarks when he visited Australia in early 2011 ahead of the trip by the research team. As such, the proposals on resource rent tax suggest a validation of a long-held view by ANC leaders.

The thrust of the SIMS report is the notion that the mining sector should serve 'developmental objectives' rather than narrowly profit motive. These development objectives are defined in wide ranging terms, and include resource rent sharing, growth and development, tightening of linkages between the mining sector and other sectors of the economy, human resource and technology development, and local economic development.

The rent sharing component is encapsulated in the proposed resource rent tax of 50%, which would be activated once 'normal' profit (calculated as Treasury Long-term Bond plus 7%) is achieved. It is hoped that through these initiatives, the state will achieve the goals of industrialisation (or diversification of the economy with a solid capital goods supplier sector), job creation, poverty alleviation, and improvement in livelihoods.

Apart from resource rent tax, the other preferred instrument for state intervention in the economy is through the vehicle of the recently established State Minerals Company (SMC), whose function would be to express the strategic-entrepreneurial role of the state, especially to participate directly, both on its own and through joint-ventures, in mining.

The SMC would be exclusively tasked with the development of 'strategic minerals', and would then decide which investors to team up with. As such, the SMC will have exclusive prospecting rights to strategic minerals, facilitated through a 'first sight of all new state-financed geo-data available through the Council of Geosciences'. The SMC will not only be recognised as a special state corporate entity that has an exclusive right over 'strategic minerals', but also as a fully empowered entity.

The precise structure of the SMC, its modus operandi, investment strategy, and governance mechanism are not clearly spelt out in the document. There is a two-step process that is proposed towards the full operation of the SMC. The first step entails using the IDC expertise and financial muscle to drive the activities of the SMC as its subsidiary.

The second would require a legislative amendment that would free the SMC to operate as a fully-fledged State Owned Enterprise, with a possibility of listing. In the interregnum, the IDC would appoint a Board to regulate the activities of the SMC. This is set to change once a mooted legislation has been prepared and a new Super-Economy Ministry is in place.

Apart from investing on its own or on a joint venture basis, a room is created for the SMC to contest free equity in a private company. Another alternative proposal is that of contributing towards upfront risk capital when investing jointly with a private company – the latter model obtains in Norway.

Both propositions are vaguely developed in the SIMS Report. There is very little consideration given to regulating the activities of the SMC in relation to the private sector. This leaves little doubt that the SMC will have preferential treatment, especially because the definition of strategic minerals is left to the whims of an ambiguous Commission, with a final decision taken by the Minister and Cabinet. This is hardly a basis for securing a level playing field in commercial activity.

In augmenting the muscle of state involvement in mining, the SIMS Report further proposes the creation of a pooled special purpose vehicle fund that is replenished with union and state pension funds in order to promote developmental outcomes in mining companies. These specific developmental outcomes are not detailed out in the report, and this leaves open the possibility of a more expansive and vague definition of development that could be politically manipulated. Does this also mean PIC will wind down? That is not dealt with in the report.

It is doubtful the unions would agree to the use of workers' money in this indeterminate and narrowly political fashion. It would be reckless to go down such a speculative route. The Report asserts that this will enable the state-union bloc to ensure a balance between shareholder returns and development outcomes. There is no clear measuring stick or defined developmental outcomes stated in the Report.

The more biting, and perhaps, one of the most contentious recommendations of the SIMS Report is that of a resource rent tax. This is tied to the establishment of a Sovereign Wealth Fund, which would have a range of funds falling under it.

The introduction of the resource rent tax is projected to increase the takings of the state to R40bn annually. It is not clear how this figure was arrived at. Royalties would be decreased to 1%, yielding R4bn to the fiscus. The royalty payments would be ring-fenced and utilised to fund the Mineral Commission, rehabilitate abandoned mines, and promote community development.

Accordingly, the sovereign wealth fund will be structured into fiscal stabilisation fund to smooth the macro-economic environment during economic slump, essentially performing fiscal support function; future fund component; regional development fund to promote regional integration; and mining development fund to invest in discovery and development of new mines, beneficiation, human resource development, technology development, and promotion of industrial zones.

In my view, this proposal should have taken as a starting point the fact that there is a range of development finance institutions (IDC and DBSA) and a major state-supported pension fund (PIC). The idea of a sovereign wealth fund is an enticing one for a minerals economy. In fact, in principle, I support the need for one.

Further, the proposed structuring and uses of the SWF in the SIMS Report are vague articulated. There is also a raft of proposals regarding creating pooled funds for infrastructure investment in the region, which makes it rather superfluous to have a sovereign wealth fund dedicated to this task, especially beyond contribution that we may already be making towards infrastructure development through the DBSA.

On resource rent, there are three taxation instruments that currently apply to South African mining companies. The first is a standard corporate income tax of 25%. There is also a Secondary Tax on Companies (STC) at 10% and a Royalties Tax of up to 7% for unrefined minerals. The maximum for refined minerals is 5%. There are also additional financial obligations linked to various laws applicable to the corporate sector.

The Mining Charter, for example, requires mining companies to spend 1% of net profit after tax on social programmes linked to Social & Labour Plans (SLPs). Notwithstanding the 1% maximum, most large mining companies spend far more due to the geographical diversity of operations, the extent of the needs in communities as well as the diversity of requirements within the mining charter.

Further, the Mining Charter requires mining companies to increase their spending on human resource development (HRD) from 4% of annual payroll to 5% by 2014. This is in addition to the 1% already being contributed to the National Skills Fund in terms of the Skills Development Act.

More thought and consideration should be given to the calculation of the resource rent tax, and the potential implications of this on investor confidence. Already we have a problem in our hands of some mining sub-sectors such as platinum that are not performing well; some have applied for Section 189. Retrenchments will inevitably happen in the sector. Some ferromanganese companies are reportedly on the skids. The ferrochrome sector is sustaining pains inflicted by China's competitiveness, despite not having chrome ore endowments; and the absence of an export tax measure to defend the sector. The future lights may switch off for the ferrochrome sub-sector as smelters are permanently rested, with dire implications for jobs and growth.

The priority should be to build confidence in the mining sector and to evolve a long-term growth and development strategy to place it on a strong competitive footing. The ambiguities in the SIMS Report around resource rent tax, the functions of the state mining company, strategic minerals, and confused slew of regulatory institutions do not inspire confidence. Instead they compound confusion.

What the mining sector needs more than anything else today is a clear roadmap on the basis of which the social actors: government, industry, and unions can engage to define the future of the sector and its contribution to the country's developmental interests.

The proposal for resource rent tax at 50% above the normal profit is unhelpful when you consider the huge infrastructure deficiency currently – a reality alluded to by the finance minister Pravin Gordhan during his budget vote in 2011, and later by the National Planning Commission. Because of poor leadership and bad planning around the country's critical energy needs, the South African mining industry lost out in the commodity boom of 1999 to 2007.

During this period, globally the mining sector achieved real average growth of approximately 5%, while the South African mining sector was a laggard and shrank by 1% in the same period. According to McKinsey Consulting, had the South African mining sector's growth tracked that of the top twenty mining economies in the world, then its value added contribution would have been $8.5 billion higher, adding another 45 000 direct mining jobs. This reality, which is a result of government's inaction, should not be ignored in proposals about resource rent tax in the industry.

The Need to Recast the Debate

Much of the debate between the ruling party and industry on the future of mining runs like a dialogue of the deaf. No one hears the other. The discussion has been on-going for more than three years, and specific policy issues are likely to be under discussion for a number of years in the future. The country does not have the luxury of time to resolve the challenges it has on its hands and cannot afford to have a reputation for policy uncertainty. This perception needs to be nipped in the bud before the country loses momentum as a global player in the minerals sector.

There is a need to recast the discussion, beginning at an informal level and with the participation of key players. There are positive and exciting developments that we sometimes miss in the adversarial interactions between the ruling party and industry.

One such exciting story, but also potentially depressing, about South Africa is the fact that at US$2.5trillion, the in situ potential value of South Africa's resource base exceeds that of countries such as Russia (US$1.6 trillion), Australia (US$1.58 trillion), Canada (US$1 trillion) and Brazil (US$726 million).

This should be an animating story but it is hardly talked about in discussions between the industry and the ruling party. Yet if there was a good base of social consensus this is what we would be talking about more, especially to explore ways in which both government and industry can work together to harness this wealth to further enhance national economic prosperity.

Paradoxically and somewhat depressingly, South Africa's mining sector is among the laggards in terms of the levels of investment it attracts and the growth it generates. Further, despite our rich mineral base, we are a country that is the most unequal in the world. South Africa is marked by high levels of poverty and unemployment.

Although the resource rent tax seems somewhat unfair on the industry, mining companies should take responsibility for the negative perceptions generated about them. They are slow to act, and do so only when government threatens them. They should not have waited for the Mining Charter for them to take a giant leap to economic empowerment.

The mining industry should change tack. It needs to be a lot more proactive. If an engagement strategy did not work yesterday, it will not work today, and it will not work tomorrow. Try something radically different, shift reputational perceptions, and show preparedness that you could do more. What is important is that there needs to be a platform of shared purpose to define what should *more* look like. The mining industry cannot afford to lose an opportunity to be a critical stakeholder in redefining the past, and shaping the country's future political economic landscape. It needs to show leadership pivoted on enlightened self-interest.

Conclusion: Dialogue for a Shared Road Map

In conclusion, I propose that the social actors: government, industry and labour, should reset the dialogue about the future of the mining sector beginning first at an informal level. This should be based on achieving two purposes.

First, this should aim at confidence-building. Second, and the ultimate goal, should be to initiate a process towards painting a different future for South Africa's mining sector.

As such, this process can take as its starting point three sets of realities: the perspective of the mining industry about the current challenges in the sector; the on-going debates within the ANC's SIMS process; and the evolving thinking within the NPC's vision casting process - National Development Plan: Vision 2030.