

The Socio-Economic Challenges of the New Millennium



Mining, Sustainability and Risk: World Bank Group Experiences



Monika Weber-Fahr
Senior Economist
Global Mining Department
World Bank Group

PDAC
Toronto
March 13, 2001



The World Bank's View: The socio-economic challenges of the New Millennium

- ❑ **1.3 billion people live on less than \$1 per day**
- ❑ **1.5 billion people have no access to clean water**
- ❑ **130 million children cannot learn to write or read**
- ❑ **In 15 years from now we will be 7 billion people on this planet – 95% of this growth in Developing Countries**
- ❑ **Sustainability?**



The World Bank's Strategy: Investing in growth and poverty reduction



With
Governments

- **Invest in People**
- **Economic Reforms**
- **Protect the Environment**
- **Stimulate Private Sector Growth**
- **Re-orient Government**



With the
private sector



The World Bank Group

IBRD

- ◆ Finance reform/development projects



IFC

- ◆ Lend for/invest in private projects

IDA

- ◆ Finance for the poorest countries

MIGA

- ◆ Guarantees against country risk



Different clients - different instruments

**Government
Interest**

- ✓ Sovereign Loans
- ✓ Advisory Services
- ✓ Partial risk guarantees
- ✓ Loan syndications
- ✓ Direct loans
- ✓ Mezzanine financing
- ✓ Equity participations

**Private
Sector
Interest**



Global Mining Department of the World Bank Group



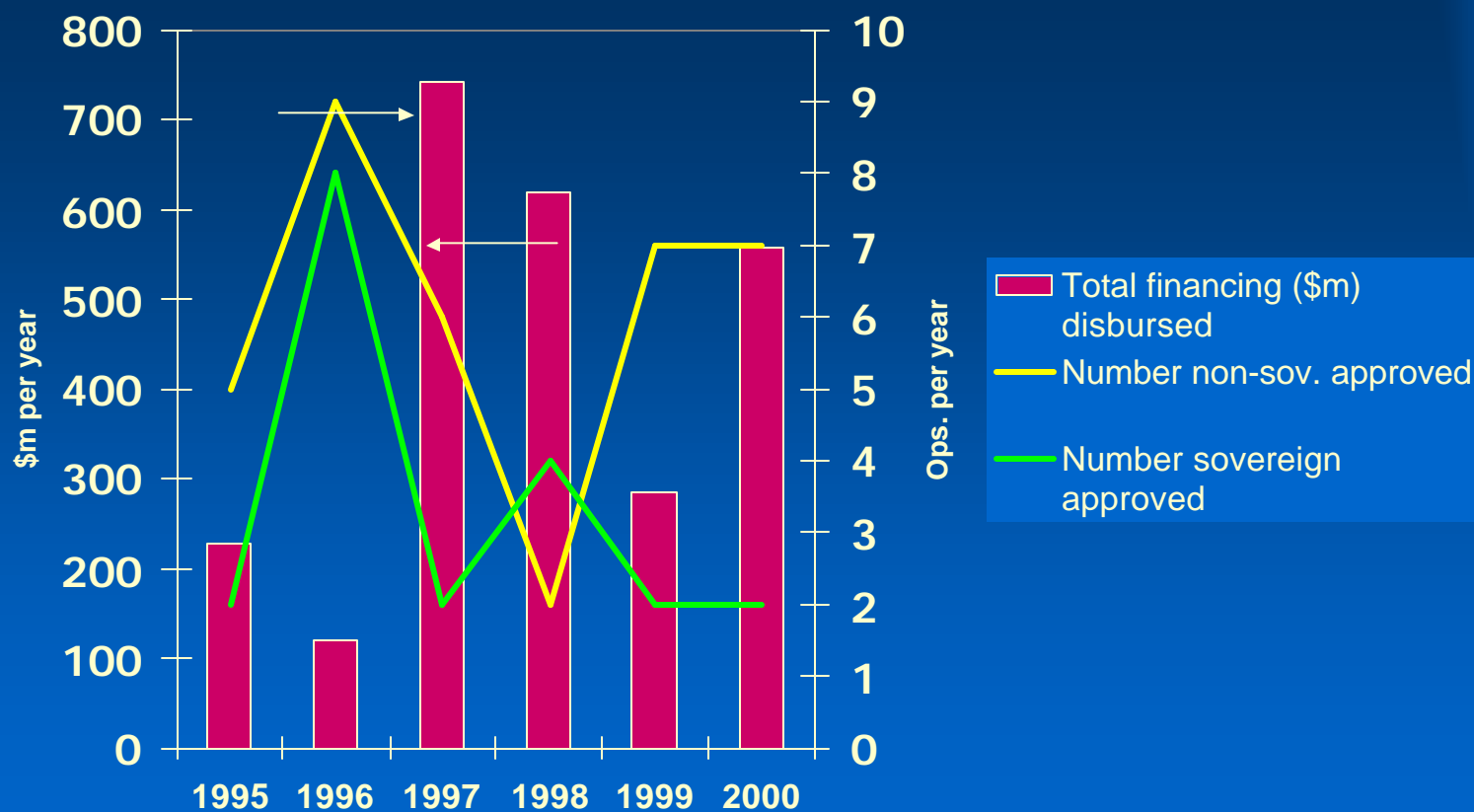
Government Role

- ✓ Sovereign Loans
- ✓ Advisory Services
- ✓ Partial risk guarantees
- ✓ Direct project loans
- ✓ Loan syndications
- ✓ Mezzanine financing
- ✓ Equity participation

Private Sector Role



World Bank Group Mining Business*



*Excludes MIGA Political Risk Insurance and Advisory Services



Why is the World Bank in the Mining Business?

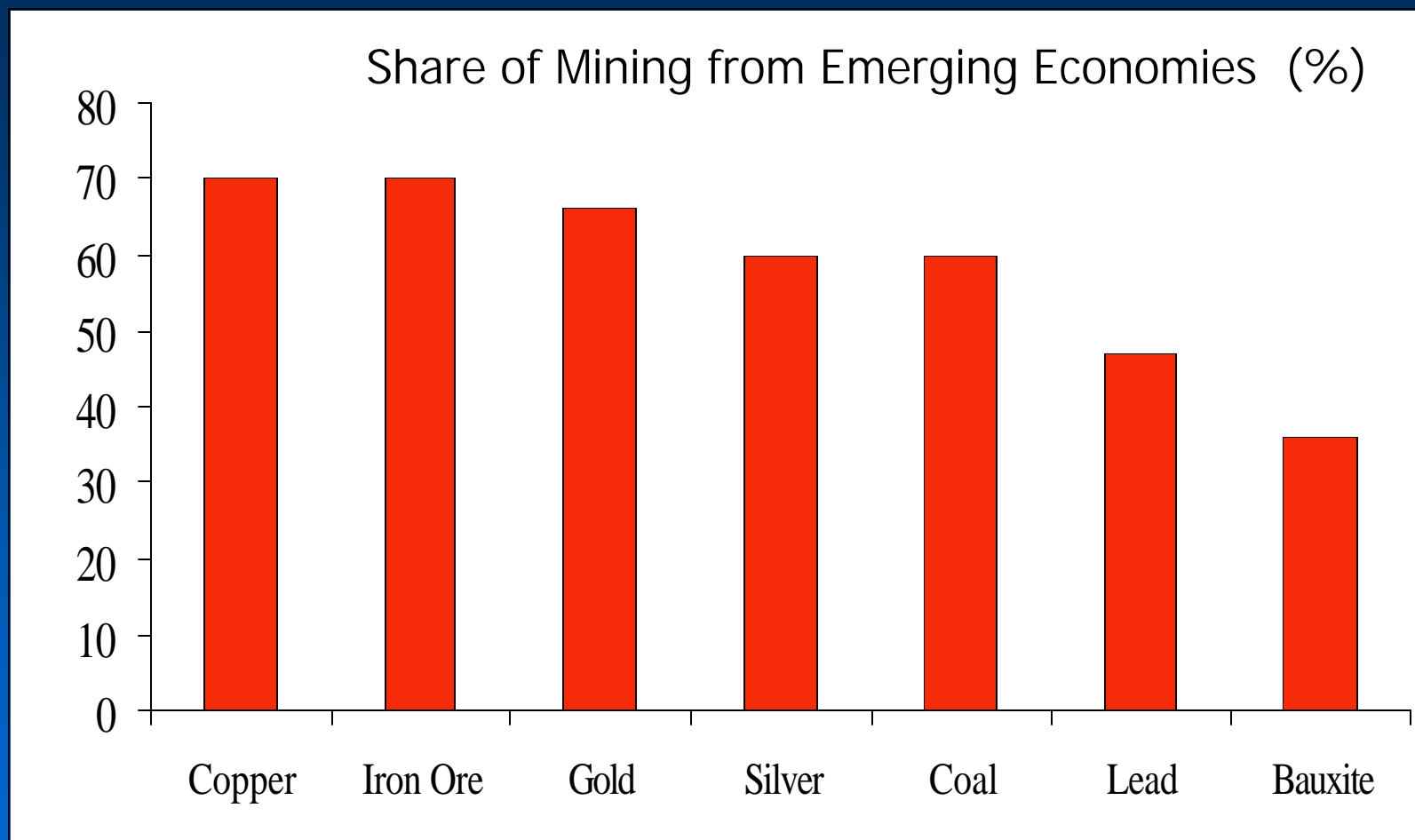
It's good for development!

Exports	3 – 41% of total country exports
Taxes	2 – 20% of total country tax receipts
Local Residents Employed	65 – 90% of total mine employment
Employment Multiplier	2 – 37 external jobs created for each mine job

*based on a study of nine mine projects in Latin America, Asia and Africa

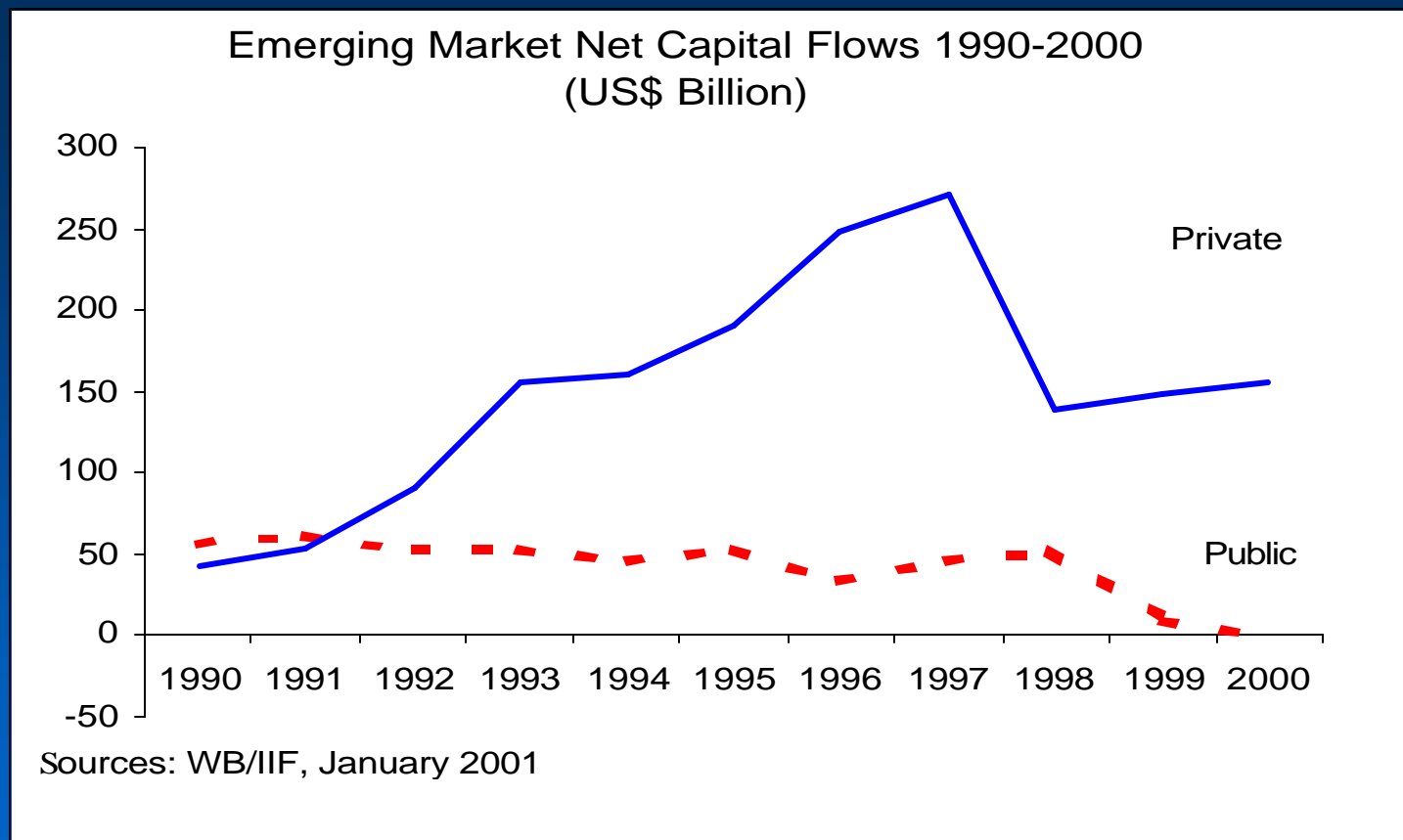


Mining is an emerging market business

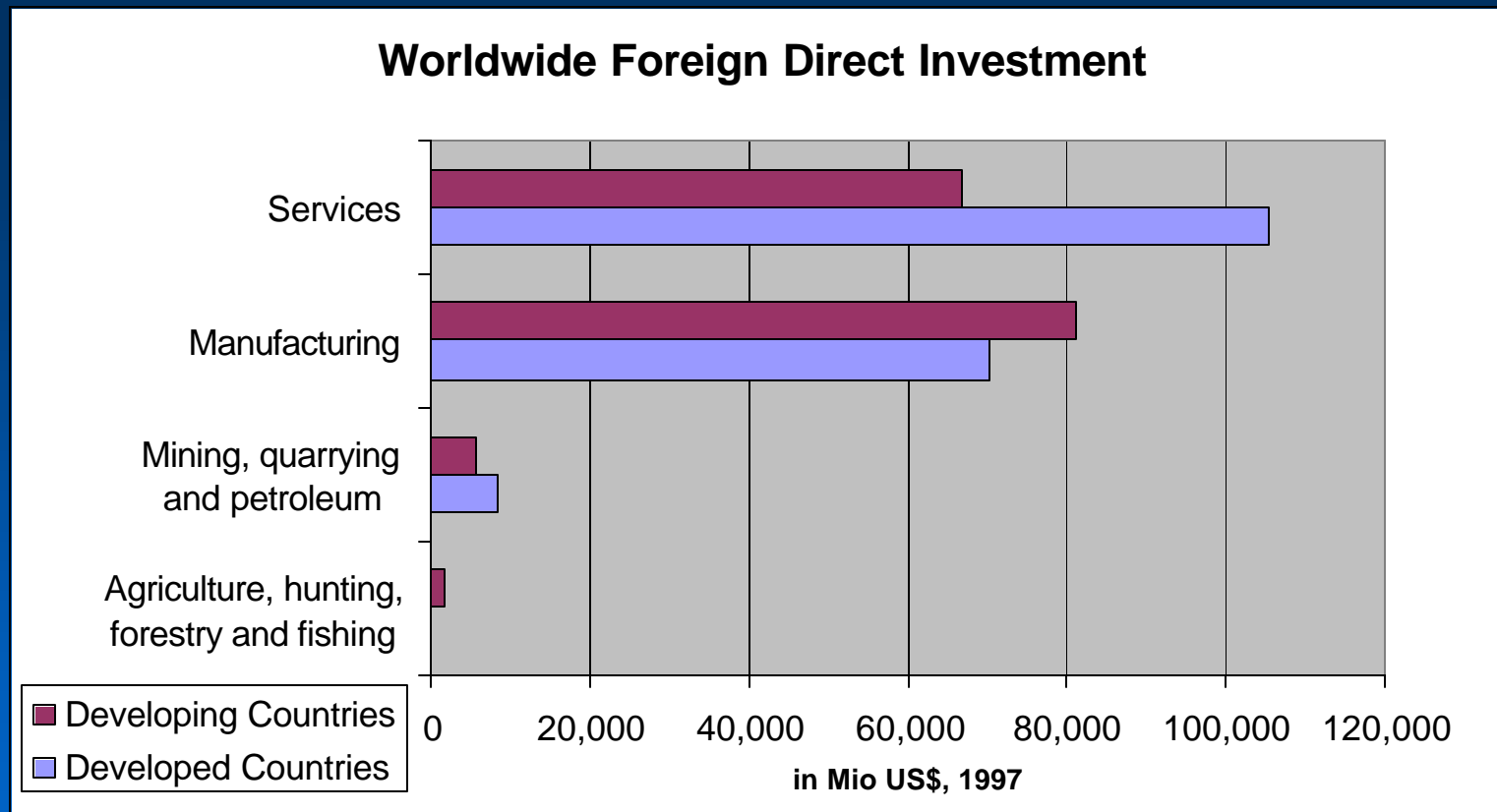




Private investors are key to emerging markets

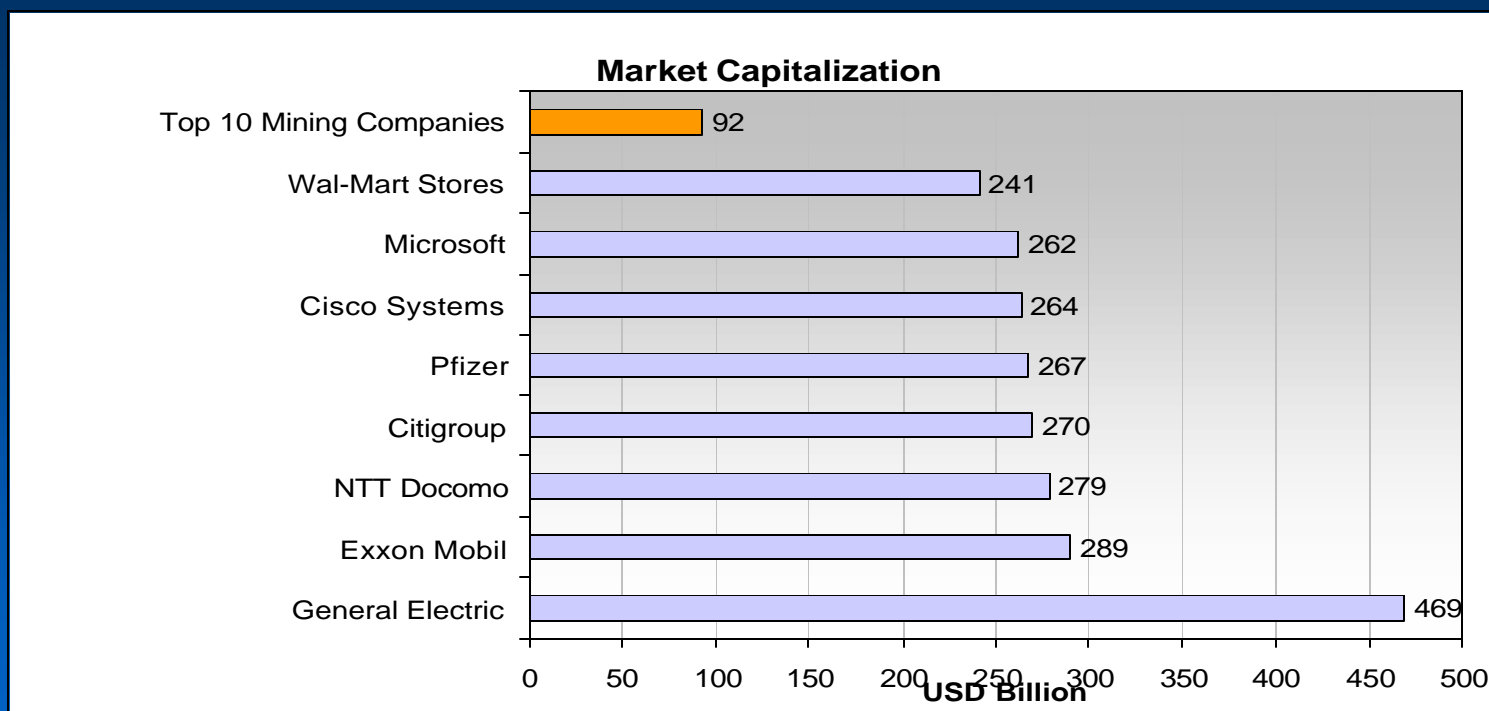


Globally - mining is not a big player





It's "old economy" – also in size

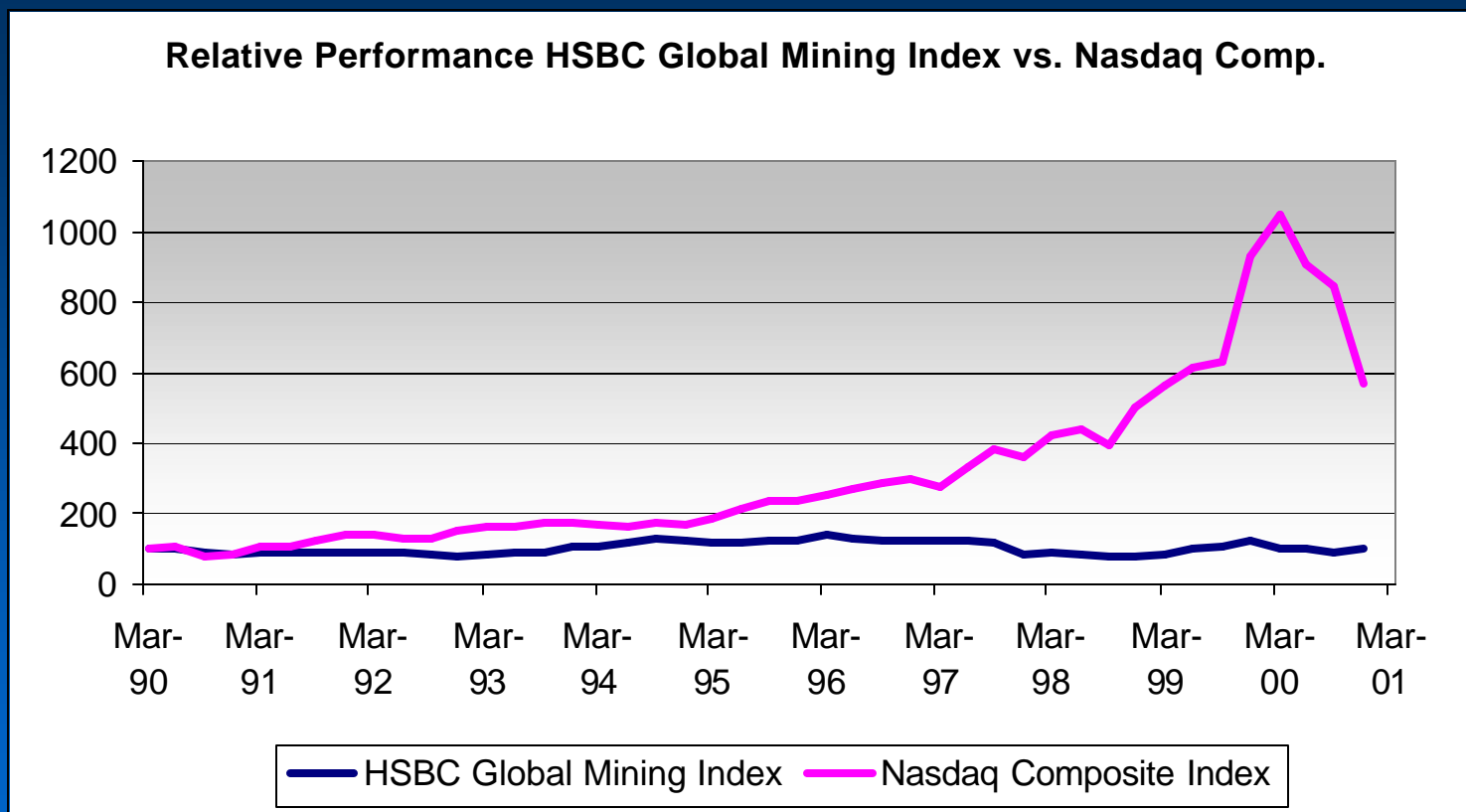


Source: Business Week Global 1000, July 10, 2000, "The World's Biggest Mining Companies," The MiningWeb.com, June 27, 2000, Yahoo Finance as of January 2001



How bankers see mining

Are there “good deals” in the mining business?

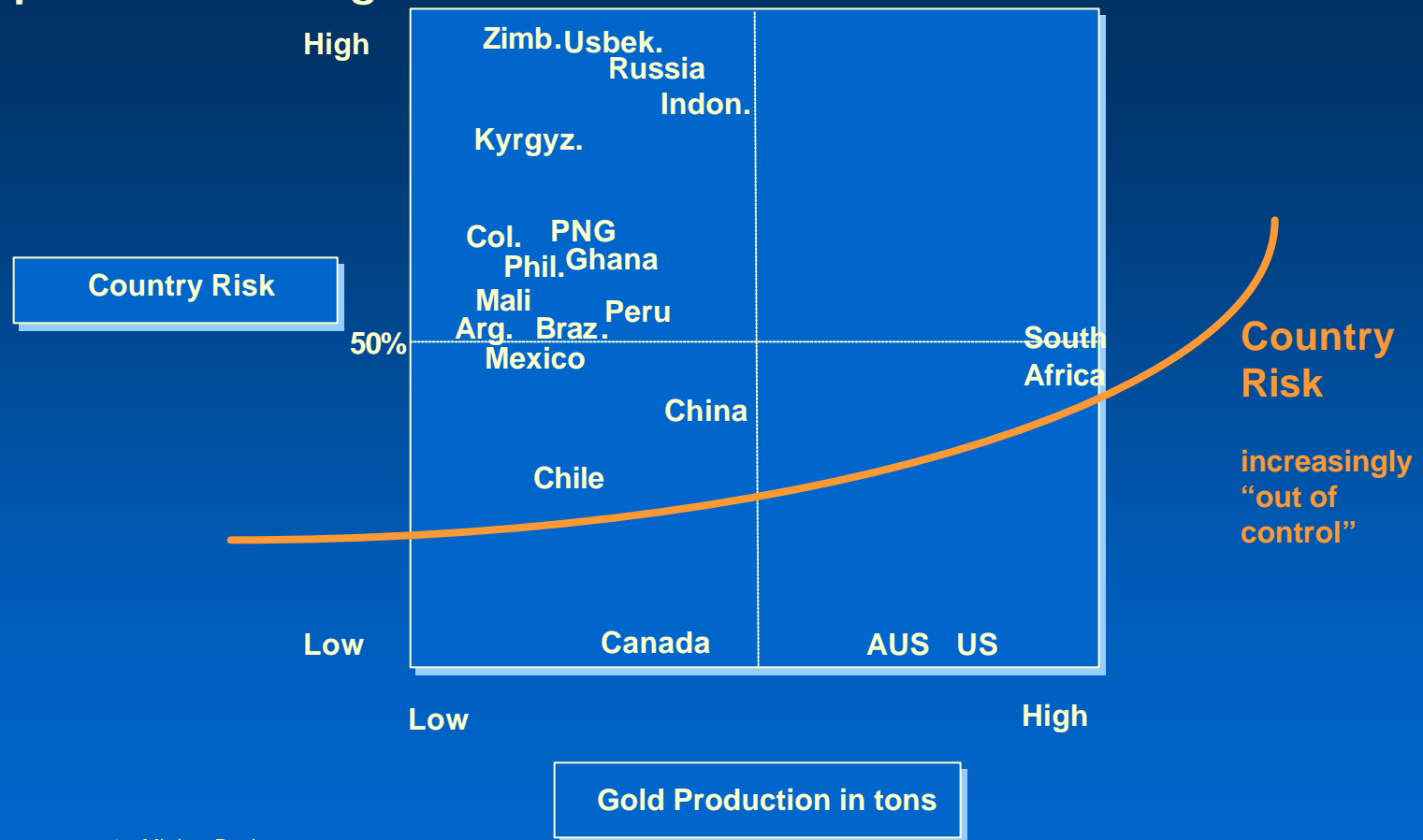


Source: Bloomberg



Working in emerging markets increases the business risk

Example: Gold Mining

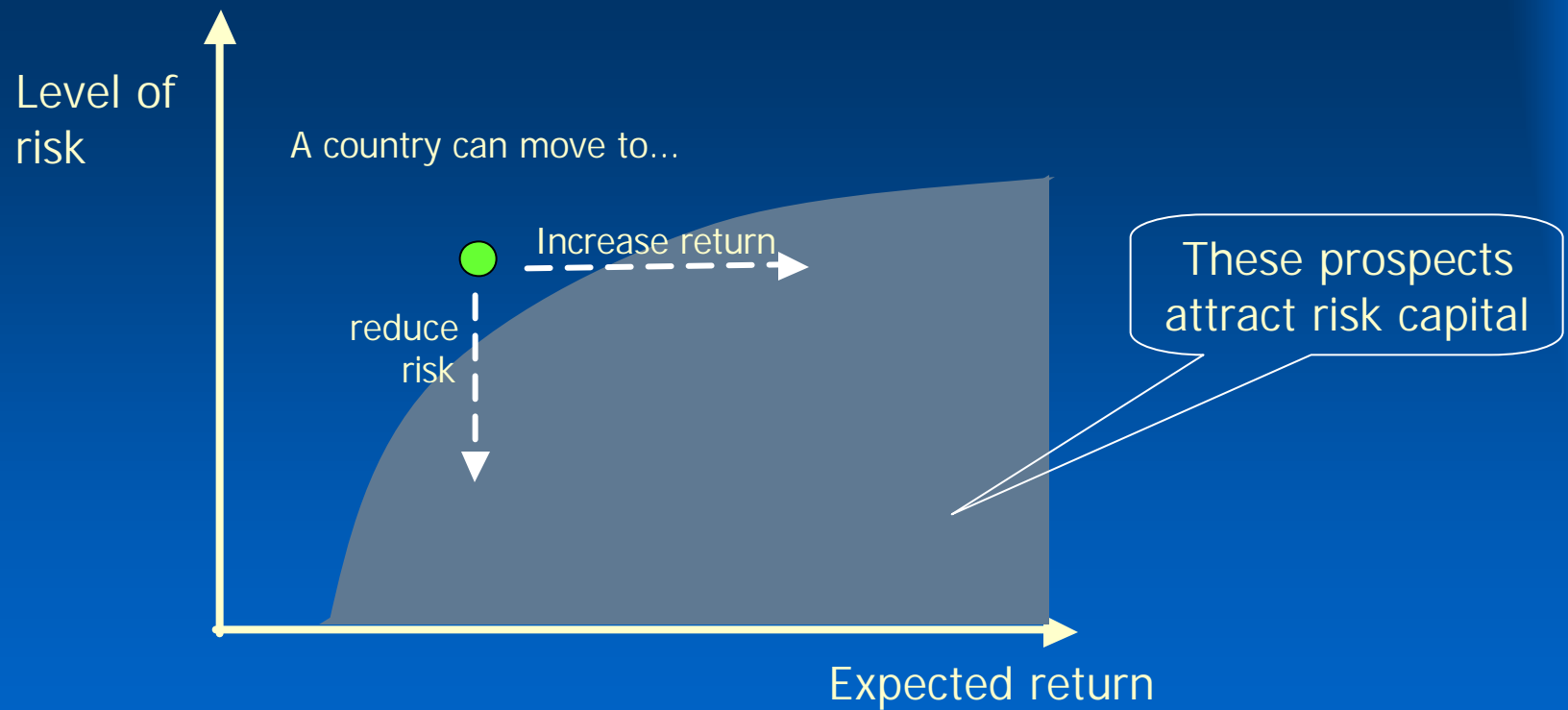


Source: IFC risk assessment, Mining Review



The risk-return equation

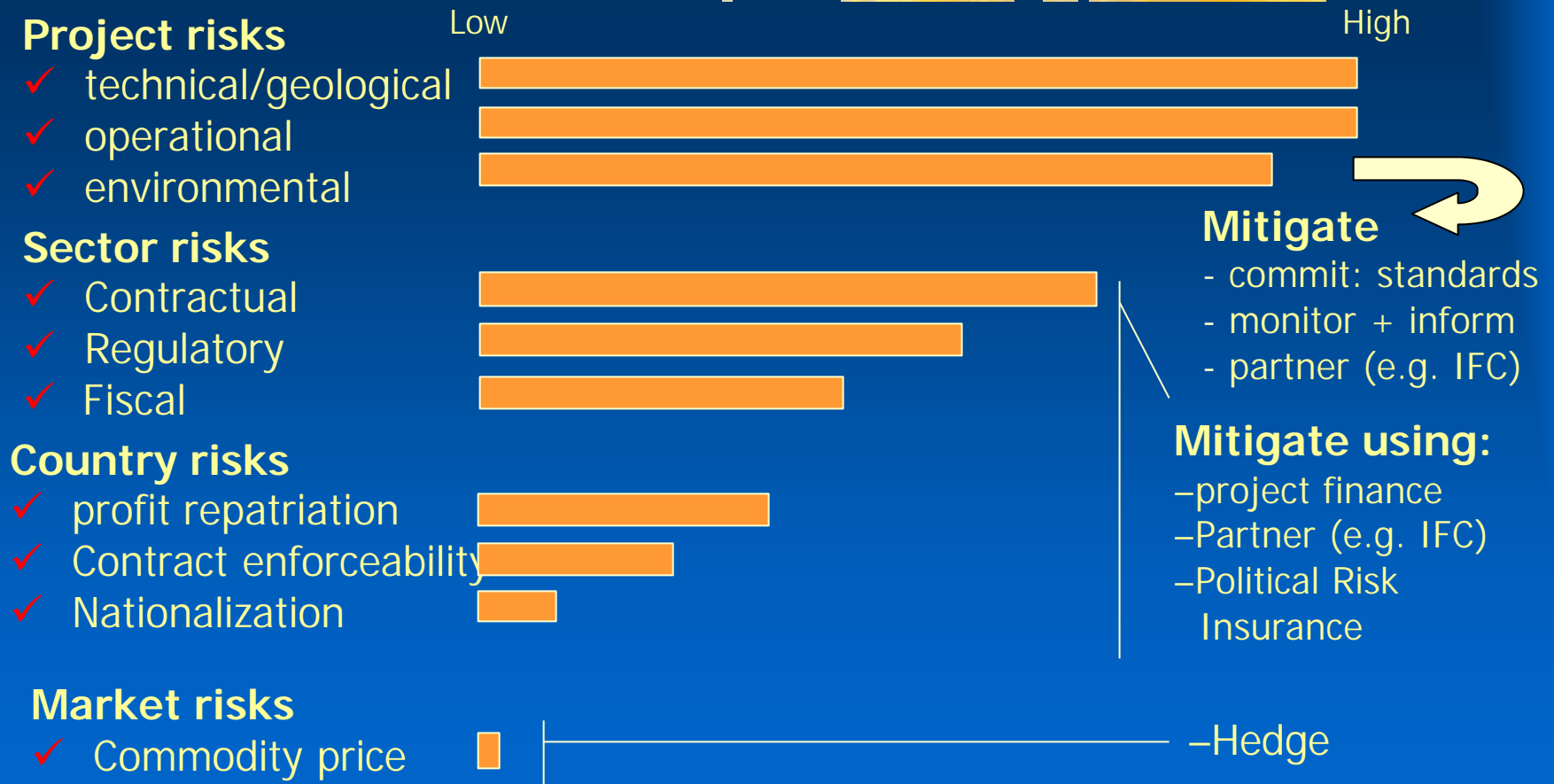
Do companies have any influence?





Managing investor risk

Degree of investor control over risk










Of course ... one can buy insurance

MIGA'S GUARANTEE PROGRAM

types of political risk coverage

- ❑ currency transfer restriction and inconvertibility
- ❑ expropriation
- ❑ war and civil disturbance
- ❑ breach of contract

Mining in a changing world

	<u>Decade of the 1980s</u>		<u>Late 1990s — 2000</u>
Macro-Economic	<ul style="list-style-type: none"> ✓ Macro/Sector reform ✓ Liberalization ✓ Some privatization of SOEs 		<ul style="list-style-type: none"> ✓ Dominance of Markets ✓ Shrinking State ✓ Decentralization
Government's Role in Mining	<ul style="list-style-type: none"> ✓ Owner/operator of mining assets 		<ul style="list-style-type: none"> ✓ Regulator/administrator
Private sector in Emerging Econs	<ul style="list-style-type: none"> ✓ By-stander in emerging economies 		<ul style="list-style-type: none"> ✓ Leading force in investment ✓ New responsibilities ✓ Role of NGOs
Environment	<ul style="list-style-type: none"> ✓ Awakening, acceptance 		<ul style="list-style-type: none"> ✓ Beginning to integrate
Social Focus	<ul style="list-style-type: none"> ✓ Benign neglect 		<ul style="list-style-type: none"> ✓ Awakening, acceptance



How does the risk-return profile of mining fit into these changes?

- ❑ Project mining risks: geology and technology
- ❑ Project implementation risks
 - 'goodwill' from local and national government
 - environmental performance
 - project social sustainability
- ❑ Sector and Country risks: transparency and predictability
 - Weak governance
 - Levels of corruption
 - Quality of mining code
 - Enforceability of contracts
- ❑ Returns are a function of
 - Geology and technology
 - Infrastructure
 - Levels of taxation
 - commodity prices



Civil Society demands for “sustainability” are changing perspectives everywhere

Governments

- ✓ Regulatory changes for several sectors
- ✓ Emphasis on “social/ethical” responsibility

Customers

- ✓ Demand “feel good” products

Firms

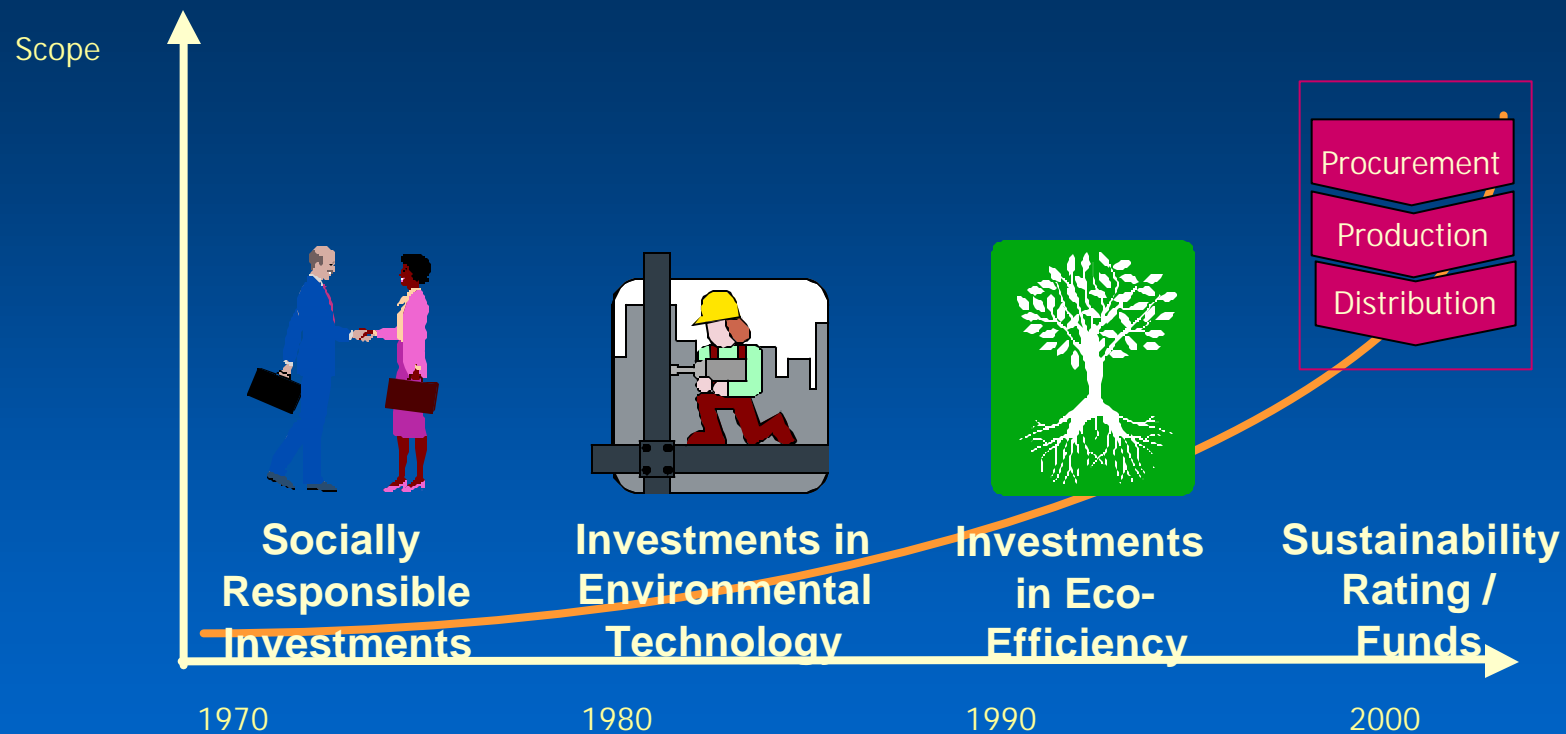
- ✓ Find “non-sustainable” operations increasingly costly
 - ✓ Reputational risks
 - ✓ Implementation risks
 - ✓ Liabilities
- ✓ Develop “Corporate Responsibility”



The Financial Sector is discovering “sustainability risks”

- ❑ Social and ethical factors in investment assessment on the rise
 - ✓ Nearly 80% of London fund managers: social and ethical factors to become important factor in company ratings
- ❑ Clients drive selective divesting as well as investing
 - ✓ One out of eight fund managers has sold shares or divested as a result of external pressure
- ❑ “Socially responsible” investments are massively growing
 - ✓ One out of \$8 under management is invested in “socially responsible” categories, up 82% from 1997
- ❑ **“Sustainability” rated companies tend to deliver better returns**
 - ✓ Dow Jones Sustainability Index, West Pac Eco fund, ...

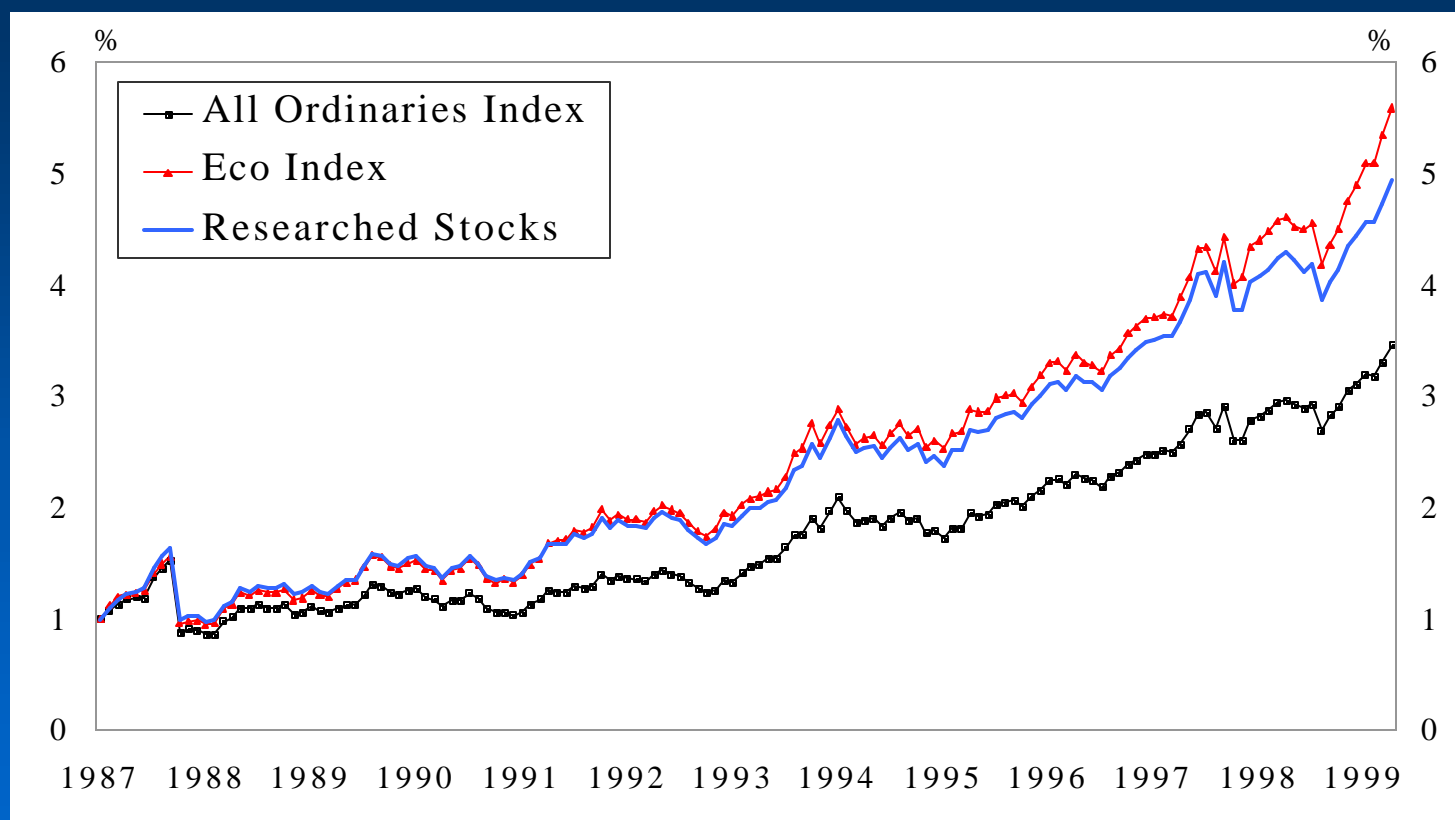
Financial products responding to societal changes have evolved over the past years





Sustainability - Is there a "business case"?

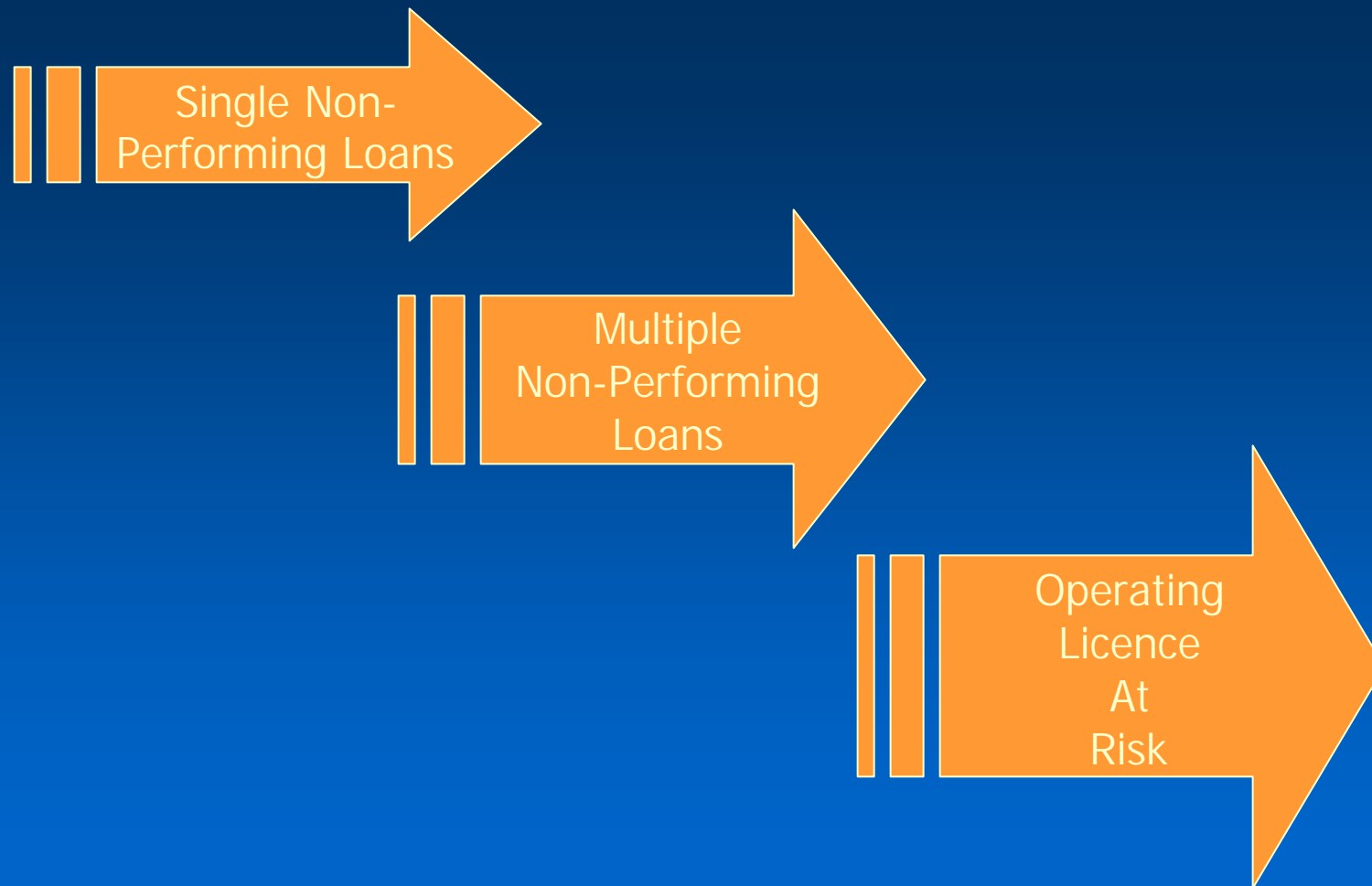
"Sustainability" ranked shares perform better



Source: WestPac



Lack of performance on "sustainability": Creates different types of risk to Financial Sector





Multiple Non-Performing Loans: Sectors at Risk

Until recently

- Wood Processing
- Fisheries
- Tuna
- Bananas
- Textiles
- Pulp and Paper
- Fur Products
- Nuclear
- Hydropower/Dams
- Tourism
- Asbestos
- Dairy



The next generation

- Coffee Tea
- Flowers
- Diamonds
- Mining (Gold, coal, iron ore, copper)
- Oil&Gas
- Mobile Phones
- Petrochemicals
- Tanneries

Operating license for the Financial Sector

Increasingly: Stakeholders and Clients prefer "feel good" stocks



Source: WestPac



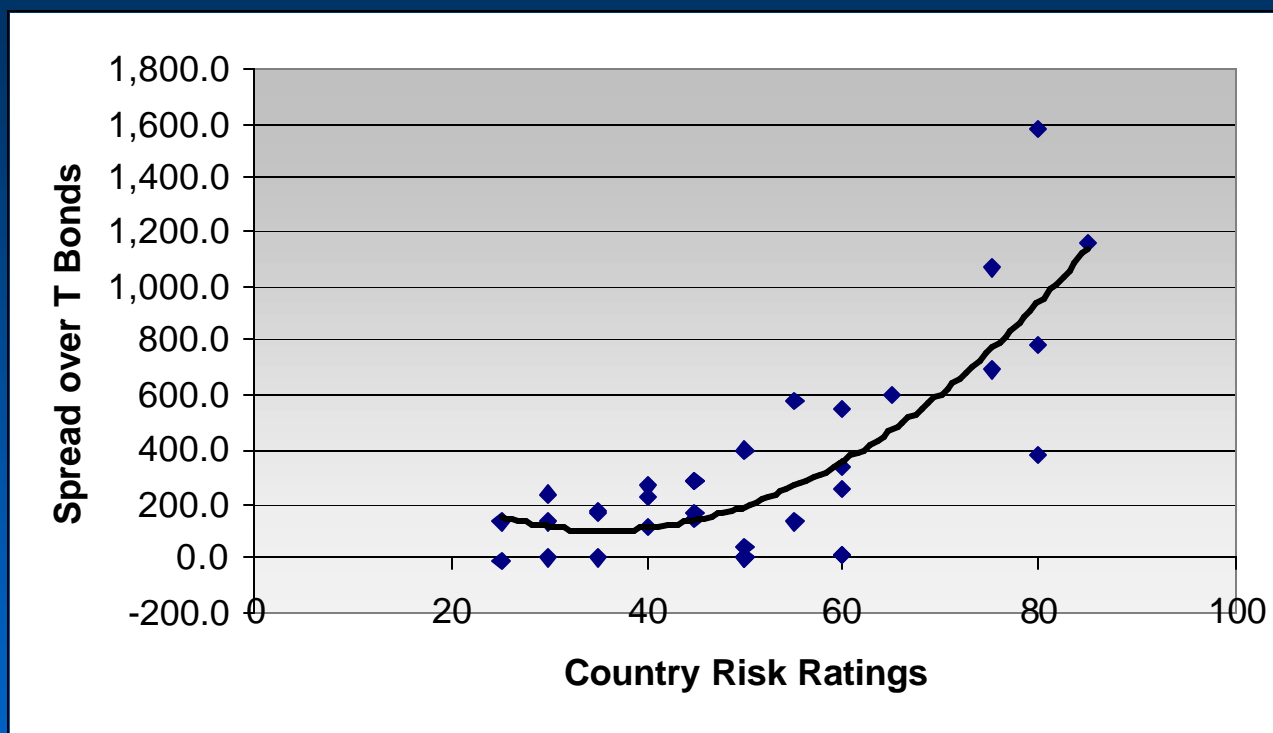
Operating License effects

- ❑ ***Shareholders:*** withdrawal, shareholder resolutions
- ❑ ***Raters:*** watch notice
- ❑ ***Analysts:*** Downgrade
- ❑ ***Central bank regulators:*** increased supervision, audit conditionality
- ❑ ***IFIs:*** withdrawal of funds, reduced term
- ❑ ***Lenders:*** withdrawal of funds
- ❑ ***NGOs/Consumers:*** boycott of products
- ❑ ***Co-financiers:*** liabilities for negligence, misrepresentation
- ❑ ***Insurers:*** Reduced coverage, increased cost



Financial markets want to be paid for taking risks

High risk countries warrant higher spreads

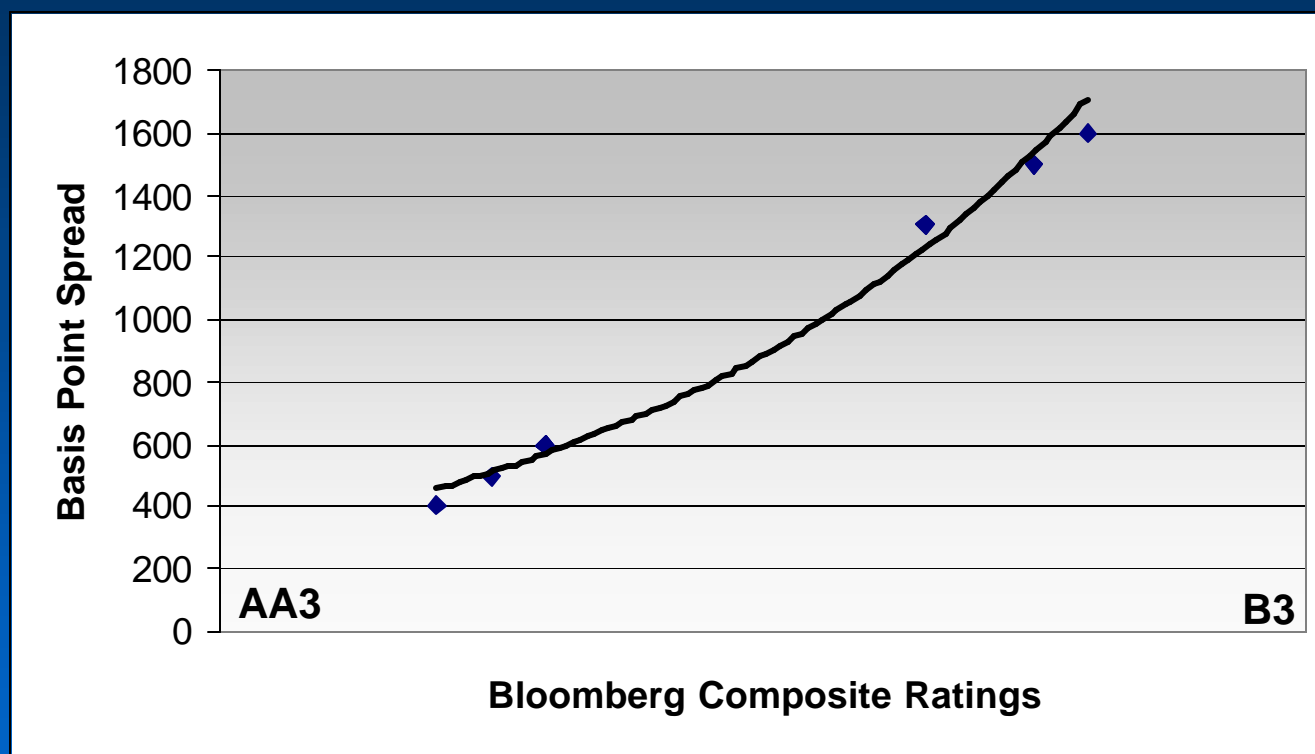


Source: IFC country risk rating, economics department



Financial markets want to be paid for taking risks

Companies with lower ratings warrant higher spreads



Source: Bloomberg

Sustainability trends in Finance - When and where will they “push” mining firms?

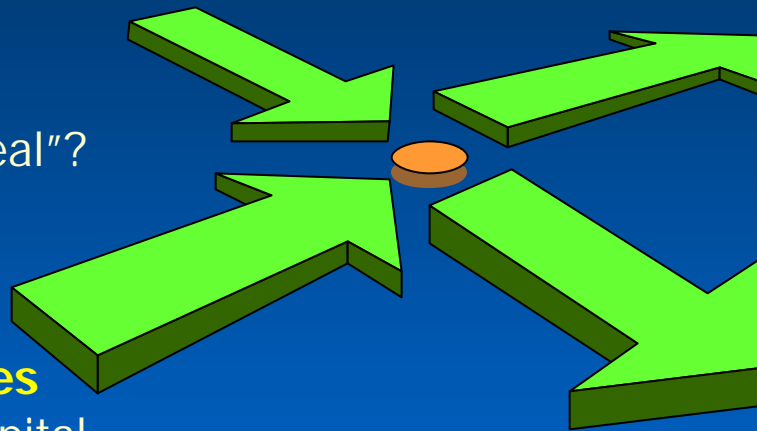
Emerging Trends in Finance

Directions

- ✓ Sectors?
- ✓ Does firm size matter?
- ✓ Increasing?
- ✓ PR or “for real”?

Consequences

- ✓ Access to capital
- ✓ Cost of capital
- ✓ Ratings
- ✓ Avoiding risks vs. increasing returns



Does mining need change?

Competitive Advantage?

Tarnished Image for the Industry?

- ✓ Differentiation possible?
- ✓ How?

Industry wide solution?

- ✓ Apply guidelines?
- ✓ Reporting?
- ✓ Certification?
- ✓ Regulation?



www.ifc.org/mining

www.worldbank.org/mining