

## AFRICA RISK CONSULTING

### Guinea Monthly Briefing November 2016

#### Guinea Summary 30 November 2016

**United Kingdom (UK)-based Rio Tinto Group announces the signature of a non-binding agreement to sell its 46.6% stake in Simandou mine operator Simfer S.A. to China-based Aluminium Corp of China Ltd (Chinalco) for \$1.1-1.3 billion. Rio Tinto loses two senior executives after notifying anti-corruption authorities of an internal investigation into a \$10.5m consultancy payment to a French adviser in 2011. President Alpha Condé (2010-present) meets with China's president Xi Jinping (2012-present) to strengthen economic and political ties.**

#### Rio Tinto sells Simandou stake to Chinalco

**United Kingdom-based Rio Tinto Group** announced on 28 October that it will sell its 46.6% stake in the **Simfer S.A.** joint-venture to **China** state-owned minor shareholder **Aluminium Corp of China Ltd (Chinalco)** for \$1.1 to 1.3 billion.<sup>1</sup> Simfer is especially significant as it holds concessionary rights to the **Simandou** iron ore mine. Rio Tinto stated that the agreement comprises a non-binding agreement, with the binding agreement to be signed within six months.<sup>2</sup> Payment will be made in line with commercial production of the mine, on a per tonne basis, assuring longer-term revenues for Rio Tinto, and enabling Chinalco to avoid a lump sum or larger instalment-based payment.<sup>3</sup> In addition to Chinese state backing, Chinalco also benefits from China being the world's single largest consumer of iron ore.<sup>4</sup> As such, the investment would appear a logical move for the Chinese government's strategic interests. China already produces and smelts approximately half of the world's iron ore, which will further strengthen its ability to influence market prices.<sup>5</sup> The Simandou project, when fully operational, will reportedly double **Guinea's** national gross domestic product (GDP).<sup>6</sup>

The announcement comes just a month after the **World Bank Group's International Finance Corp's (IFC)** sale of its 4.6% stake in Simfer for approximately \$200m (see *ARC Briefing Guinea October 2016*). Although full details of the sales have not been confirmed, presumably Chinalco, with the majority of capital in the project, will reclaim both the IFC's and Rio Tinto's shares. Acquisition of both of these stakes would take Chinalco's share in Simfer to 92.5%, with the remaining 7.5% belonging to the Guinean government.<sup>7</sup> Commentators view this as a positive step for Guinea,

*"President **Alpha Condé's** (2010-present) government has been praying for more decisiveness with regards to Simandou. Rio Tinto's apprehension actually made Condé very unpopular over the last few months. The retraction of both Rio Tinto and IFC must be seen as a good thing, as Chinalco will provide the much-needed investment to launch this project and bring the benefits to the Guinean people sooner."<sup>8</sup>*

Following Rio Tinto's appointment of **Jean-Sébastien Jacques** to the position of global CEO in July, the company employed a largely risk-averse strategy, with immediate shelving of the project (see *ARC Briefing Guinea July 2016*). This raised significant doubts about medium-term development of the

<sup>1</sup> GuinéeTime, 1 Nov 2016.

<sup>2</sup> www.riotinto.com

<sup>3</sup> www.riotinto.com

<sup>4</sup> Reuters, 28 Nov 2016.

<sup>5</sup> www.usgs.gov

<sup>6</sup> Reuters, 28 Nov 2016.

<sup>7</sup> GuinéeTime, 1 Nov 2016.

<sup>8</sup> Source, journalist, Conakry

world's largest untapped high-grade iron ore reserve, especially if low commodity price market conditions continue. However, market conditions have improved favourably in recent months – the iron ore spot index on 29 November exceeded \$80 a tonne, thereby returning to pre-October 2014 levels.<sup>9</sup>

The sale marks a conclusion to the tumultuous period since Rio Tinto first obtained concessionary rights to the Simandou mine in 1997.<sup>10</sup> Rio Tinto owned the entire Simandou concession until 2008 when the government of former president **Lansana Conté** (1984-2008) took away Rio Tinto's share in blocks 1 and 2 (**Simandou North**), assigning them to **BSG Resources Ltd (BSGR)**, mining company of **Israeli** businessman **Beny Steinmetz**.<sup>11</sup> Rio Tinto retained blocks 3 and 4 (**Simandou South**) but entered a dispute with the government for the blocks. BSGR officially paid nothing for the concession, although claimed to have invested \$160m in order to produce a feasibility study.<sup>12</sup> After Conté's death, BSGR sold 51% of its interest to **Brazil-based Vale S.A** for \$2.5 billion, though only paid \$500m of this after development milestones were missed.<sup>13</sup> In 2010, Condé's new government set up a committee to review the approval of past mining contracts. The committee in 2011 concluded that BSGR obtained blocks 1 and 2 through bribery.<sup>14</sup> Rio Tinto then settled its dispute with government for blocks 3 and 4, for which Rio Tinto paid a \$700m fee.<sup>15</sup> Rio Tinto then began litigation in the **United States (US)** against Vale and BSGR in order to seek damages. In November 2015 the **US District Court for the Southern District of New York** dismissed Rio Tinto's lawsuit against Vale and BSGR over the disputed concessions (see *ARC Briefing Guinea November 2015*) on the grounds that the statute of limitations applied against Rio Tinto.<sup>16</sup> BSGR is still embroiled in legal investigations and cases in the **US, France, Switzerland** and Guinea over the allegations of bribery.<sup>17</sup>

### Rio Tinto loses two executives after admitting to \$10.5m consultancy payment

Rio Tinto lost two senior executives on 16 November after notifying anti-corruption authorities in the **US, United Kingdom (UK)** and **Australia** on 9 November about an internal inquiry.<sup>18</sup> Rio Tinto suspended energy and minerals chief **Alan Davies**, while **Debra Valentine** resigned from her position as legal & regulatory affairs group executive.<sup>19</sup> Rio Tinto alerted **US Justice Department, Securities and Exchange Commission (SEC)**, the **UK Serious Fraud Office (SFO)** and **Australian Securities and Investments Commission (ASIC)** of an internal inquiry into a \$10.5m consultancy payment.<sup>20</sup> The announcement came just over a week after its non-binding agreement to sell its stake in the Simandou mine (see above). Rio Tinto claims that on 29 August it became aware of details of a \$10.5m consultancy fee to **François Polge de Combret** in 2011, contained in internal e-mail correspondence between then chief executive **Tom Albanese**, iron ore head **Sam Walsh** and Davies, then Simandou project head.<sup>21</sup> Rio Tinto later terminated Davies' contract.<sup>22</sup> Rio Tinto executives claim the fee was used to secure blocks 3 and 4 of the Simandou mine.<sup>23</sup> De Combret is a former adviser to former French president **Valéry Giscard d'Estaing** (1974-1981) and reportedly a former classmate of Condé'.<sup>24</sup> In the e-mails, Davies referred to de Combret's closeness to Condé,

<sup>9</sup> Multiple sources: Reuters, 29 Nov 2016; www.vale.com

<sup>10</sup> The Economist, 6 Dec 2014.

<sup>11</sup> Economist, 6 Dec 2014.

<sup>12</sup> Globe & Mail, 2 Oct 2015.

<sup>13</sup> Multiple sources: Bloomberg, 18 Nov 2016; www.mining.com

<sup>14</sup> Economist, 6 Dec 2015.

<sup>15</sup> Economist, 6 Dec 2014.

<sup>16</sup> www.nysd.uscourts.gov

<sup>17</sup> Bloomberg, 18 Nov 2016.

<sup>18</sup> www.riotinto.com

<sup>19</sup> www.riotinto.com

<sup>20</sup> www.riotinto.com

<sup>21</sup> Australian Financial Review, 10 Nov 2016.

<sup>22</sup> Bloomberg, 18 Nov 2016.

<sup>23</sup> Australian Financial Review, 10 Nov 2016.

<sup>24</sup> Financial Times, 10 Nov 2016.

*“I accept that this is a lot of money, but I also put forward that the result we achieved was significantly improved by Francois’ contribution and his very unique and irreplaceable services and closeness to [Condé]. He vouched for our integrity when it was needed and helped bring us together when things were looking extremely difficult. These services were of the most unique nature, and we will never fully be able to judge the potential outcome if he was not assisting in us in good faith.”<sup>25</sup>*

Davies claimed that de Combret “behaved with the utmost integrity” and stated that he “helped [Davies] on a number of communication issues with [Condé] and [then mines minister] **Mohamed Lamine Fofana**.”<sup>26</sup> Rio Tinto appointed Davies energy and minerals chief executive in July 2016, and the company immediately suspended Davies after making the statement.<sup>27</sup> Valentine was also a board member of sector-wide accountability advocate **Extractive Industries Transparency Initiative (EITI)**.<sup>28</sup> Albanese stepped down as group chief executive in 2013 while Walsh stepped down from this same position in July 2016.<sup>29</sup> Anti-corruption group **Transparency International** Australia representative, **Anthony Whealy** says that these are positive steps but do not necessarily show a change in corporate governance,

*“The company did self-report and people have been stood aside, but that doesn’t tell a lot about the ethical governance within Rio Tinto.”<sup>30</sup>*

In response to the events, Davies published a statement confirming that he would begin litigation against Rio Tinto,

*“Rio Tinto has made no effort to abide by due process or to respect my rights as an employee and it has given me no opportunity to answer any allegation. This treatment of me and my past and recent colleagues is totally at variance with the values and behaviours of the company to which I have devoted my professional life... My rights are fully reserved, and I have been left with no option but to take the strongest possible legal action in response.”<sup>31</sup>*

Despite this, current CEO Jacques claimed that “the board’s decision [to sack Davies] is not in any way meant to prejudice the course of any external inquiries on this matter.”<sup>32</sup> This appears somewhat contradictory, especially as this communicates a public view from within Rio Tinto that Valentine and Davies were responsible for this payment, without proof that it consisted of corrupt payment or breach of anti-corruption laws.

### Condé meets Jinping in Beijing

President Condé on 2 November met Chinese president **Xi Jinping** (2012-present) in **Beijing** to consolidate strategic economic and political ties.<sup>33</sup> The meeting was not on Condé’s agenda, and was presumably scheduled soon after Chinalco acquired Rio Tinto’s stake in the Simandou mine (see above). Outside of habitual protocol, Condé revealed more information concerning the nature of Sino-Guinean relations for the Simandou project, without specifically referring to the project. Condé said that “we will provide raw material to China, and in return, China will give us infrastructure.”<sup>34</sup> Chinalco is likely to take over responsibility for the construction of the planned 650km railway that would connect the Simandou mine to the coast, also building another mineral port.<sup>35</sup> Beyond this, Condé

<sup>25</sup> Australian Financial Review, 10 Nov 2016.

<sup>26</sup> Australian Financial Review, 10 Nov 2016.

<sup>27</sup> www.riotinto.com

<sup>28</sup> Financial Times, 10 Nov 2016.

<sup>29</sup> Financial Times, 10 Nov 2016.

<sup>30</sup> Reuters, 10 Nov 2016.

<sup>31</sup> Bloomberg, 16 Nov 2016.

<sup>32</sup> Australian Financial Review, 10 Nov 2016.

<sup>33</sup> www.guineeconakry.info

<sup>34</sup> Africa Guinée, 2 Nov 2016.

<sup>35</sup> Jeune Afrique, 4 Nov 2016.

hinted that Chinese aid would help to build roads, airports, ports, energy and agriculture.<sup>36</sup> Condé stated that Guinea is also seeking to collaborate further with the **China International Water and Electric Corp (CWE)**.<sup>37</sup> CWE has already made investments in Guinea in the form of the \$446m **Kaléta** hydroelectric dam, launched in September 2015.<sup>38</sup> CWE and the Guinea government in January signed an extension to this project, seeking a \$1.3 billion investment in order to redevelop the **Souapiti** dam launched in 1956.<sup>39</sup> Analysts believe that Condé is seeking further funding from China to enable its redevelopment over the coming months.<sup>40</sup> An anonymous member of the Guinea delegation claimed that Condé is seeking further financing from China in order to accelerate several major infrastructural projects.<sup>41</sup>

## Implications

The sale of Rio Tinto's stake to Chinalco is largely a positive development for Guinea insofar as assuring investment into the Simandou mine. Once Chinalco and Rio Tinto consolidate the terms of the agreement, communication about Chinalco's proposed investment and development timeline should follow. Market conditions have also improved for iron ore, which will act as a further incentive to accelerate the investment plan.

Anti-corruption authorities' investigations are likely to take a long time to complete, and therefore it will be difficult to evaluate, until then, the true nature of the payment to de Combret. It is clear that Rio Tinto has chosen rather to act hastily, suspending Davies and allowing Valentine to leave in order to avoid greater brand and reputation damage. For the moment there is no indication that the payment breached anti-corruption laws.

The sale of Simandou to Chinalco has consolidated further Guinea's dependence on China for economic development. The duration of progress on these projects will depend on the willingness of Chinese officials to afford the Guinean government further funding for major infrastructural projects.

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<sup>36</sup> Jeune Afrique, 4 Nov 2016.

<sup>37</sup> Jeune Afrique, 4 Nov 2016.

<sup>38</sup> Jeune Afrique, 4 Nov 2016.

<sup>39</sup> Jeune Afrique, 4 Nov 2016.

<sup>40</sup> Jeune Afrique, 4 Nov 2016.

<sup>41</sup> Jeune Afrique, 4 Nov 2016.

### About Africa Risk Consulting:

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