

## AFRICA RISK CONSULTING

### Zambia Monthly Briefing February 2019

#### Zambia Summary 6 February 2019

*Mines minister Richard Musukwa confirms that the board of state-owned mining investment company, Zambia Consolidated Copper Mines-Investment Holdings Ltd (ZCCM-IH), fired chief executive officer Pius Kasolo due to his negative comments about the new mining tax regime. Canada-based mining company First Quantum Minerals reportedly offered the government \$700m in 2018 to purchase ZCCM-IH's 20% stake in Kansanshi Mining Plc, which would give First Quantum 100% ownership of the Kansanshi mine. Zambia's Eurobond has been the best performing emerging market sovereign bond thus far in 2019, delivering a higher return than any of the 75 nations (excluding Venezuela) in the Bloomberg Barclays Emerging Markets USD Sovereign Bond Index.*

#### Government holds firm on mining tax but may offer individual concessions

Zambia's mines minister, **Richard Musukwa**, confirmed on 1 February that the board of the state-owned mining investment company, **Zambia Consolidated Copper Mines-Investment Holdings Ltd (ZCCM-IH)**, fired chief executive officer, **Pius Kasolo**, due to his negative comments about the new mining tax regime.<sup>1</sup> Kasolo's dismissal shows that the government intends to hold firm on the tax regime and will not change it unless there is proof of major economic hardship, though mining companies may find that the government is open to individual negotiations for concessions. Kasolo stated to reporters on 28 January that the new tax regime would hurt ZCCM-IH, as it holds shares on behalf of the government in mining companies:<sup>2</sup>

*"At the moment, taxes have not come to fruition but by projection the move will affect ZCCM-IH because we get dividends from the companies."<sup>3</sup>*

The government clearly disagreed with Kasolo's outlook on the new mining taxes. The president's office reportedly instructed Kasolo not to stray from the party line that the new taxes would not hurt mining companies.<sup>4</sup> After announcing Kasolo's dismissal, Musukwa claimed that the new taxes would not hurt ZCCM-IH and that some mining companies are even looking to invest further in new mining projects.<sup>5</sup> Musukwa is correct in one regard: **United Kingdom**-based mining company **Vedanta Resources**, which owns the **Konkola Copper Mine** with ZCCM-IH, announced on 28 January that it would not fire any workers and would continue its expansion plans.<sup>6</sup> However Vedanta has shut down some smelter operations due to the new taxes and **Canada**-based **First Quantum Minerals** has said it will need to fire some workers (see *ARC Briefing Zambia* January 2019).

Vedanta's announcement came after a meeting with the government, including finance minister **Margaret Mwanakatwe**, over the new tax regime.<sup>7</sup> There is no indication of what the government said or offered to Vedanta to result in the new optimism over the mining taxes, but it indicates that the government realises it may have over-reached in its attempt to raise revenue to lower its growing debt. While the government is not yet reviewing the tax changes, **Zambia Chamber of Mines (ZCM)**

<sup>1</sup> Lusaka Times, 1 Feb 2019

<sup>2</sup> Zambia Reports, 1 Feb 2019

<sup>3</sup> Pius Kasolo quoted in Zambia Reports, 1 Feb 2019

<sup>4</sup> Zambia Watchdog, 1 Feb 2019

<sup>5</sup> Zambia Watchdog, 1 Feb 2019

<sup>6</sup> Mining Weekly, 30 Jan 2019

<sup>7</sup> Mining Weekly, 30 Jan 2019

president **Goodwell Mateyo** said at a presentation in **Cape Town (South Africa)** on 5 February that there is a precedent for this:

*“The government has in the past decreased mining taxes. It has changed the mining tax laws ten times in sixteen years and there is a precedent of taxes being decreased. However, the government will only do that if it sees that the new tax regime is actually reducing its revenues.”<sup>8</sup>*

A reduction in the government’s revenue from mining appears likely. According to a ZCM-commissioned report, the new tax regime makes Zambia the highest-cost mining country in the world,<sup>9</sup> and the government’s estimates that the new tax will increase revenue by over \$150m is grossly overstated.<sup>10</sup> According to Mateyo,

*“...it is very likely that the government will see falling revenues due to these taxes which, as stated, may make them go back to the drawing board on the mining taxes.”<sup>11</sup>*

The reduction of mining revenue will affect the treasury and may reduce the forecasted growth. The **African Development Bank** forecast 4% growth in 2019 on the back on mining production continuing to rise,<sup>12</sup> but the new taxes may result in companies not reaching their previous production targets. Any change to the mining tax will not happen until at least the end of 2019, after the government is able to see the economic figures for the financial year. Mwanakatwe said on 5 February that the government will not consider a review to the tax regime before then:

*“There is no renegotiation taking place because a law has been passed in parliament to change the tax regime. We don’t want to keep changing regimes frequently. We want a regime that is stable, that can ensure that government gets a fair share of revenue to supports its development agenda. I can’t see a royalty tax changing.”<sup>13</sup>*

Despite this, and perhaps to illustrate the deal with Vedanta, Musukwa and Mwanakatwe both said the government may make temporary concessions on an individual basis if companies can show they need them, or to encourage increased local production.<sup>14</sup> This stance allows the government to continue the publically popular taxes, while ensuring that the tax regime does not harm Zambia’s important mining sector and future investment in the sector.

### **First Quantum looks to purchase stake in ZCCM-IH and increase Kansanshi mine share**

First Quantum Minerals reportedly offered the government \$700m in 2018 to purchase ZCCM-IH’s 20% stake in First Quantum’s subsidiary **Kansanshi Mining Plc**, which would give First Quantum 100% ownership of the **Kansanshi** mine.<sup>15</sup> The deal consists of \$300m-\$400m in cash, with the balance to be paid in special royalties over 10 years.<sup>16</sup> The deal also stipulated that ZCCM-IH would have to drop a \$1.4 billion legal claim against First Quantum over a loan that First Quantum received from its subsidiary, Kansanshi Mining.<sup>17</sup> First Quantum and government spokespeople have not commented on the report, which appears to have resulted in confusion over what assets are to be sold. Finance minister Margaret Mwanakatwe did not mention the Kansanshi mine deal, but reportedly stated at the **Investing in African Mining Indaba** in Cape Town (4-7 February) that there are unsolicited bids for a 17% stake in ZCCM-IH:<sup>18</sup>

<sup>8</sup> Lecture, Cape Town, 5 Feb 2019

<sup>9</sup> Diggers, 7 Jan 2019

<sup>10</sup> Lecture, Cape Town, 5 Feb 2019

<sup>11</sup> Lecture, Cape Town, 5 Feb 2019

<sup>12</sup> 2019 African Economic Outlook

<sup>13</sup> Bloomberg, 5 Feb 2019

<sup>14</sup> Bloomberg, 5 Feb 2019

<sup>15</sup> Diggers, 6 Feb 2019

<sup>16</sup> Diggers, 6 Feb 2019

<sup>17</sup> Diggers, 6 Feb 2019

<sup>18</sup> Reuters, 5 Feb 2019

*“There are multiple unsolicited offers on the table, including from First Quantum, which are based on preferential share conversions. The offers related to the ministry’s 17% holding in ZCCM-IH and a sale would be subject to cabinet approval.”<sup>19</sup>*

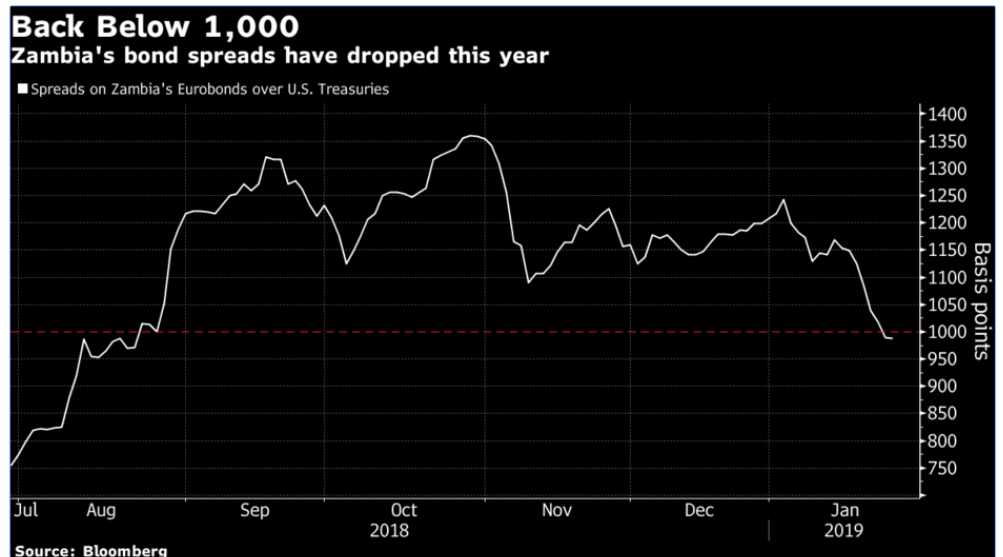
The ZCCM-IH shareholders include the **Industrial Development Corporation** (60.28%), the government, which is held through the finance ministry (17.25%), the **National Pension Scheme Authority** (15%), and remaining minor shareholders (7.47%).<sup>20</sup> It is unclear whether this was a communication error or whether First Quantum has asked to buy out the government’s shares in ZCCM-IH, but it is unlikely that the cabinet would approve a partial privatisation of the state-owned mining investment company. The communication error may be due to the government’s reported desire to sell ZCCM-IH’s stake in Kansanshi mine without too much public exposure. According to a Zambia-based political analyst, the government fired ZCCM-IH CEO Pius Kasolo due to his refusal to allow the sale of the 20% stake (see above) and, with Pius removed, President **Edgar Lungu** (2015-present) is moving fast to conclude the deal.<sup>21</sup> However, Lungu will be unable to conclude this deal quietly as ZCCM-IH is listed on the **Lusaka Securities Exchange**, which requires a cautionary note for any company wishing to dispose of assets.<sup>22</sup> The ZCCM-IH shareholders and board will also need to approve the transaction, so even without Kasolo in charge, Lungu will have many obstacles in front of him before the deal can be concluded.<sup>23</sup>

There is still much information missing in regards to the reported deal and the government’s reports of unsolicited offers for ZCCM-IH shares, but First Quantum’s acquisition of the remaining 20% shares of Kansanshi mine would be positive for both the government and First Quantum. The government would earn some much needed revenue in the short- and long-term while First Quantum would have total control over its mine, at the same time signalling to other mining companies that it is invested for the long term in Zambia.

### Zambian Eurobond one of best performing emerging market bonds in 2019

Zambia’s **Eurobond** has been the best performing emerging market sovereign bond thus far in 2019, delivering a higher return than any of the 75 nations (excluding **Venezuela**) in the **Bloomberg Barclays Emerging Markets USD Sovereign Bond Index**.<sup>24</sup> The high

return is by no means a sign that the economy has improved in Zambia and investors should still be wary of the government’s high debt and the lack of an **International Monetary Fund** bailout, at least in the short term. Zambia’s Eurobond



<sup>19</sup> Reuters, 5 Feb 2019

<sup>20</sup> www.zccm-ih.com.zm

<sup>21</sup> Lusaka Times, 6 Feb 2019

<sup>22</sup> www.luse.co.zm

<sup>23</sup> Lusaka Times, 6 Feb 2019

<sup>24</sup> Bloomberg, 28 Jan 2019

has offered a 10.3% return since the end of December, though the enthusiasm for the bond is due less to government improvements than investors' increased appetite for risky assets.<sup>25</sup> Some asset managers see Zambia, as well as **Bahrain** and **Papua New Guinea**, as the bonds with the best returns in 2019.<sup>26</sup> Zambia's spread (the difference between the yields of two bonds) against the **United States** Treasury notes has dropped from a high of around 1,350 basis points to under 1,000. While it is an increase, the 988 basis points are still the highest in emerging markets which are not in default which will still keep more risk averse investors away from investment into Zambia in any sector other than its sovereign bonds.

There has been debate and concern both in Zambia and within international financial institutions about Zambia's risk of debt distress. The **World Bank's International Development Association (IDA)** described Zambia's risk of external debt distress as "high" in its 4 October report on Debt Vulnerabilities in IDA countries. In its latest **African Economic Outlook** report, the **African Development Bank (AfDB)** notes that in 2018, Zambia's domestic debt was estimated at 20% of GDP while external debt, including government guarantees, fell to an estimated 39.2% of GDP. The AfDB noted that the Zambian government had announced measures aimed at improving debt sustainability and returning to a rating of "moderate risk of debt distress" in order to improve investor confidence in Zambia. These measures include an indefinite postponement of new infrastructure projects and the cancellation of some contracted loans that are yet to disburse.<sup>27</sup>

### Planner

19 Feb 2019 **Lusaka (Zambia) Bank of Zambia** (central bank) interest rate decision  
 8-12 Apr 2019 **Livingstone (Zambia) Commonwealth Law Conference (CLC)**  
 11-13 Apr 2019 **Chisamba (Zambia) Agritech Expo Zambia**  
 13-14 Jun 2019 **Lusaka (Zambia) Zambia International Mining and Energy Conference and Exhibition (ZIMEC)**  
 26 Jun - 2 Jul 2019 **Ndola (Zambia) Zambia International Trade Fair**  
 12-13 Sep 2019 **Lusaka (Zambia) Zambia E-commerce Expo and Conference**  
 3-5 Oct 2019 **Lusaka (Zambia) Africa Food Manufacturing and Safety Summit Southern Africa (AFMASS Zambia)**  
 2021 **(Zambia) Scheduled presidential elections;**

### Chronology

5 Feb 2019 **Lusaka (Zambia) Mining Weekly**. State-owned mining investment company **ZCCM-IH** reportedly received bids from **Canada-based First Quantum Minerals** and others for a 17% stake;  
 5 Feb 2019 **Lusaka (Zambia) Business Day**. The **Anti-Corruption Commission** arrests infrastructure and housing minister **Ronald Chitotela** for concealing property alleged to have been purchased with proceeds of crime;  
 4 Feb 2019 **Lusaka (Zambia) Financial Post**. **Canada-based First Quantum Minerals Ltd** offered up to \$700m in 2018 for the government's 20% stake in the **Kansanshi** mine;  
 4 Feb 2019 **Lusaka (Zambia) Reuters**. Mining minister **Richard Musuka** announces that

<sup>25</sup> Bloomberg, 28 Jan 2019

<sup>26</sup> Bloomberg, 28 Jan 2019

<sup>27</sup> AfDB African Economic Outlook 2019

**Zambia** will enforce its new 5% copper import duty despite criticism of the new tax;

1 Feb 2019 **Lusaka (Zambia)** *CNBC Africa*. Mines minister **Richard Musukwa** fires **Pius Kasolo**, the CEO of state-owned mining investment arm, **Zambia Consolidated Copper Mines Investment Holdings (ZCCM-IH)**, for unknown reasons;

31 Jan 2019 **Lusaka (Zambia)** *Lusaka Times*. National development planning minister **Alexander Chiteme** asks the **Climate Investment Fund** to help expand investment in renewable energy in Zambia;

30 Jan 2019 **Lusaka (Zambia)** *Lusaka Times*. The **Public Procurement Authority** suspends **Budocoro Enterprises Ltd** and **R. Phiri Enterprises Ltd** for interfering with the participation of other suppliers;

29 Jan 2019 **Lusaka (Zambia)** *Bloomberg*. **United Kingdom**-based **Vedanta Resources** states that it will expand its mines and will not fire workers despite **Zambia's** new tax regime;

28 Jan 2019 **Lusaka (Zambia)** *Zambia Reports*. **Zambia's Eurobonds** return 10.3% at the end of December, one of the highest returns on **Bloomberg Barclays Emerging Market's** sovereign bond index;

22 Jan 2019 **Lusaka (Zambia)** *ZNBC*. **Turkey**-based energy company **Bendis Holdings** expresses interest in investing in **Zambia's** energy sector.

### About Africa Risk Consulting:

**Africa Risk Consulting (ARC)** is a pan-African consulting company that provides timely, relevant information and advice that enables its clients to take informed investment decisions and to safeguard their reputations.

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