Highlighting trends in the South African mining industry

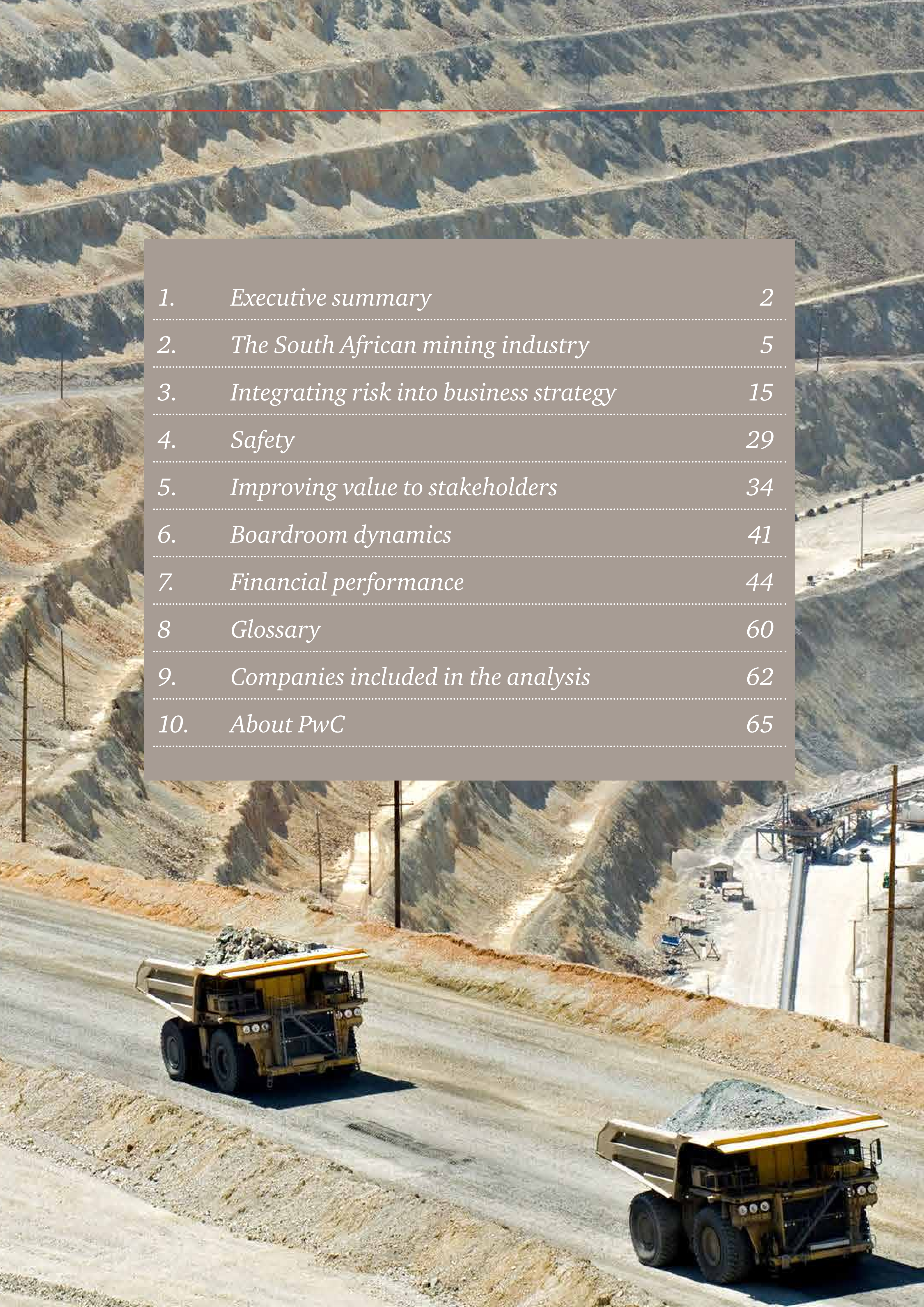
November 2014

SA Mine

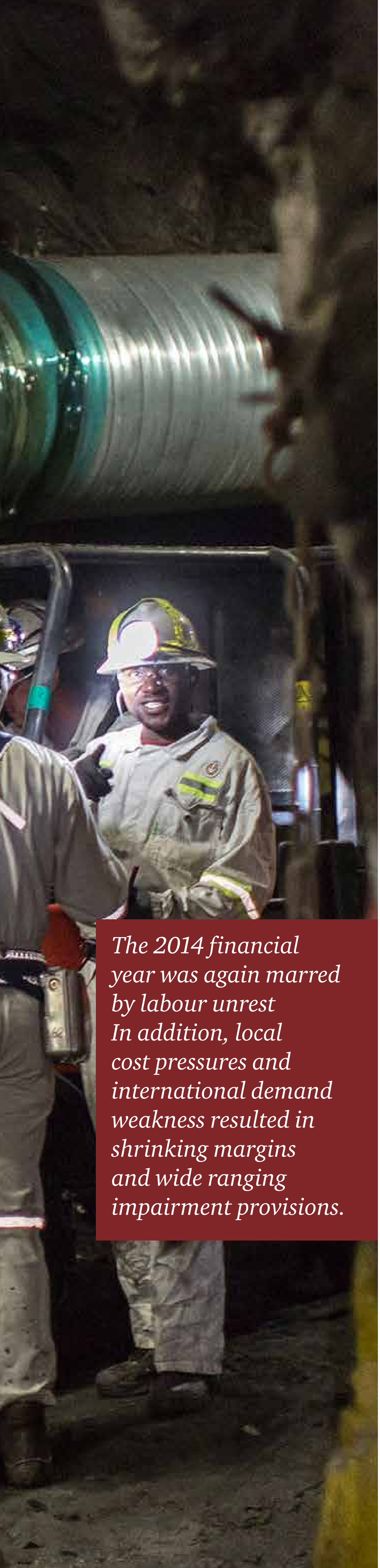
6th edition

www.pwc.co.za/mining

Contents



1. Executive summary



The 2014 financial year was again marred by labour unrest In addition, local cost pressures and international demand weakness resulted in shrinking margins and wide ranging impairment provisions.

Highlights

	Current year R ’billions	Prior year R ’billions	Difference R ’billions	% change
Revenue from ordinary activities	327	291	36	12%
Adjusted EBITDA	91	83	8	10%
Impairment charge	49	20	29	145%
Net profit	6	27	(21)	(78%)
Distribution to shareholders	19	29	(10)	(34%)
Net operating cash flows	70	75	(5)	(7%)
Capital expenditure	57	70	(13)	(19%)
Total assets	694	687	7	1%

This is the sixth in our series of annual publications highlighting trends in the South African mining industry.

The significant decrease in the industry’s profitability fuelled contraction in market capitalisation of South African mining stocks. This decrease is in line with global mining counterparts who are also struggling with higher costs and lower prices.

A weakening rand over the period somewhat shielded the South African mining industry from the decline, with rand prices remaining relatively flat. Unfortunately, flat prices will not support the industry’s significantly increased cost base.

Generally, balance sheets remained strong, with stable liquidity. However, increased gearing was needed for companies to fund sustaining capital expenditure and in some cases operating losses. The R49 billion impairment provisions raised highlights the difficulty in making long-term decisions in volatile markets.

Mining companies implement various strategies to mitigate the significant risks they face over their total life cycle.

The mining industry still adds significant value to the South African economy with regards to GDP contribution, employment, tax and export revenues. Leadership will be required from all stakeholders to ensure long-term optimisation of the industry as opposed to the threat of instant gratification claims by stakeholders.

Mining companies now need to integrate risk and performance management and they need to evolve risk management to be more predictive in order to anticipate and plan for potential negative events.

Mining charter requirements will be measured as at the end of 2014, with formal reporting thereon due in 2015. Most companies report good progress towards achieving targets with housing and equity at certain management levels still a challenge for some.

Safety statistics underline the long-term focus on safety and the resulting improvements achieved.

We trust you will find this publication to be of value and look forward to sharing future trends with you. We would appreciate any feedback you may have to share with us.

Hein Boegman
African Mining Leader

Andries Rossouw
Project Leader

Scope

Our findings are based on the financial results of mining companies with a primary listing on the Johannesburg Stock Exchange (JSE), as well as those with a secondary listing on the JSE whose main operations are in Africa.

We only included companies with a market capitalisation of more than R200 million at the end of June 2014 and excluded companies with suspended listings. In all, similar to last year, 37 companies met these criteria. Section 9 provides a list of all mining companies included in our analysis.

Although the number of entities did not change from the prior year, six new entities were included in the current year. Tharisa Plc was included after its listings during the year. Infrasors, Randgold & Exploration, Tawana Resources and Waterberg Coal Company were included after their market capitalisation grew to above the R200m threshold and Resource Generation was included as it started actively trading on the JSE.

Six companies from the prior year were excluded this year: Gold One and Palabora Mining Company were delisted after acquisitions by foreign investors. Sephaku Holdings was moved to the Construction and materials sector. Jubilee Platinum, Sentula Mining and Wits Gold have been excluded, as their market capitalisation has declined below the threshold noted above.

Our selection criteria excluded global mining companies Anglo American[1], BHP Billiton and Glencore Xstrata. Although these companies have significant South African operations, their global exposure and size mean that they do not necessarily reflect trends in the South African mining environment.

While many of the entities that are included also have international exposure, the bulk of their operations are in Africa. A global view on mining is provided in our Mine: Re-aligning expectations publication.[2]

The findings of this report are based on publicly-available information, predominantly annual reports, for financial years ending no later than 30 June 2014. Where annual reports were not available, we have used preliminary reviewed results.

1 Kumba Iron Ore and Anglo American Platinum are included in our analysis.

2 http://www.pwc.com/gx/en/mining/publications/mine-realigning-expectations.jhtml

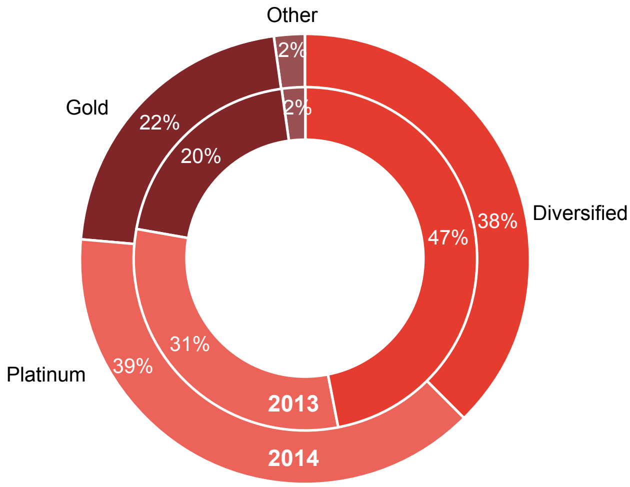
2. The South African mining industry

Market capitalisation

The 2014 financial year saw the declining trend in market capitalisation temporarily halted. Market capitalisation for the top 37 companies analysed in this publication increased marginally to R675 billion as at 30 June 2014 (R597 billion at 30 June 2013).

Platinum and gold companies generally recovered on the back of the weak rand and the hope of a more stable labour environment after the protracted platinum strike that lasted from January to June 2014. This improvement was partially offset by the significant decrease in iron ore and coal prices, which impacted the diversified companies. Anglo American Platinum showed the best recovery in market capitalisation with Kumba Iron Ore the hardest hit.

Figure 1: Market capitalisation by commodity



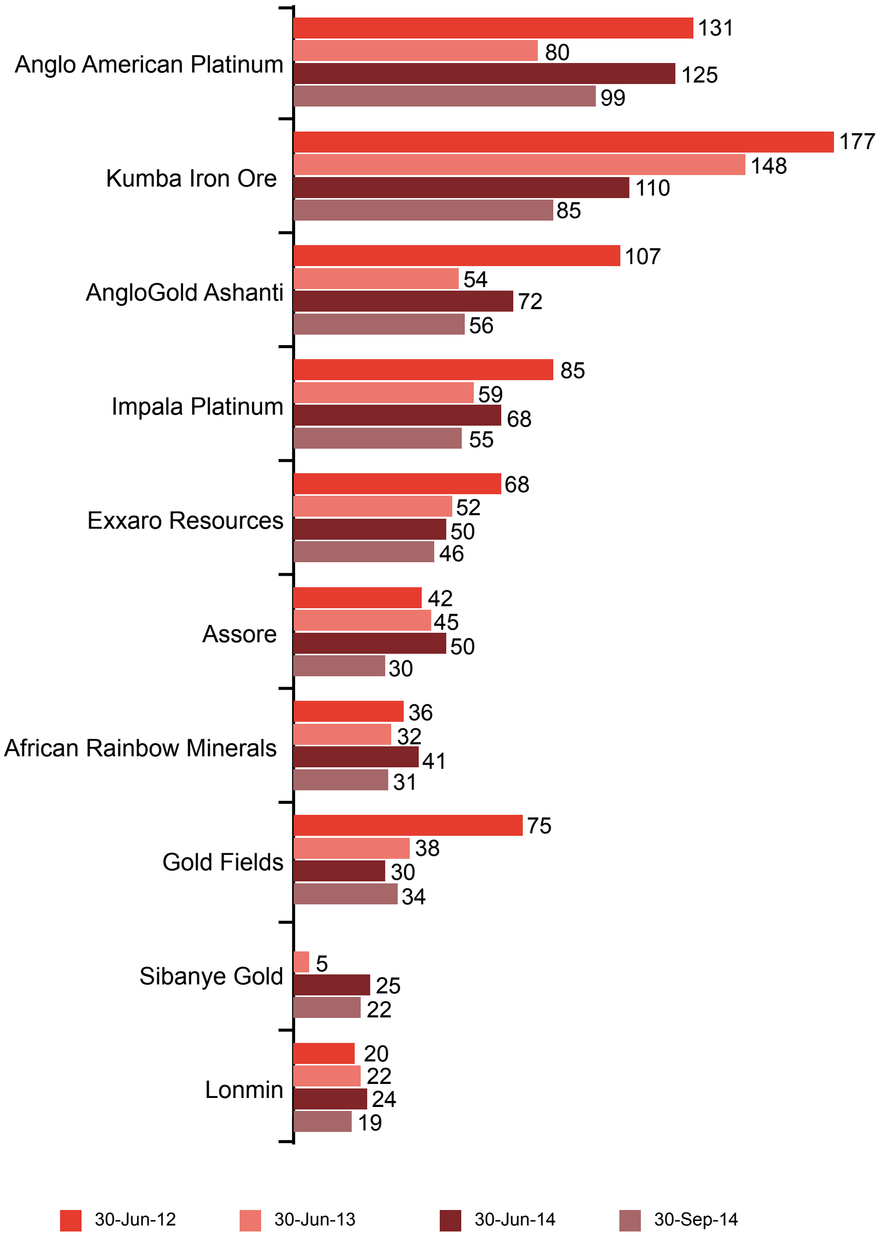
Source: PwC analysis

The declining market capitalisation trend of the top 10 entities was temporarily halted in June 2014 with a R60 million increase on the prior year to R594 billion. Unfortunately, the slide subsequently continued and as at 30 September 2014 the top 10 dropped to R478 billion.

In September 2014, other than Anglo American Platinum and Sibanye Gold, all of the top 10 were at similar or lower levels than last year with Kumba Iron Ore losing R63 billion.

The composition of the top 10 remained consistent, except for Harmony Gold, which was replaced by Sibanye Gold. Anglo American Platinum regained the top spot in terms of market capitalisation from Kumba Iron Ore. AngloGold Ashanti overtook Impala Platinum to take third place.

Figure 2: Market capitalisation of the top-10 mining companies (R 'billions)



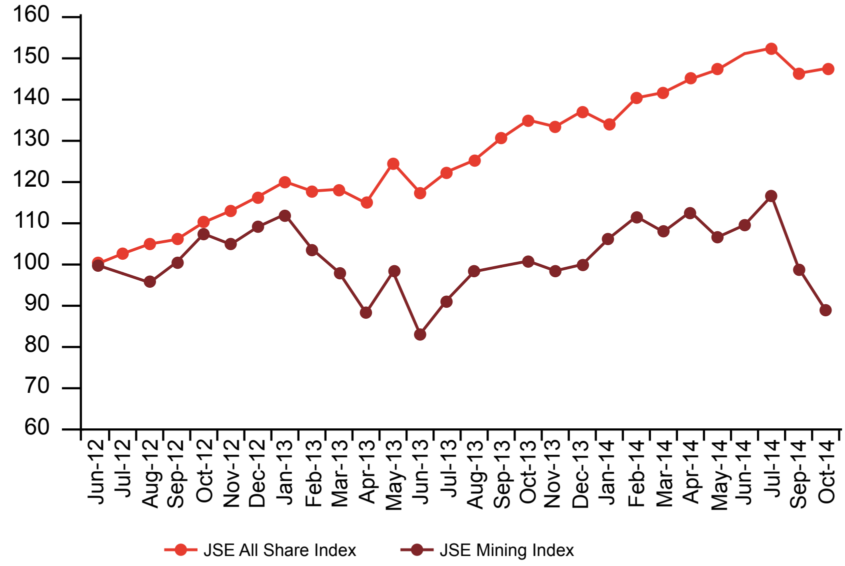
Source: Business Day

Market capitalisation of the 37 companies decreased after 30 June 2014 and as at 30 September 2014, had declined by 19% to R545 billion.

The scale of the challenges facing the industry is reflected in the relative decline in the JSE Mining Index in comparison to the JSE All Share Index over the last two years.

Despite the JSE All Share Index reaching record levels and the exchange posting steady increases in overall market capitalisation since 2010, the market capitalisation of the mining sector has substantially lagged this performance.

Figure 3: Market capitalisation: JSE Mining Index vs JSE All Share Index

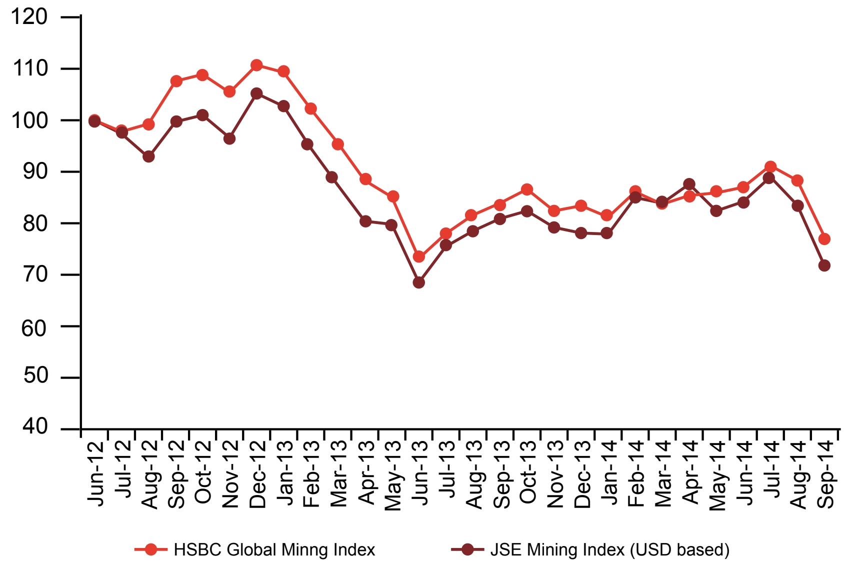


June 2012 = 100
Source: I-Net Bridge

The weak rand somewhat shielded the Mining Index, but could not fully compensate for the new decade lows in commodity prices. Although the challenging local mining environment, particularly relating to labour, played a role in the overall decrease in market capitalisation, the global economic environment was also a significant contributor.

The impact of the global economic environment on the mining industry is apparent when one compares the movements of the HSBC Global Mining Index to the JSE Mining Index in US-dollar terms. There is an almost perfect correlation between these indices, with variances almost exclusively explained by price movements in the different baskets of commodities.

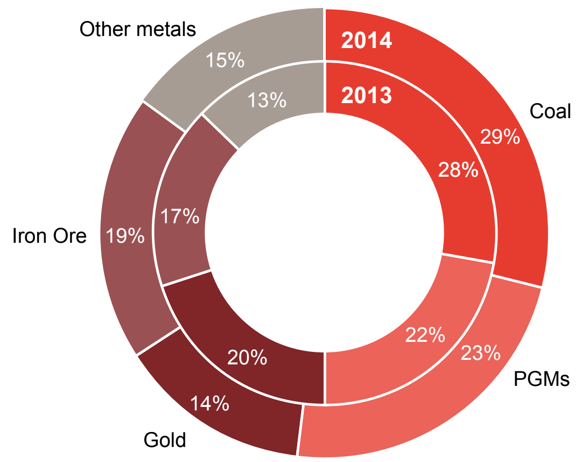
Figure 4: JSE Mining Index vs HSBC Global Mining Index



June 2012 = 100
Source: I-Net Bridge

Contribution by commodity

Figure 5: Percentage of mining revenue per commodity, 2013 vs 2014



Source: Stats SA

Despite a slight reduction in production, coal maintained its strong position as the leading South African mining commodity revenue generator.

The increase in the rand price of platinum was offset by lower sales volumes resulting in revenue only marginally up on the previous year.

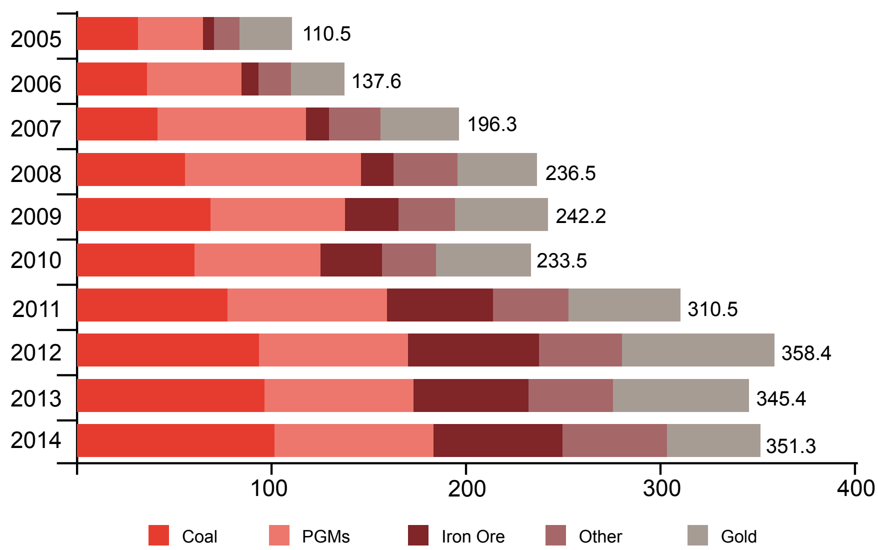
Although gold showed a welcome increase in annual production, lower production in the second half of the year more than offset the increase in the rand price in that period.

The increase in iron ore production, after lower production in 2013 aided iron ore revenues.

Figure 6 depicts the relative breakdown of revenues per commodity for the 12 months to June. The long-term increase trend was mainly rand-price driven and was partially offset by lower production, except for the increase in iron ore production.

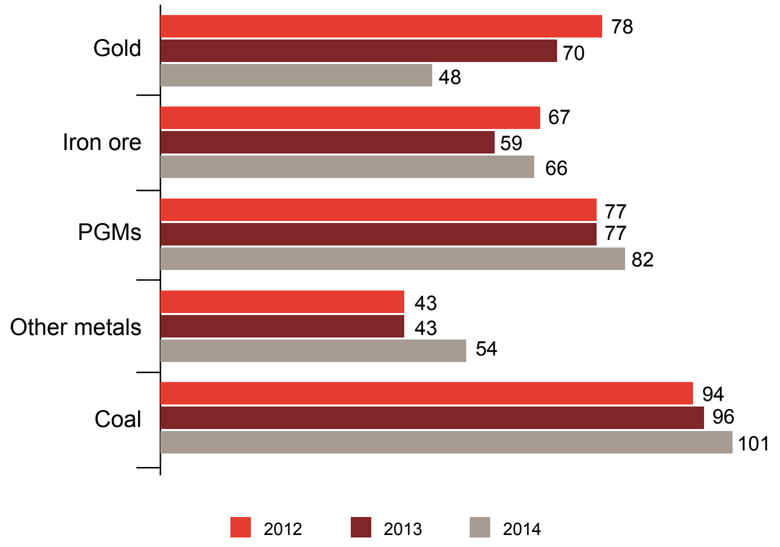
In the last year, the increase in production off the low 2013 base for all commodities except the strike-affected platinum sector – coupled with the weak rand, offset lower US-dollar prices to reflect a marginal increase in revenue.

Figure 6: Annual mining revenue per commodity (R 'billions)



Source: Stats SA, PwC analysis

Figure 7: Annual revenue per commodity (R 'billions)



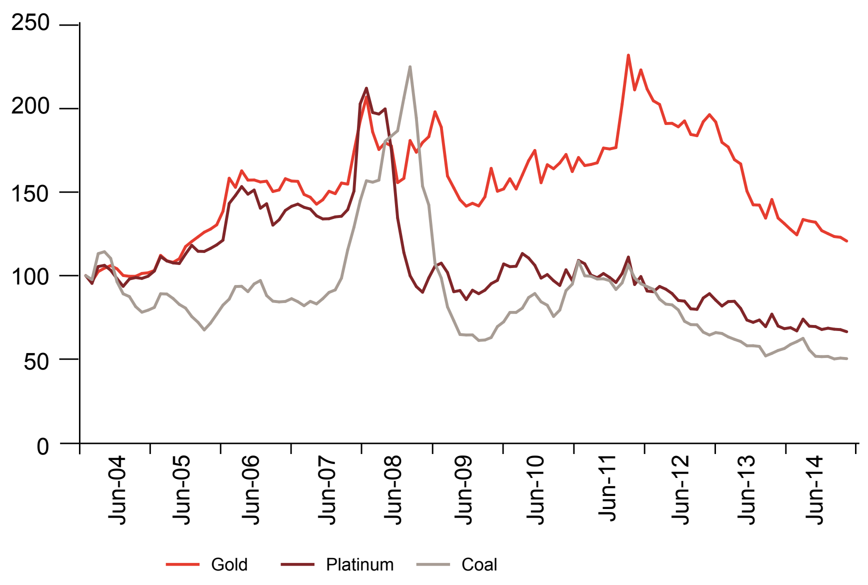
Source: Stats SA, PwC analysis

A slump in prices

We calculated real-rand prices for commodities by applying mining unit cost inflation to rand commodity prices. Of the three main revenue-generating commodities in South Africa, gold is the only commodity to have gained in real rand terms over the last 10 years. Many would argue that that is merely a result of artificially low gold prices in the first five years of the century.

The price of coal, which was at a high in 2004, has, despite significant volatility above 2004 price levels, decreased to almost half its 2004 level. Platinum in real terms continued its declining trend after the highs of 2008.

Figure 8: Indexed real-rand prices per commodity



June 2004 = 100
Source: World Bank, PwC analysis

The financial challenge faced by mining companies is apparent in the decreases in real-rand prices. Gold has dropped by nearly 50% since it achieved a 10-year high 2011. Similarly, platinum has proceeded to fall to its lowest real price in the last decade with a 68% decline on its highest price in 2008 and a 40% decrease since its 2011 highs. Coal has dropped by 52% from its 2011 high.

Real prices are lower as a result of the significant cost pressures, subdued global demand, which is only partially offset by the weaker rand. Not factored into these real prices, and often overlooked by investors, is the increased cost of capital expenditure required to maintain production.

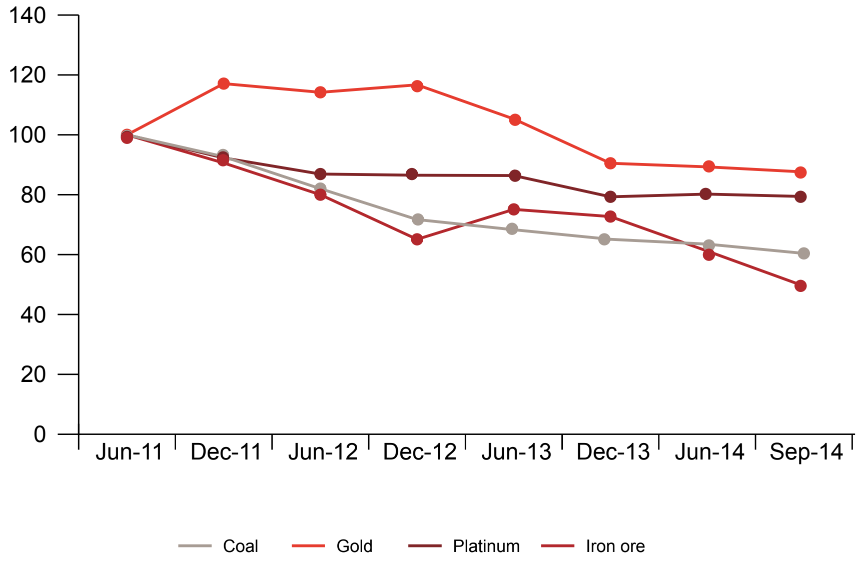
Although there are still demand-side pressures on prices, these low price levels are not sustainable. This is especially true for platinum where South Africa supplies more than 70% of global primary production.

Mining companies have an ever-diminishing capacity to continue absorbing operational cash outflows in unprofitable operations. A decline in local production as a result of closure of marginal mines, lack of new and sustaining investment and more expensive deeper mines will add significant supply-side upward pressure on prices.

Judging by the significant growth in platinum-backed exchange-traded funds (ETFs), this view seems to be shared by investors. The limited impact that the protracted strike in the Rustenburg platinum belt had on spot prices was an indication of the large value of unknown quantities of inventory held by consumers, which offset excess demand requirements and could assist in reducing volatility when demand-side growth resumes.

Even for gold and coal, where South Africa contributes a smaller portion of global supply, it is likely that supply-side cost pressures that are not unique to South Africa may also ensure a recovery in prices.

Figure 9: Indexed US-dollar prices per commodity



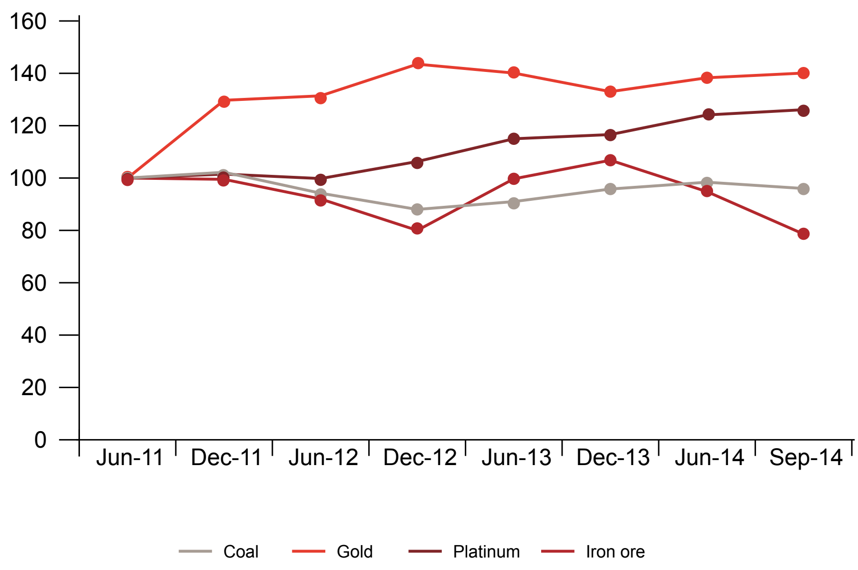
July 2011 = 100
Source: World Bank, PwC analysis

While the 2009-2011 period was characterised by a recovery in overall commodity prices from the lows of the 2008 financial crisis, 2012 saw a reverse in this recovery with gold being the only commodity to gain value.

In 2013, gold gave away all its gains of the last three years. A weakening rand over the period somewhat shielded the South African mining industry from this decline with rand prices remaining relatively flat and actually increasing in 2014.

Unfortunately, flat prices will not support the industry's significantly increased cost base. The weaker rand is also likely to add to inflationary cost pressure, which means that any respite will only be temporary.

Figure 10: Indexed ZAR price per commodity (July 2011 =100)



July 2011 = 100
Source: World Bank, PwC analysis

Platinum price: a basket case?

Although the platinum price already reflects the pressure the platinum industry is experiencing, the reality is that the situation is actually worse than it appears.

Platinum mining companies generally generate revenue from five platinum group metals (PGMs): platinum, palladium, rhodium, ruthenium and iridium. In addition, revenue is also generated from products such as gold, nickel, copper, cobalt and chrome.

The basket price reflecting total revenue from these metals per platinum ounce is the true indication of a platinum company's ability to generate revenue. This price is not only dependent on the individual prices of each commodity, but also on the volume of commodity content extracted.

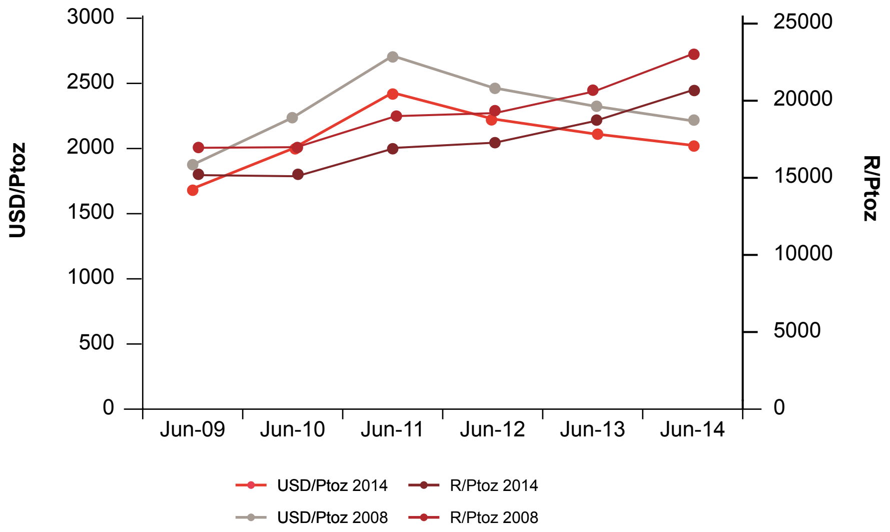
In South Africa, the Merensky Reef, UG2 Reef and Plat Reef are mined. In the current price environment, Merensky has the most profitable basket price. Unfortunately, most platinum companies have mined out most of their shallow Merensky and are now producing from the less-profitable UG2 or deeper Merensky. The result is a decrease in revenue for the same tonnes mined.

In Figure 11, we calculated an indicative basket price for platinum, palladium, rhodium and nickel, which make up more than 92% of PGM producers' revenues. This basket price does not include revenue generated from iridium, ruthenium, gold, copper, cobalt, chrome and other by-products.

The calculation is based on the aggregated production of the four largest PGM producers included in the analysis for the 12 months to June 2014

To demonstrate the negative impact of the change in reef mix, we also calculated the basket price using the production for these entities for the 12 months ending June 2008.

Figure 11: Indicative platinum basket price for the four main revenue-generating PGMs



Source: PwC analysis

The annual effective price growth rate in rand terms for these six years was only 3.7%. Considering the decrease in total production and the significant increase in costs, make the challenges faced by the platinum industry all the more apparent.

Production

Iron ore is still the only commodity with significant production gains over the last 10 years. With new mines ramped up, production is likely to remain at these levels subject to sufficient demand.

Gold production marginally increased for the first time in a number of years. The increase is as a result of less industrial action in 2014 compared to the significant production losses incurred in the previous year.

The long-term decline in gold production is indicative of the ever-increasing depths of existing mines, technical difficulties experienced by start-up operations and a continually growing cost base. The recent decrease in the gold price is likely to put further pressure on production as marginal mines are mothballed.

A focus on modernising mines by companies like AngloGold Ashanti and a successful back-to-basics approach by companies like Sibanye Gold could potentially address the long-term decline in the sector.

PGM production has been severely impacted by industrial action in the last two years and by mine closures in the low-price environment.

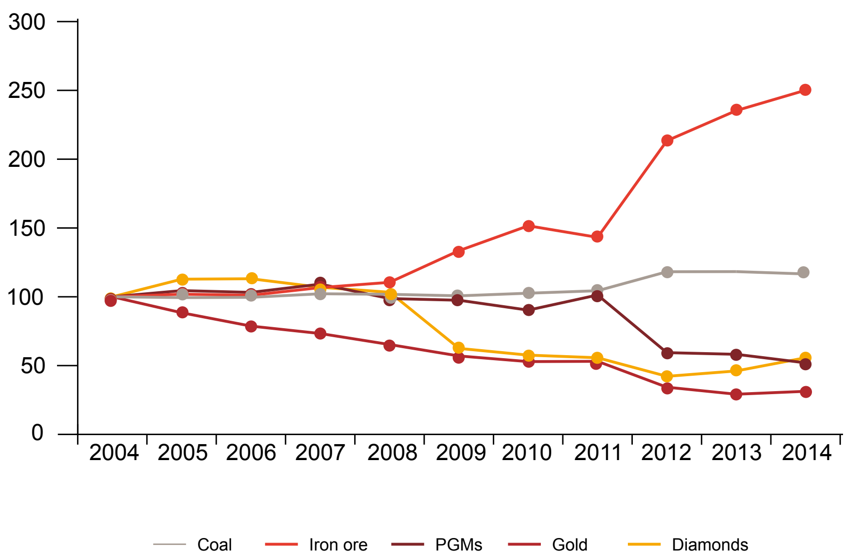
The protracted strike in the Rustenburg platinum belt in the first half of 2014 had a severe impact on production in the six months to June. This impact will be felt into the next six months as processing stock levels are rebuilt and affected mines are ramped up. Although there were encouraging reports from the affected platinum producers on how quickly they were operating back at pre-strike levels, one should bear in mind that these levels were already low post the Marikana strike in 2012.

However, supply and demand fundamentals should improve the price environment and result in increased production in the long term. The lack of and deferral of investment in platinum mines and the long lead time in increasing production would probably mitigate any significant medium-term increases to production levels in excess of pre-2012 levels.

Coal had a solid performance over the last 10 years with marginal increases in production in the last couple of years. The current low coal prices are likely to hamper any potential growth in short- to medium-term supply.

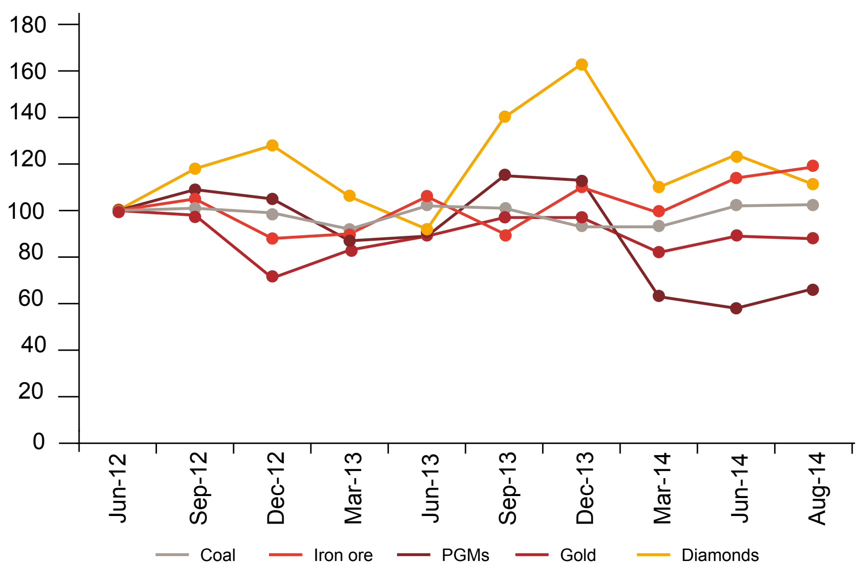
Diamonds, which were the most severely impacted by the global economic crisis and pressure on disposable income, continued to comeback this year. This improvement is likely to continue based on the new capacity created.

Figure 12: Indexed annual production per commodity



2004 = 100
Source: Stats SA

Figure 13: Indexed recent quarterly production per commodity



June 2012 = 100
Source: Stats SA

Recent production statistics to the end of August 2014 show a promising increase in production for all commodities except diamonds. In the absence of significant industrial action, one would expect this trend to continue into 2015. The challenge for the industry, especially PGM producers, will be to rebuild trust between employers and employees to improve productivity and output.

3. Integrating risk into business strategy

Risks facing the mining industry

When an industry is faced with challenges to the scale of those experienced by the mining industry, the need to effectively mitigate risks increases significantly. When one compares the risks facing the mining industry from the prior to the current year, overall they have not changed. What has changed is the priority ratings allocated to the different risk exposures.

In the prior year the highest ranking risks included: health & safety, employee labour relations, social licence to operate and securing funding.

In the current year, most companies' top exposures include: labour relations, sustainable business plans or budgets, volatility of metal prices and exchange rates, infrastructure access and capacity and regulatory, political and legal environment.

The table below indicate the top risks disclosed by mining companies, but are by no means meant to present a comprehensive list of risks faced by the industry.

Risks disclosed by mining companies

Risk description	Movement from prior year	Mitigation strategies
Labour relations		
The industry has seen a rise in labour unrest and violent strike action for increased wages and improved employee conditions. The events at Marikana in 2012 and the 2014 extended platinum strikes have highlighted the importance of sound labour relations. Ongoing business disruptions and work stoppages lead to significant losses.	↑	Formalising relations with trade unions. Increasing focus on direct communication with employees. Engaging with the Chamber of Mines, Government and labour representatives to find sustainable solutions to industrial relations challenges in the country.
Achievable business plans or budgets		
In recent times mining companies have been struggling to meet business plans for operations and capital projects.	↑	Implementing robust operational plans and production monitoring. Focusing on geological and mining conditions that are an issue. Implementing initiatives relating to mining quality, training, visible and felt leadership
Volatile commodity prices and foreign exchange fluctuations		
The market price for commodities continues to be significantly volatile due to global economic conditions that are beyond the control of South African companies. This could have a negative impact on revenue, cash flows, profitability and asset values. Transactions denominated in foreign currencies expose companies to exchange-rate fluctuations, which could result in significant accounting volatility.	↑	Implementing cost-reduction and efficiency measures. As sales prices are often outside management's control, cost performance has become a key measure of management performance. Understanding the future demand of minerals and the corresponding industry supply-side profile. Closely monitoring the rand/dollar exchange rate.
Reliance on third-party infrastructure		
Power shortages remain a key obstacle that could hinder growth in the mining sector in South Africa and elsewhere in Africa. At worst, power outages can impact production and employee safety and at best add significantly to the cost of operations. Bulk commodity exports are reliant on the road, rail and port infrastructure. Unavailability of water in some areas poses a risk.	↑	Improving efficiency of energy and water consumption with adoption of appropriate technologies. Implementing back-up power solutions in case of catastrophic power outages. Establishing public-private relationships to address transport issues. Linking water-intensity targets to performance targets

Employee safety and health

Failure to maintain high levels of safety may result in harm to employees and safety stoppages in terms of Section 54 of Mine Health and Safety Act, which will impact production and a company's licence to operate.

Exposure to noise and dust are significant occupational health risks, especially given the focus on silicosis claims in the industry.

HIV and TB continue to impact employees' health.

Health and safety are still reflected as the number one focus area, but has reduced in risk prominence due to improvements achieved and increases in other risk exposures.

Implementation of regular safety awareness campaigns and safety transformation programmes.

Enhancing reporting systems.

Performing medical surveillance in compliance with legislation.

Social licence to operate

Non-compliance with Social Labour Plan (SLP) targets as approved could negatively impact on community expectations and mining licences.

The increased focus on implementation in this area has resulted in better levels of compliance and communication, hence a reduction in compliance risk.

Driving existing SLP programmes to comply with or exceed the Mining Charter requirements.

Undertaking proactive socio-economic activities in communities in which companies operate.

Delivering on SLP projects on time and in full.

Aligning contractors with SLP requirements.

Regulatory, political and legal environment

Regulatory uncertainty is still hailed by a large number of companies and investors as a significant concern for the industry.

The uncertainty of the Mining Charter assessment set for 2015 and what might supersede it, as well as the still-to-be-signed amended Mineral and Petroleum Resource Development Act (MPRDA) are regularly commented on.

Added to this is the beneficiation debate with potential export taxes on raw materials.

More transparent communication with Government in an effort to create a better understanding of the sector's challenges.

Improve interaction and communication to establish valuable stakeholder relationships.

High input costs

Input costs have been increasing at a rate higher than inflation. The 2014 platinum strike has seen employee wage increases ranging between 8% and 18.1% depending on employee level. In October 2014 The National Energy Regulator (NERSA) granted Eskom a 12.69% increase in electricity prices for next year.		Reducing costs aggressively and organisational restructuring for greater efficiencies. Focusing on core businesses. Increasing productivity.

Human resource skill and capacity

Global competition for expertise and skills in technical fields, as well as the distance of operations from major urban areas, puts pressure on attracting and retaining skills.		Developing appropriate remuneration policies Developing policies and practices to retain key talent

Other risks

In addition to the high-rated risks identified above, we anticipate specific focus on the following aspects in the coming year:

- Mining Charter compliance;
- Aligning expectations;
- Beneficiation of mining output;
- Losing out to other regions for foreign direct investment;
- Water scarcity; and
- Productivity challenge at mines.

Mining Charter compliance

The Mineral and Petroleum Resources Development Act (MPRDA), approved by the Cabinet in 2002, opened the door for meaningful participation of black people in the exploration of mineral resources. The MPRDA enshrines equal access to mineral resources, irrespective of gender or race. In terms of the Act, new-order rights may be registered, transferred and traded, while existing operators are guaranteed security of tenure. Mining rights are valid for 30 years, while prospecting rights are valid for up to five years and renewable for another three.

The introduction of a new Mining Charter in 2010 was aimed at transforming the mining industry in order to redress historical imbalances resulting from apartheid. This year sees the deadline looming for compliance with the Charter. Compliance with the Charter and its precursors has been and remains a concern for mining companies in South Africa. The outcome of the participation process for the MPRDA assumes greater importance as more and more companies were put through charter audits by the Department of Mineral Resources (DMR).

Mining Charter Scorecard

This table summarises the results disclosed by most companies included in our analysis:

Scorecard for the Broad-Based Socio-Economic Empowerment Charter for the South African Mining Industry

	Element	Description	Measure	Compliance target by 2014	Weighting	Performance
1	Reporting	Has the company reported the level of compliance with the Charter for the Calendar year	Documentary proof of receipt from the department	Annually	Y/N	Annually
2	Ownership	Minimum target for effective HDSA ownership	Meaningful economic participation	26%	Y/N	Ranges from 26% to 56%
			Full shareholder rights	26%	Y/N	Ranges from 28% to 56%
3	Housing and living conditions	Conversion and upgrading of hostels to attain the occupancy rate of one person per room.	Percentage reduction of occupancy rate towards 2014 target.	Occupancy rate of one person per room - 100%	Y/N	Ranges from 19% to 100%. This was not applicable for some mining companies as they do not have hostel accommodation.
		Conversion and upgrading of hostels into family units	Percentage conversion of hostels into family units	Family units established - 100%	Y/N	Ranges from 69% to 100%
4	Procurement & Enterprise Development	Procurement spent from BEE entity	Capital goods	40%	5%	Ranges from 40% to 72%
			Services	70%	5%	Ranges from 46% to 74.5%
			Consumable goods	50%	2%	Ranges from 46% to 113.89%
		Multinational suppliers contribution to the social fund	Annual spend on procurement from multinational suppliers	0.5% of procurement value	3%	0.50%
5	Employment Equity	Diversification of the workplace to reflect the country's demographics to attain competitiveness.	Top Management (Board)	40%	3%	Ranges from 40% to 67%
			Senior Management (Exco)	40%	4%	Ranges from 25% to 67%
			Middle Management	40%	3%	Ranges from 26% to 65%
			Junior Management	40%	1%	Ranges from 40% to 85%
			Core Skills	40%	5%	Ranges from 40% to 100%

6	Human Resource Development	Development of requisite skills, incl. support for South African based research and development initiatives intended to develop solutions in exploration, mining, processing, technology efficiency (energy and water use in mining), beneficiation as well as environmental conservation	HRD expenditure as percentage of total annual payroll (excl. mandatory skills development levy)	5%	25%	Ranges from 4% to 6%
7	Mine community development	Conduct ethnographic community consultative and collaborative processes to delineate community needs analysis	Implement approved community projects	Up-to-date project implementation	15%	Ongoing community development projects
8	Sustainable development & growth	Improvement of the industry's environmental management	Implementation of approved EMPs.	100%	12%	Progress noted against approved EMPs.
		Improvement of the industry's mine health and safety performance	Implementation of the tripartite action plan on health and safety	100%	12%	Ongoing projects to achieve health and safety targets.
		Utilisation of South African based research facilities for analysis of samples across the mining value	Percentage of samples in South African facilities	100%	5%	Not disclosed significantly to comment
9	Beneficiation	Contribution of a mining company towards beneficiation (this measure is effective from 2012)	Additional production volume contributory to local value addition beyond the base-line	Section 26 of the MPRDA (percentage above baseline)	0	Not disclosed significantly to comment

Source: PwC analysis

As the table shows, most companies are on track to meet most Mining Charter requirements. However, Housing & Living Conditions, Services Procurement and Employment Equity (Senior Management and Middle Management) still seem to be a challenge for some companies.

The Mining Charter calls for the conversion and upgrading of hostels to attain the occupancy rate of one person per room. In a number of instances, housing allowances replaced hostel accommodation to allow miners to obtain their own accommodation. Unfortunately, it is apparent that housing allowances are often used for other purposes and that miners move into informal housing. The housing question is likely to play a key role in future labour negotiations.

The Mining Charter calls for 26% full shareholder rights as the minimum target for effective Historically Disadvantaged South Africans (HDSA) ownership. Companies have disclosed that this target has been reached, and in most cases, exceeded.

The companies included in the analysis have done well in meeting the targets of 40% HDSA representation for Employment Equity, specifically in Top Management and Senior Management positions compared to the rest of the country and the industry. The Commission for Employment Equity Report published in April 2014 indicates that white people still occupied 57% of senior management positions across all sectors.

According to the commission, HSDSAs represents 28.3% of top management positions and 26.8% of senior management positions in the mining industry. Companies disclosed their representation at top and senior management as between 40% and 67% and 25% and 67% respectively, which is well above the Commission's disclosed levels.

Despite the progress made to date, it goes without saying though that there is still significant room for improvement over the long run.

Where to from here as the 2014 deadline has passed?

The measurement deadline is 31 December 2014 with reporting due in March 2015. Now that the deadline is imminent, the big question remains – where to from here? A breach of the Charter alone presumably cannot result in the cancellation of a mining right. Clause 2.9 of the Charter makes the following provision:

> *Every mining company must report its level of compliance with the Mining Charter annually, provided for by Section 28(2)(c) of the Mineral and Petroleum Resources Development Act.*

It should be noted, however, that there is no clause in the Charter that refers to the scorecard attached to the Charter. So what are the real ramifications on non-compliance with the scorecard? Is the Mining Charter Policy or Law? This is one of the regulatory uncertainties along with the unsigned MPRDA Amendment Bill raised by investors as a deterrent to investment since the way forward is not clear.

Mineral Resources Minister Ngoako Ramatlhodi has been reported as saying that not enough has been done by mining companies. Ramatlhodi has further reiterated his view that the MPRDA Amendment Bill should be reconsidered. Changes to the Bill could go beyond the oil & gas sector and include changes to the pricing of strategic minerals such as coal.

In a recent interview with Business Day, the Minister said that he

would like to see a higher level of black equity ownership in mining companies. Asked his view of the 26% ownership requirement stipulated by the Charter, he said ‘I think it should be increased’. Until now he has not said how much it should be increased to.

The ‘once empowered, always empowered’ principle

There are growing discussions as mining companies do not see eye to eye with the DMR over the ‘once empowered, always empowered’ principle. The mining sector argues it has put empowerment transactions in place to meet the requirements of the Charter and that these historical transactions should count towards their empowerment credits even if those partners no longer hold their shares.

Questions have arisen as to whether companies whose Black Economic Empowerment (BEE) partners have chosen to exit will lose their empowerment credits. The DMR seems to imply that mining companies should repeatedly enter into new BEE transactions every time an existing BEE partner exits, while mining companies argue that deals from the past should count towards empowerment credits.

The fact that there is nothing formal from the DMR stating that companies should constantly ensure that they have at least 26% HDSA ownership is one of many concerns, as it raises uncertainty as to whether Mining Charter requirements are being met, despite years of investment in BEE by mining companies. However, indications are that the DMR will apply a strict measurement of ownership on the measurement date.

Alignment of stakeholder interests

In the previous edition of this publication we disclosed the risk of stakeholders pursuing maximisation of short-term gratification at the expense of longer-term sustainability and value. This risk received a significant attention during the platinum strike with allegations made by various stakeholders as to the benefits derived by other stakeholders. The risk is manifested by:

- Demand for higher dividends instead of reinvestment;
- Government drive to maximise short-term tax revenue;
- Organised labour demands for excessive salary increases, unconnected to increased productivity or long-term viability;
- Unions competing for a larger share of the existing workforce instead of looking for solutions that secure existing jobs and grow the workforce;
- Management incentives that drive short-term profit targets at the expense of longer-term profits and sustainability; and
- Communities demanding short-term benefits instead of deriving the longer-term social advantages of improved infrastructure and education.

At the recent 2014 Joburg Indaba a number of participants from various stakeholder groups indicated that long-term sustainability is more important than short-term gains. We can only hope that the negative circumstance experienced by the mining industry force all stakeholders to reassess their positions and realise the need for long-term sustainability.

Beneficiation of mining output

The public debate on beneficiation of mining output is a relevant and valid one. But rather the stance on the matter is becoming clearer or rather louder. The South African Development Community countries (South Africa, Botswana, Lesotho, Namibia, Swaziland, Angola and Mozambique) resisted the inclusion of prohibition on export taxes in the economic partnership agreement between them and the EU signed in July 2014.

The ruling ANC's transformation committee has informed the media that the party has decided to introduce measures, including export taxes, in the next five years to encourage companies to use raw local materials for domestic manufacturing and local beneficiation. The political landscape in South Africa is changing with new parties coming in and pushing for more radical policies. The ruling party may feel under pressure to implement transformation policies to maintain supporters. Mining in South Africa is not just an economic matter but also a political one.

The legislation for beneficiation is already in place. The Mineral and Petroleum Resources Development Act of 2002, Act 26 of 2002, includes provisions that will ensure that the Minister of Mineral Resources promotes the beneficiation of minerals in the Republic. The Mining Charter of 2004 specifically stipulates that mining companies will be able to offset the value of the level of beneficiation achieved by the company against its HDSA ownership commitments.

Two ways of beneficiation have been discussed mainly: ring fencing a percentage of production for local use or a price advantage for the local market.

What this may mean for mining companies:

- Additional government intervention in business;
- Pressure to deliver at lower cost as prices will be lower than market; and
- Investors may be persuaded to look at other companies whose profitability is not dictated by the Government.

The priority accorded to beneficiation on the mining industry's to-do list differs among the different stakeholders.

Losing out to other regions for foreign direct investment

South Africa has an unparalleled resource base and should be very attractive to foreign direct investment. However, the capital required to develop its mineral resources is significant.

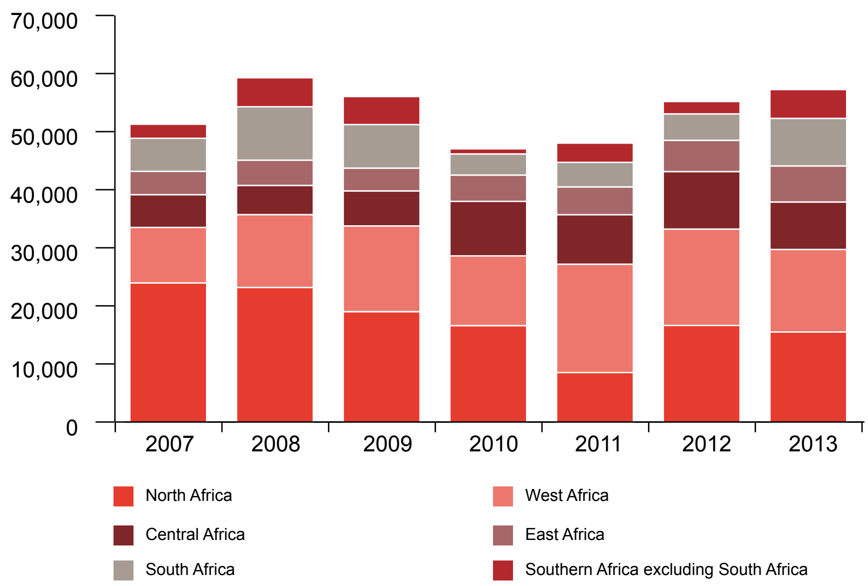
Various international surveys indicated global perceptions of the negative investment environment.

In its Global Competitiveness Report 2014-2015, the World Economic Forum rated South Africa 56th of 144 countries (prior year 53 of 148) in terms of competitiveness. The main concern in terms of competitiveness related to the shortcomings in the labour market. Industrial action in the mining sector over the last two years underlines these concerns.

The Fraser Institute's annual Survey of Mining Companies 2013/2014 includes national policies and mineral resources in its assessment of the perceptions of the mining companies surveyed. Survey findings are impacted by individual experiences and sentiments which have a powerful influence on investment decisions. According to the survey, South Africa ranked 64th out of 112 jurisdictions for policy potential (prior year 64 of 96) and 53rd for investment attractiveness which was a welcome improvement from 67th in the prior year. Although it's pleasing to see an improvement in this survey, there is clearly still significant scope for improvement.

It is pleasing to note that declining trend in foreign direct investment was halted in 2013 for South Africa and Southern Africa. Although these investments were mainly energy and infrastructure related they should assist in providing long-term opportunities and improvements for the mining industry. It will be interesting to see what impact the platinum strike will have on these investments in next year.

Figure 14 Foreign direct investment in Africa (USD millions)



Source: World Investment Report 2014

Water scarcity

Over the past decade, since the promulgation of the National Water Act (NWA) in 1998, an improvement in understanding the complexities of water resource management has taken place. The National Water Resources Strategy 2 (NWRS 2) states:

> *Although the regulatory framework and the institutional arrangements have changed since the advent of democracy, one aspect remains constant: Water scarcity – whether quantitative, qualitative or both – which originates as much from inefficient use and poor management as from real physical limits.*[3]

This increasingly poses a significant threat to quality of life in South Africa.

South Africa has low levels of rainfall relative to the world average with high variability as well as high levels of evaporation due to the warm climate. There are also increasing challenges from water pollution. All of these factors pose constraints on the quantity of surface water available for use. In many parts of the country, we are fast approaching the point at which all of our easily accessible surface water resources will be fully utilised.[3]

Mining companies increasingly understand the risk associated with ineffective water resource management practices, which is not only limited to criminal liability, but which also has increasing financial consequences pertaining to remediation obligations for existing contamination of water resources and consequences for mine closure.

Groundwater is increasingly regulated as an important strategic water resource and is included under the definition of a water resource in the NWA. Groundwater resources had not previously been acknowledged and developed to the same level as surface water resources. The NWRS 2 notes that, as at 2012:

> *South Africa has had 16 consecutive years of above average rainfall in the majority of summer rainfall areas and in these areas the last major drought was more than two decades ago. This trend is unlikely to continue.*

[3] National Water Resource Strategy 2: Annexure B: Understanding Water Resources

Interpreting the NWRS 2, there will be increasing pressure on mining operations to ensure adequate protection of groundwater resources and where the need arises, to remediate groundwater pollution. It is stated in the NWRS 2 that:

The Department of Water and Sanitation (DWS) will strengthen its compliance monitoring and enforcement capacity to take strong action against illegal water use in accordance with the enforcement protocol. The DWSs will also develop and ensure compliance with norms and standards for various water resource development options and strategies, such as groundwater management, rainwater harvesting, desalination, and water re-use, to provide guidance to the sector.

There is a direct relationship between the effectiveness of groundwater pollution prevention operational controls and the pollution impact on groundwater. This pollution impact on groundwater is measurable for decades and sometimes centuries after the impact occurred due to the relative slow movement of groundwater. Furthermore, risks such as groundwater decanting from mine works can pose a significant threat to surface water receptors such as streams and wetlands. The abstraction of groundwater can also negatively influence the water rights of other water users should the radius-of-influence of the cone-of-depression caused by groundwater abstraction intersect with water supply boreholes of third parties.

It is in this context that mining companies should realise the potential consequences of failing to implement reasonable measures to ensure appropriate groundwater impact management (pollution and abstraction). It is imperative that mining companies understand and quantify their groundwater impact (in terms of abstraction, decant and pollution) to the extent that informed risk-based decision-making can take place.

Groundwater impact management and risk interpretation is complex and dependent on a number of factors (which do not always remain consistent). It is in the interests of mining companies to develop groundwater governance frameworks for their operations to ensure an appropriate proactive approach towards groundwater impact management.

The objective of a groundwater governance framework is to ensure responsible and effective groundwater resource management (within the context of relevant legal and defined other requirements).

This should include the significant groundwater impacts from the mining operation's products, services and activities. The groundwater governance framework should comprise information on policy, translating it into risk-based objectives and strategies that provide structure and guidance on effective groundwater impact management at both corporate and operational level.

The NWRS is the legal instrument for implementing or operationalising the National Water Act (Act 36 of 1998) and it is thus binding on all authorities and institutions implementing the Act. It is the primary mechanism to manage water across all sectors towards achieving national government's development objectives. This is the second edition of the NWRS, as required under the National Water Act (Act 36 of 1998) (NWA). The first edition (NWRS1) was published in 2004, and was the blueprint for water resources management in the country. The NWA requires that the Strategy is reviewed every five years.

National Water Resource Strategy 2: Section 1.1 Purpose and Scope

Productivity challenge at mines

The dreaded 'P' word, Productivity, is sometimes neglected and often avoided when mining labour trends are considered. Looking at the ranking of the South African workforce in 2012, most mining companies are negative in relation to the calculation of operating cash flow per worker (after the contribution of capital in the production process is accounted for).

In to a recent Productivity SA report, the CEO of the National Employers Association of South Africa indicated that wage increases without accompanying productivity increases are just not sustainable and that in the long run, this could lead to more job losses. This is also echoed by the Adcorp Group, which has observed that labour marginal productivity is at the lowest mark in more than 40 years.

Best practice and trends around productivity improvement

The world of work has changed dramatically in the past few years and recent global economic trends and events have had on major impact on how the executives and employees of companies perceive their careers and the relationship between themselves and their employer. This is equally relevant in the mining industry where we see substantial changes being planned for some existing mines, while new mines are being designed and implemented to be less dependent on labour.

According to author and leadership development specialist Jack Zenger, writing in Forbes[4], the long-term interest in productivity improvement has led to two obvious and practical questions:

- What is it that leaders do to create a climate in which people go the extra mile and perform at remarkably high levels? and;
- What causes people to make extraordinary discretionary effort?

In relation to these questions Zenger's research identified several important elements:

- Redefine work. You often hear people say, 'I'm going to work', as if work was a destination. One way of obtaining higher performance from people is to move from viewing work as a place to instead viewing it as results that need to be accomplished, and for which someone is responsible. The Best Buy organisation has found that productivity increases by approximately 35% when you take this approach of holding people accountable for outcomes, not merely to be 'at work' for a certain number of hours.

In the mining sector, output is something that can be measured and monitored	Make the targets highly visible and clear. Nothing confuses people more and reduces productivity to a greater degree than murkiness about the objectives being sought. The simple process of reminding everyone of the target and asking team members to describe to each other their interpretation of the big goal is extremely powerful.
The visibility and management of targets for teams on shifts in the sector is an ideal way of increasing productivity and related rewards	Emphasise continuous improvement. Everyone in the organisation needs to know that the organisation aspires to continuously improve and to reach ever higher levels of performance. Adopt new technologies that enhance productivity.
Focus on new ways of work and allow the lower-level workers to become part of crafting solutions for improving the productivity – do that within teams	Convey infectious enthusiasm about projects. Emotions are highly contagious. A leader's upbeat enthusiasm for a project causes others to put in extra effort. If the leader's goal is to increase discretionary effort, then the organisation needs to feel enthusiasm emanating from their leaders.
Use the supervisors or team leaders to generate excitement amongst their teams and create a new wave of teams aiming for performing at a higher level	Treat colleagues at work with great respect. The leader who poses important questions to subordinates and who listens to the answers will obtain higher levels of productivity than one who doesn't. The leader who invariably seeks a subordinate's opinion before expressing his or her own is far more likely to have high productivity from that individual.
Create a new focus on the teams and give the team leaders the necessary development to improve themselves and eventually their teams	Express appreciation and provide recognition. These simple acts take small bits of time, yet pay huge dividends. Frequent expressions of sincere appreciation from a leader create a positive work environment and have been shown to have a direct link to greater productivity.
By doing this in a shift – or a team context, a new culture may develop that will assist with the general productivity improvement issue on the mines	Take an active role in the development of subordinates. Carving out time for ongoing coaching is highly correlated with the highest levels of employee productivity. The importance of practical support is very often ignored and business coaching initiative for supervisors/shift leaders can change the entire industry

[4] Zenger, Jack, 'The Productivity Improvement Steering Wheel: 7 Powerful steps leaders can take' Forbes, August 2012. http://www.forbes.com/sites/jackzenger/2012/11/08/the-productivity-improvement-steering-wheel-7-powerful-steps-every-leader-can-take-beginning-today/

Getting back to the basics

Organisation development and leadership training usually have two focus areas:

- Junior employees with potential; and
- Executive leadership or senior management programmes.

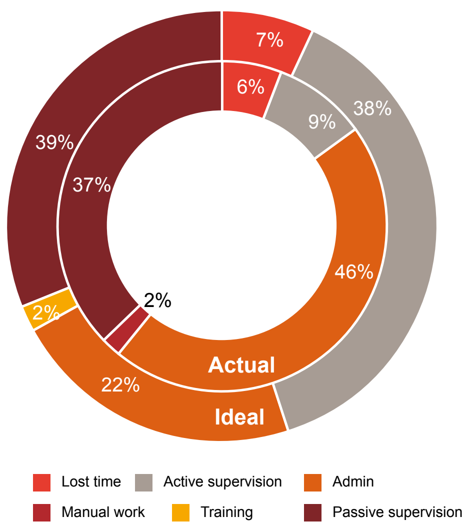
The neglected environment is always the middle management or supervisory level. In the mining context we are talking about the shift leaders or team supervisors. This level of management in the mines is sometimes overwhelmed and unprepared for what they are required to achieve. On a daily basis, they are under constant pressure to deal with:

- Managing the production cycle;
- Leading the teams;
- Representing the executive team on the floor;
- Daily administration;
- Occupational health and safety; and
- Act as compliance officers.

It is important to drive the basic behaviour and to deal with the individuals who are actually delivering the productivity numbers for the mines. The only way for them to perform is to be empowered and to be rewarded appropriately for real productivity improvement. Getting the balance between active supervision, passive supervision, administration, training, manual wok and lost time is something that most individuals cannot manage on their own. This can however be resolved with some individual focus and attention.

Through understanding a supervisor's natural style and preference, the leadership process can be enhanced and guided. The approach is a simple but effective intervention to assist the most neglected group of managers in the mining industry:

How the supervisor spends his day vs how he should spend his day



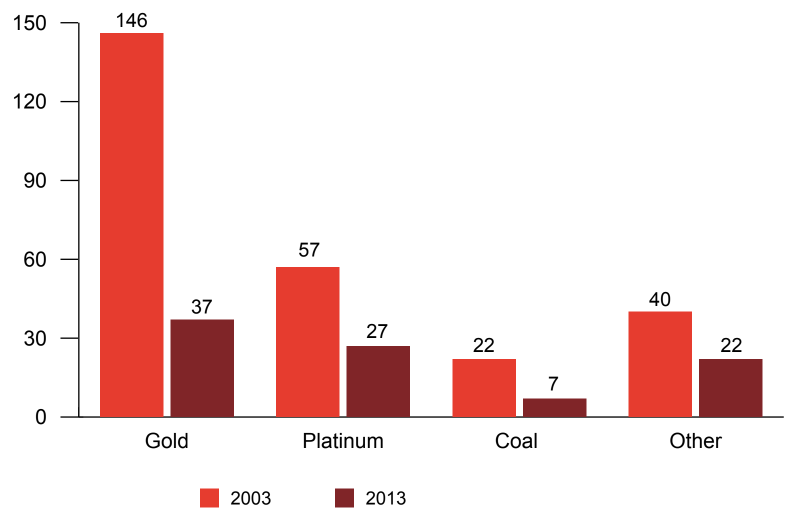
4. Safety

Mining companies continue to focus priority attention on creating a safe working environment for all their employees across all commodities.

Company CEOs consistently highlight this in company annual reports and do not shy away from the fact that additional funds are invested in mining operations to avoid loss of life, injuries and safety stoppages.

According to statistics made available by the Department of Mineral Resources, safety is improving. This becomes particularly clear when one compares current statistics to historic rates, which show a significant decrease in fatalities over the last 10 years.

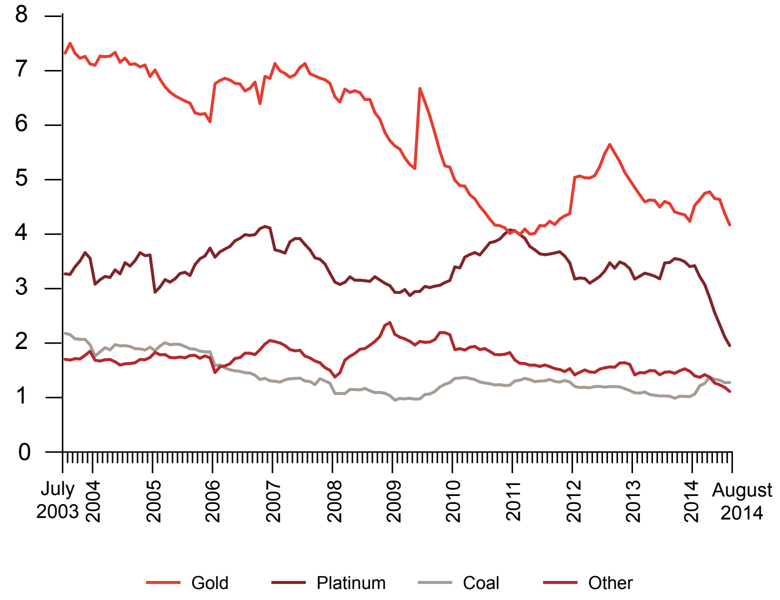
Figure 15: Mining fatalities, 2003 vs 2013



Source: Department of Mineral Resources

All commodities showed decreases in fatalities with gold miners having declined the most. The injuries and fatality rates per million man hours worked have also decreased steadily over the last 10 years

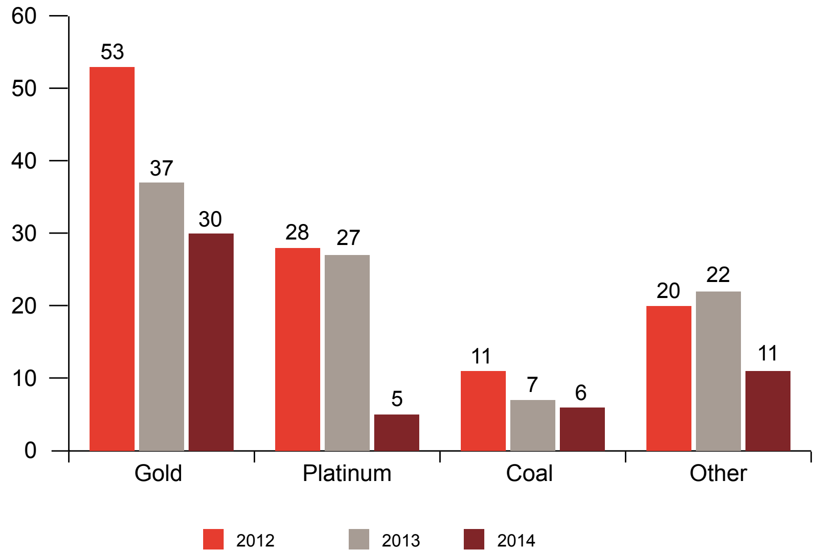
Figure 16: Injury rate per million man hours worked 2004-2014



Source: Department of Mineral Resources

All major commodities (gold, platinum, coal) have shown a decrease in fatalities, injuries and accidents between 2012 and 2014, with the trend continuing in 2014. The fatality rate per million hours worked has shown a steady decrease over the last decade.

Figure 17: Fatalities per commodity for the years ending 30 June

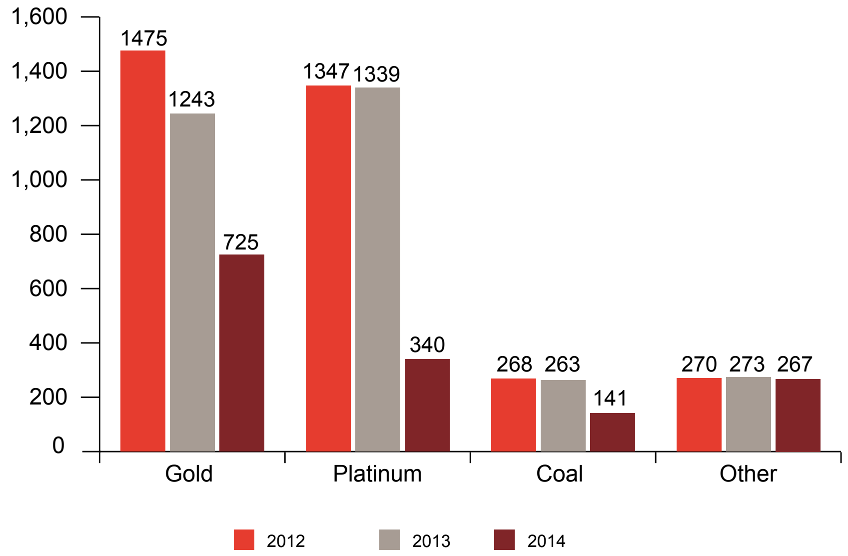


Source: Department of Mineral Resources

The absolute number of fatalities and injuries in the platinum sector decreased as a result of the strike action when fewer people were at work. There is always a risk that in times of industrial action safety records slip. This seems to be evident in the weakening in lost time injury frequency rates (LTIFR) for gold, coal and other commodities during the platinum strike months as the negative environment also impacted on workers not on strike.

There was a significant risk that when mining activity resumed, LTIFR would go up as a result of unsafe working conditions and the fact that employees hadn't worked for an extended period of time. However, it is pleasing to see that lost time injury frequency rates actually decreased in July and August 2014. A lot of credit must go to all parties involved for the significant investment made in retraining employees and ensuring that all work areas were declared safe before work recommenced.

Figure 18: Injuries per commodity for the years ending 31 August

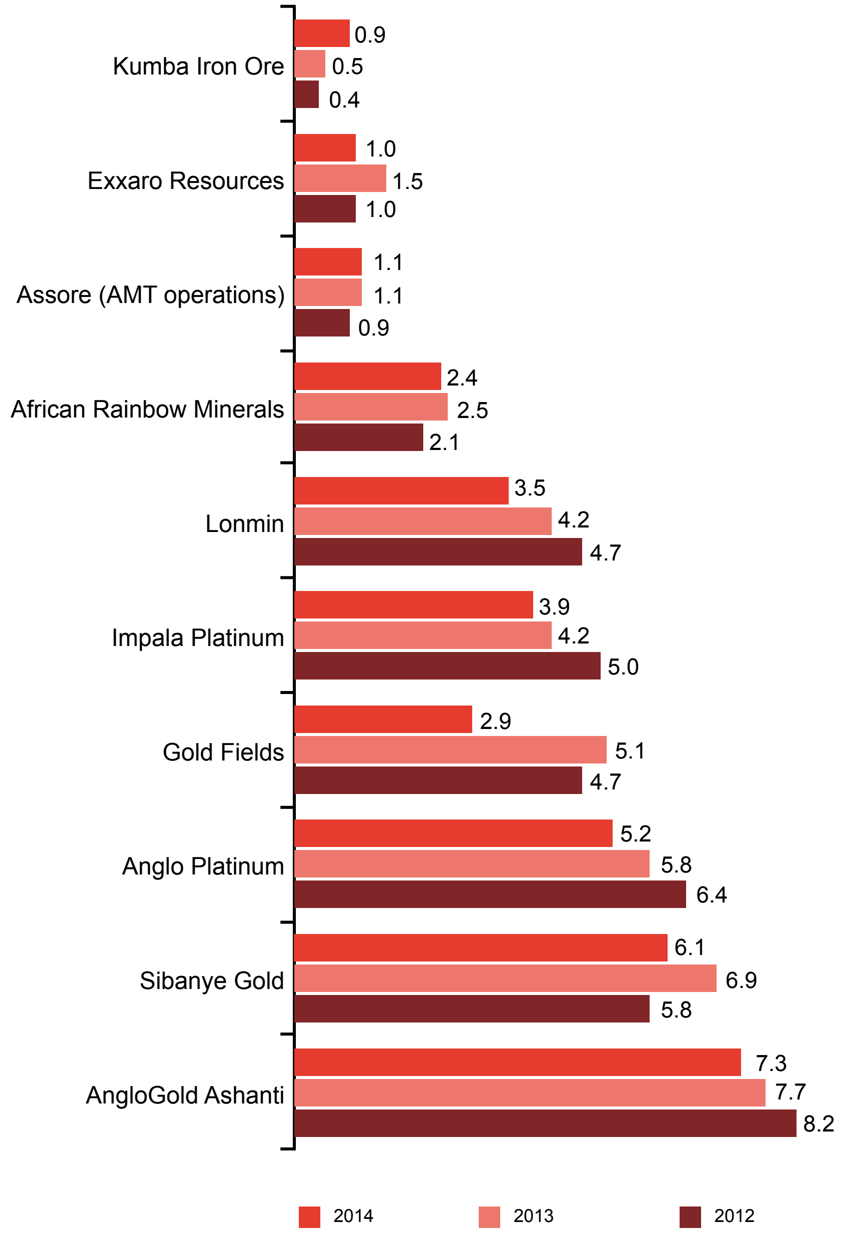


Source: Department of Mineral Resources

Companies realise that the cost of lost production due to self-imposed and Section 54 closures is real and are continuing to invest in safety.

The top-10 companies' individual safety performances are set out in Figure 19.

Figure 19: Top-10 companies' lost-time injury frequency per million man hours



Source: PwC analysis of company sustainability reporting

Of the top-10 companies that disclosed lost-time injury frequency rates, Kumba Iron Ore reflected the best safety record with regard to lost-time injuries. Exxaro Resources and Assore followed closely. It is pleasing to note that all entities, other than Kumba Iron Ore, reflected an improvement on the prior year.

5. Improving value to stakeholders

Despite challenges faced due to industrial action and safety stoppages as well as the continuing decline in commodity prices, the mining industry continues to add significant value to our country and its people. Stakeholders in the mining industry include employees and their families, unions representing them, the Government as regulators and custodians of tax income for the country, investors, suppliers and customers.

The monetary benefit received by each of these stakeholders is often summarised by companies in their value added statements.

It is a lot more difficult to quantify benefits resulting from costs that assist in uplifting communities or protecting the environment for future generations.

A third of the companies included in this analysis – representing approximately 77% of revenue for all companies analysed – provided readily-available value added statements.

Although we could not ensure consistency in disclosures in all cases, we made certain adjustments based on information shared in annual reports (e.g. employee taxes) to ensure a level of consistency.

The accompanying table shows how the value created, being the difference between income and direct purchases, was distributed to the various stakeholders.

Value distributed

	2014	2013	2012*	2011*	2010*
Funds reinvested	34%	41%	27%	32%	43%
Employees	38%	38%	27%	30%	36%
Shareholder dividends	11%	19%	20%	11%	12%
Direct taxes	9%	10%	10%	11%	9%
Employee taxes	7%	7%	6%	6%	6%
Mining royalties	4%	4%	3%	1%	1%
Borrowings	4%	3%	2%	3%	5%
Community investments	1%	1%	1%	N/A	N/A
Funds (utilised)/ retained	(8%)	(23%)	4%	6%	(12%)
Total value created	**100%**	**100%**	**100%**	**100%**	**100%**

Comparatives were taken from our 2013 publication to illustrate the cycle impact
Source: PwC analysis

Total value created for these entities increased by 11% from R129 billion to R 144 billion.

The majority of the analysed increase is attributable to Anglo American Platinum Limited (a 31 December issuer), which returned to profitability on the back of higher sales volumes and due to the impact of the weakening rand exchange rate.

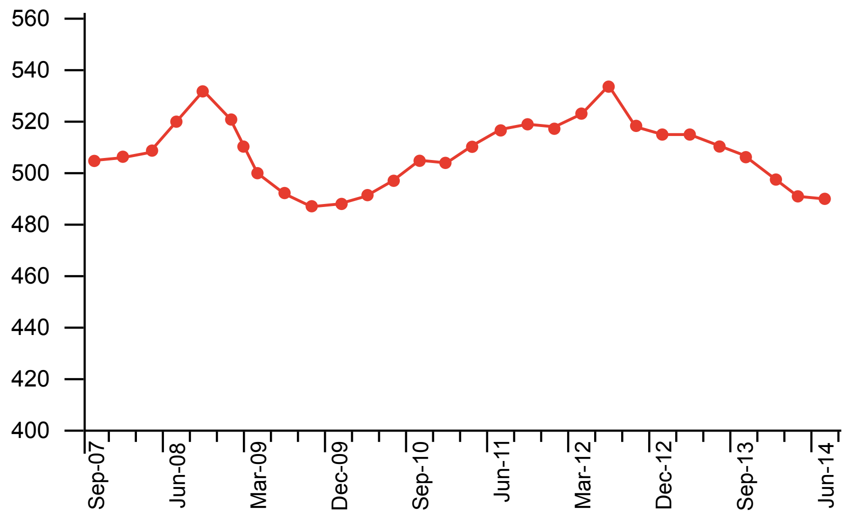
Results were skewed by another good year for Kumba Iron Ore. If the results of these two entities were to be excluded from the analysis, it would have been a decrease in value of approximately 2%. This is due to the difficult operating environment the industry faced, continued threats of labour unrest, increasing costs and declining commodity prices, somewhat offset by a weakening rand exchange rate.

It must further be noted that the full impact of the unprecedented five-month strike in the Rustenburg platinum belt experienced during the first half of 2014 has not been included in the reported results analysed here except for Impala Platinum's results.

The value received by employees represented 38% (2012: 38%) of the value created. The value presented, as a percentage, remained flat over that of the prior year despite the increase in salaries and wages. If the exceptional results of Kumba Iron Ore were to be excluded from the breakdown, employees received 48% (2013: 46%) of the value created. This occurred in an environment of decreasing employment within the mining sector.

According to Statistics SA, the number of employees employed within the mining sector in June 2014 was 4.1% less than in June of the prior year, which is similar to the decrease of 4.3% experienced from June 2012. This suggests a trend of increased pressure on companies to manage resources and costs through downsizing.

Figure 20: Directly employed mining employees (Thousands)



Source: Stats SA

The high percentage of value received by employees is not sustainable and is expected to move back to a longer-term average of 30% through either a return to profitability or, if that is not possible, through a decrease in the number of employees.

It should be noted that this amount excludes benefits from share schemes for employees, which are reflected as part of shareholders' dividends and share-based payments. In some instances, this is substantial.

The state received 20% (2013: 20%), consisting of direct tax, mining royalties and tax on employee income deducted from employees' salaries. The actual contribution received by the state is significantly higher, with indirect taxes like VAT, import and export duties also being collected. As more companies start to report their total payments made to governments in line with the Extractive Industries Transparency Initiative, we will in future be better able to assess their contributions.

Distributions to shareholders decreased from 19% to 11% and declined significantly in rand terms.

This distribution is skewed by the performance of Kumba Iron Ore and the resulting dividend of R13.7 billion (2013: R18.0 billion).

Excluding Kumba Iron Ore, shareholders received only 2% of value created (2012: 7%), highlighting the volatility of returns to shareholders and the continued pressure on the entities analysed to contain and manage costs and mine efficiently in a tough economic climate.

Funds reinvested in the form of acquisitions and capital additions made up 34% (2012: 41%) of the total value created. This high percentage of reinvestment, although less than in the prior year, highlights the long-term nature of capital investment required to maintain production levels in the mining industry and puts pressure on additional distributions to employees and investors.

To create more value for all stakeholders, it will be necessary to increase the size of the pie. An increase in the number of profitable mines will increase the total benefits received by employees, the Government and investors. It will also provide greater resources for mining companies to spend in and on the communities in the vicinity of their operations.

Creating an environment with adequate infrastructure, less policy and regulatory uncertainty and a skilled, yet flexible workforce should attract investment and benefit all stakeholders.

Mining tax regime in South Africa currently under review

A significant portion of the value created by mining companies goes to the state.

The Davis Tax Committee (DTC) was given terms of reference by the former Minister of Finance that specifically states that it needs to make recommendations on whether the current mining tax regime is appropriate, taking account of:

- The mining sector's commitment to contribute to growth and job creation, to remain a competitive investment proposition and to contribute to better working and living conditions; and
- The challenges the mining sector faces, which includes low commodity prices, rising costs, falling outputs and declining margins, including its current contribution to tax revenues[5]

5 Terms of Reference of Davis Tax Committee: Mining Sub-Committee http://www.taxcom.org.za/termsofreference.html

The DTC's terms of reference are more or less in-line with the National Development Plan relating to mining; that is to promote, amongst others, growth in job creation and exportation, and the creation of a more competitive infrastructure.[6]

The DTC is the first committee to revisit the terms of the Marais Committee, which was appointed by the Minister of Finance and contributed to the mining tax regime reform back in 1988.

The Marais Committee focused mostly on gold mining due to the fact that taxation generated from gold accounted for approximately 10% of total tax revenue during 1987, having fallen since 1981 when it contributed approximately 27%.[7]

6 National Development Plan, page 39

7 Report Of The Technical Committee On Mining Taxation, December 1988, Chapter 3

In the 1980s, gold was South Africa's most important export commodity, whereas today it is only the fourth-most exported commodity after, coal, iron ore and platinum.

The commodity landscape has changed significantly since the Marais Committee provided its recommendations on the South African mining tax regime. This may therefore lead the DTC to a change in focus to other commodities in South Africa.

Understanding the tax design principles

An ideal minerals taxation regime is one that is both neutral and progressive. It is, however, difficult to achieve this in practice, but governments are encouraged to strike a balance between them.

During the assessment of a new approach to tax policy by the Treasury Committee of the House of Commons in London in 2011, it emphasised the importance of a tax policy change:

Over the long term, there may be a case for substantial changes to the tax system. As society and the economy changes, the tax system should change to reflect them.

There are several key tax design principles that should be incorporated in any tax policy and there are often trade-offs that need to be made between these different principles. Targeted relief should also be provided where such reliefs can be justified as externality-correcting (for example support for investment spending).[8] The key tax design principles will be discussed in short in the next few paragraphs.

Neutrality

A tax system should minimise economic distortions. A tax instrument will be neutral if investments and production decisions are not distorted by tax.[9] This closely interlinks with the 'flexibility' principal, as discussed below, where distortionary taxes have a strong negative effect on growth and employment.

8 OECD (2010), Tax Policy Reform and Economic Growth, OECD Publishing, Page 10 http://dx.doi.org/10.1787/9789264091085-en

9 Mining taxation – the South African context Economic Tax Analysis, August 2013 http://www.pmg.org.za/files/131106mining.pdf

The neutrality of export commodities is important to promote competitiveness in the international market and to ensure the efficient allocation of resources and investment.

Equity

The principal of equity can be addressed through the need for a tax system to be fair to all income earners, be it business, the wealthy or the poor. Achieving a level of fairness in society has been a topical issue for the past century. In a perfect world where there is equality of income among taxpayers, the principal of equity would be best addressed through proportionality in taxes.

Practice does not allow it to be this straightforward since inequalities do exist and therefore a tax regime should strive for equity through considering the entire range of taxes a taxpayer is subject to, the ability of taxpayers to pay and the benefits they receive from government. Therefore, those in similar circumstances should bear the same burden (horizontal equity) and those in different circumstances should bear an appropriately different burden (vertical equity).

Simplicity and certainty

It should not be difficult for businesses to understand the tax system and the cost of compliance should be kept as low as possible. The administrative and collection cost to the fiscus should also be kept low. This interlinks with the principal of creating certainty with clear and concise legislation, allowing taxpayers to know what taxes to pay and when to pay.[1]

Flexibility and stability

Where a tax regime specifically targets a certain commodity, government needs to make sure that the objective of this isolated taxation does not distort the economic performance of the commodity. In other words, careful consideration needs to be given to the elasticity of supply and demand of the commodity.[10] The tax regime needs to be amendable in times of change. As an example, reconsidering the appropriateness of the emphasis placed on gold in the 1980s. A fine line needs to be drawn between being too flexible and the need to create a sense of stability and certainty in the tax laws.

Global considerations

The International Monetary Fund (IMF) issued its 'Fiscal Regimes for Extractive Industries: Design and Implementation' report in August 2012.[11] The purpose of the report is to suggest better ways to realise revenues from extractive industries, particularly in developing countries.

A principle highlighted in this report is that taxes should be distributed fairly among different stakeholders such as companies, national government and regional government. The report suggests the best way to avoid corruption and erosion of tax revenue is to ensure that transparent, balanced, progressive and environmentally-friendly tax regimes are promoted.

The IMF continues to explain that the Extractive Industry Transparency Initiative (EITI), to which many resource-rich countries subscribe, requires extractive industry companies to publish what they pay and for governments to report what they receive, and for these amounts to be audited and reconciled. The EITI has led to important progress in transparency; however more needs to be done. For example, government accounting of resource revenue needs to be improved.

The IMF considers stability and credibility to be one of the most important issues currently facing the fiscal regimes for extractive industries. The IMF states that there needs to be a credible commitment by governments to maintain predictability in their fiscal regimes. This would also need to apply to the processes and/or criteria by which a fiscal regime may be modified.

A common rate of corporate income tax across all sectors is usually preferable. Corporate income tax is regarded as a tax attributable not specifically to resource extraction, but to doing business in the country; by contrast, royalty and any additional rent taxation are specific to resource extraction, representing a levy for the right to extract.[12]

Country circumstances require tailored regimes, but a regime combining a royalty and a tax targeted explicitly at rents (along with the standard corporate income tax) has appeal for many developing countries. Such a regime ensures that some revenue arises from the start of production, and that the government's revenue rises as rents increase with higher commodity prices or lower costs; in so doing, it can also enhance the stability and credibility of the fiscal regime (although processes to allow renegotiation may also be needed).[13]

[10] P Daniel et al.(2010), The Taxation of Petroleum and Minerals: Principles, problems and practice

[11] International Monetary Fund Report Fiscal Regimes for Extractive Industries (EI): Design and implementation http://www.imf.org/external/np/pp/eng/2012/081512.pdf

[12] International Monetary Fund Report Fiscal Regimes for Extractive Industries (EI): Design and implementation, Page 44 http://www.imf.org/external/np/pp/eng/2012/081512.pdf

[13] International Monetary Fund Report Fiscal Regimes for Extractive Industries (EI): Design and implementation, Page 6

The International Council on Mining and Metals (ICMM) issued a report[14] during 2009 on the issues and challenges in the design and application of minerals taxation regimes. One clear finding of the report is the need to establish a framework through which multi-stakeholder consultation can occur.

The ICMM argues that it is more feasible and preferable for mining companies to be subject to a country's general tax system, incorporating some mining-specific features that address some of the mining industry's special characteristics (e.g. special allowances). If taxpayers are on an equal footing, this may provide greater certainty and stability. This may increase incentives for governments to improve tax administration and fiscal policymaking more generally.

From the perspective of the companies that participated in the ICMM's research, stability and predictability are seen as the most important aspects of taxation regimes. A complex tax regime is likely to give rise to an increase in compliance and administration costs and disputes. Transparency is also an important factor as it can raise awareness of the financial benefits that mining delivers to a country and its citizens.

14 The International Council on Mining and Metals (ICMM) Report on Minerals Taxation Regimes: A review of issues and challenges in their design and application, February 2009. http://www.icmm.com/document/520

Changes in a mining tax regime should encourage investment

Important factors that investors seek include stability and predictability. Uncertainty can be reduced if the government has a legislated tax regime that reflects consistency across the entire industry rather than having to negotiate contract terms and arrangements per project. [15]

One of the purposes of the Fraser Institute Annual Survey of Mining Companies[16] is to assess what affects stakeholders' investment in exploration by looking at mineral endowments and public policy factors such as taxation and regulatory uncertainty.

The survey most recent survey found that investors considered the region's policy climate to be an important factor in investment decisions. The policy climate included factors such as uncertainty concerning administration of current regulations, environmental regulations, regulatory duplication, legal system and taxation regime, uncertainty concerning protected areas, disputed land claims, infrastructure, socioeconomics and community development conditions, trade barriers, political stability, labour regulations, quality of geological database, security, and labour and skills availability.

Countries such as India and Brazil were in the same range as South Africa relating to the policy perceptions participants held. The outcome for South Africa reflects a large expectation gap between pure mineral potential with world-class policies in place and the status quo with current policies in place. These findings suggest that South Africa has approximately 30% room for improvement on its current policies.

15 International Monetary Fund Report Fiscal Regimes for Extractive Industries (EI): Design and implementation, Page 6

16 Fraser Institute Annual Survey of Mining Companies 2013 http://www.fraserinstitute.org/uploadedFiles/fraser-ca/Content/research-news/research/publications/mining-survey-2013.pdf

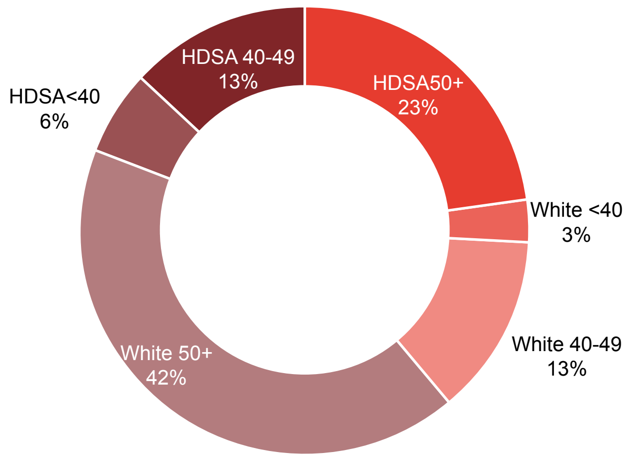
6. Boardroom dynamics

Board composition

An analysis of the companies suggests that the mining industry currently exceeds the minimum empowerment levels of board representation required by the Mining Charter.

At present, 41% (prior year 43% of the companies analysed) of board members are represented by HDSAs. The Mining Charter requires a minimum of 40% representation by 31 December 2014. When this board composition is analysed by age it interesting to note that 35% of board members are younger than 50 and 54% of these board members are HDSA.

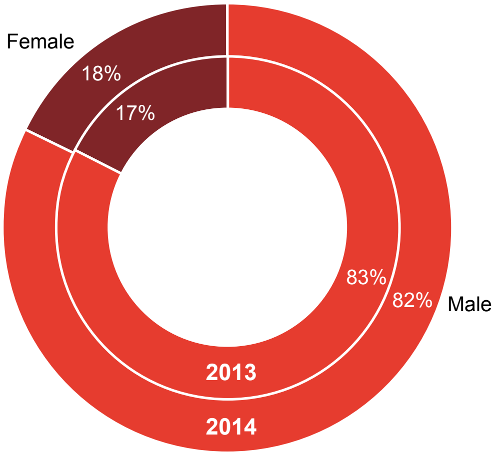
Figure 21: Board composition by race and age



Source: PwC analysis

Female representation at board level also exceeds the minimum requirements of 10% by 2014 set out in the Mining Charter.

Figure 22: Board composition by gender

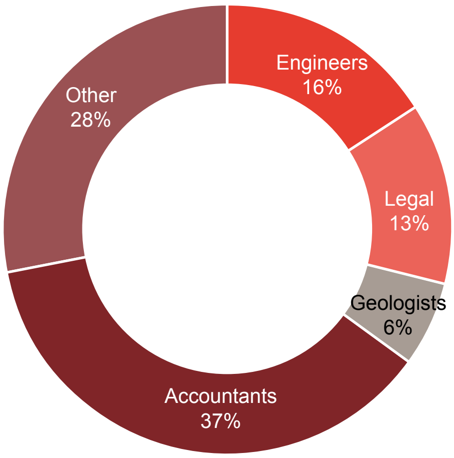


Source: PwC analysis

The changing mining and governance environments require a changed skill set. The average board size for the companies analysed was nine, which allows for an adequate spread of skills. The smallest board had three members and the biggest board 15 members.

Although qualifications are by no means the only indication of expertise and experience, the following categorisation of board members by their primary qualification provides an interesting spread. As expected, board members provide a wide array of experience.

Figure 23: Board skills represented



Source: PwC analysis

7. Financial performance

Five-year summary

The information included for the five-year summary provided in this section differs from the rest of our analysis as it includes the aggregated results of those top companies reported on in each edition of SA Mine.

The column for 2013 presented below relates to the results of the companies included in the previous edition of this publication, while in the financial review, we analyse the results of this year's top-37 companies for both 2014 and 2013.

The reason for the difference in revenue and EBITDA for 2013 between this summary and the income statement used in the financial performance section relates not only to the entities excluded from the publication offset by new entities included, but also to the first-time adoption of *IFRS 11 Joint Arrangements*.

Revenue and EBITDA is negatively impacted in the current year with the adoption of IFRS 11, which more often than not requires incorporated joint arrangements to be equity accounted and not proportionally consolidated as was the practice previously.

Although this change in accounting treatment does not impact net profit, it reduces all categories on the income statement and increases associate income. It also reduces items categorised separately on the balance sheet with an increase in the net investment figure.

Five-year summary

	2014 R 'billions	2013 R 'billions	2012 R 'billions	2011 R 'billions	2010 R 'billions
Revenue	327	332	339	303	227
Adjusted EBITDA	91	92	123	101	48
Net profit	6	25	65	55	20
Adjusted EBITDA margin	28%	28%	36%	33%	21%
Net profit margin	2%	7%	19%	18%	9%
Cash flow from operating activities	70	69	112	62	40
Total capital expenditure	57	71	70	55	58
Total assets	694	714	650	595	548

Source: PwC analysis

The five-year summary shows an initial recovery in revenue and profitability since the financial crisis of 2008. However, it also reflects the economic woes of the last two years, which have seen a decrease in revenue and profitability. Net profits are at their lowest levels since the inception of this publication and total assets decreased for the first time.

Financial performance for 2014

Income statement	Current year R 'billions	Prior year R 'billions	Difference R 'billions	% change
Revenue from ordinary activities	327	291	36	12%
Operating expenses	(236)	(208)	(28)	13%
Adjusted EBITDA	91	83	8	10%
Impairment charge	(49)	(20)	(29)	145%
Depreciation	(34)	(36)	2	(6%)
PBIT	8	27	(19)	(70%)
Net interest	(6)	(3)	(3)	100%
Tax expense	(8)	(13)	5	(38%)
Equity accounted income	9	9	0	0%
Discontinued operations	3	7	(4)	(57%)
Net profit	6	27	(21)	(78%)
Adjusted EBITDA margin	28%	29%		(1%)
Net profit margin	2%	9%		(7%)

Source: PwC analysis

As expected given the turmoil in the industry, financial performance was disappointing.

Revenue

Revenue increased by R36 billion on last year. Top-10 companies accounted for 81% (R29 billion) of the revenue increase. Over the past three years the top-10 companies have continued to account for approximately 85% of the revenue generated by the companies in the analysis.

Most notably, the revenue increase was as a result of:

- Anglo Platinum up R9.7 billion to R52.8 billion;
- Kumba Iron Ore up R9 billion to R54.5 billion;
- AngloGold Ashanti up R3.7 billion to R55.1 billion;
- Gold up R2.8 billion to R19 billion; and
- ARM up R2.7 billion to R10 billion.

The increase in Anglo American Platinum's revenue is as a result of R8 billion due to exchange rates, a R3.3 billion increase in volumes sold and a R1.9 billion decrease as a result of commodity dollar prices. This result does not reflect the impact of the extended strike in the platinum sector, which only commenced after the Anglo American Platinum year end.

The increase in Kumba Iron Ore's revenue is as a result of R7.0 billion from exchange rates, R2.3 billion in iron ore price increases and a R0.3 billion decrease as a result of a decline in sales volumes.

Revenue

	Current year R 'billions	Prior year R 'billions	Difference R 'billions	% change
Gold	122	119	3	2.5%
Platinum	109	97	12	12.4%
Other	96	75	21	28%

Source: PwC analysis

Gold mining companies have continued to be top contributors in terms of revenue for the companies analysed. This is on the back of the weak rand and satisfactory production performance.

Platinum sector performance only includes the impact of the strike for Impala Platinum, as Lonmin and Anglo American Platinum's year ends were before the commencement of the strike. The impact of strike on these entities will be reflected in the next financial year.

The National Treasury estimated that the mining sector contracted by 25% in the first quarter of 2014 and that 19% of the contraction was as a direct result of the strike in the platinum sector.

This finding was echoed in the Reserve Bank's Quarterly Bulletin in the June 2014, where it indicated that real gross domestic product shrank at an annualised rate of 0.6% in the first quarter of 2014. The bulletin attributed the negative growth in the first quarter of 2014 to the marked decrease in the real value added by the mining sector, reflecting the impact of the prolonged strike in the platinum sector.

The severe impact of the industrial action is reflected in these examples from the annual reports of companies analysed:

- Anglo Platinum: 440 000 ounces of lost production;
- Lonmin: 348 000 ounces of lost production; and
- Impala Platinum: 411 000 ounces of lost production

Using a rand platinum basket price of R22 000, the lost revenue over the strike period amounted to approximately R26 billion.

Operating expenses

Operating expenses increase by 13%, which is lower than the 16% seen in the previous financial year. However, when adjusted to remove the effects of the R3.8 billion reduction in costs owing to the cost saving measures implemented by Impala over the unprecedented five-month long strike, operating expenses showed a 16% increase on the prior year, proving that operating costs continue to remain a challenge for miners.

A breakdown of the operating expenses for companies that disclosed expenses by nature (representing 94% of aggregated revenue) is depicted in the table that follows, with the year-on-year increase for these companies also included.

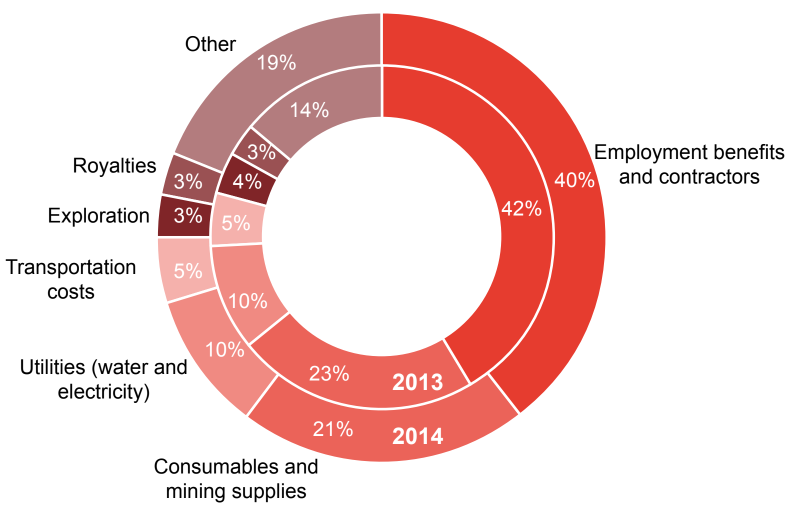
Breakdown of operating expenses

Year-on-year increase (decrease)

Cost component	Current year excluding Impala	Current year	Prior year
Employee benefits and contractors	10.5%	8.4%	14.3%
Consumables and mining supplies	6.0%	2.4%	14.6%
Utilities	12.2%	11.5%	17.2%
Exploration	(7.0%)	(7.6%)	55.1%
Royalties	24.6%	21.0%	(11.0%)
Transportation costs	12.7%	12.7%	32.1%
Other	53.9%	58.7%	58.9%

Source: PwC analysis

Figure 24: Breakdown of operating expenses



Source: PwC analysis

Labour costs

Labour costs are still by far the biggest cost component in the South African mining industry. The share of labour costs decreased marginally from 42% to 40% in the current year. Labour cost percentages vary from above 50% for deep-level conventional mines to below 30% for those companies that mine predominantly opencast.

The unprecedented five-month platinum sector strike that commenced on 23 January 2014 ended with a three-year wage deal being struck on 24 June 2014. Some of the key terms of the agreement are:

- An annual increase of R1 000 per month in basic pay for A and B-band employees in years one and two and R950 per month in year three;
- Increases in basic pay of 8% per annum for C and D1-band employees for years one and two and 7.5% for year three and;
- Increases in both housing and living-out allowances

One of the mining companies' key concerns is that despite the vigorous discussions that were held in reaching agreement, productivity improvement did not form part of the final settlement.

The salary differential debate

The subject of remuneration in the mining industry – at the executive level, for entry-level workers and all levels in between has been a particularly hot topic this year. The platinum miners' strike earlier this year brought the debate regarding miners' income and living conditions the forefront of public debate, and also put the spotlight on CEO pay within the large platinum mining companies.

The median of total CEO pay within the large South African mining companies is R18 million, comprised of guaranteed package (salary and benefits) of R7 – 8 million, a cash bonus of around R3 million and the balance in shares awards totalling R7 million. This quantum, while many times that of junior workers, is in line with large listed companies in other industries in South Africa. Global mining companies pay their CEOs 2-3 times this amount!

Entry-level miners are in general paid better than their counterparts in other industries. We looked at the pay for the most junior job grades from the PwC REMChannel® survey, which contains salary data for many listed and unlisted South African mining companies. The data indicates that the miners are paid 5% higher in terms of base salary and 14% higher in terms of guaranteed package (including the value of additional benefits and allowances enjoyed by miners). In certain sectors of the mining industry, entry-level workers are paid more than 50% more than their counterparts in other industries.

Companies and their remuneration committees are trying to balance the economics and ethics of pay at the top and at the lower levels of the staff hierarchy. Global demand for the skills, experience and leadership abilities of mining executives and CEOs is pushing up salaries at the top, while the tough economics of the industry constrain what can be afforded for junior workers, despite the social pressure and the aspiration to narrow the wage gap and focus on the financial wellness of junior workers.

Average total guaranteed package year-on-year increases in the mining industry.

Employee category	2014	2013	2012	2011	2010
Executive	6.50%	6.50%	8.30%	8.80%	8.20%
Management	6.60%	7.00%	8.10%	8.80%	8.20%
Key specialist	6.80%	6.30%	8.90%	10.70%	8.20%
General staff	7.20%	7.20%	8.40%	8.50%	8.30%
Unionised staff	8.80%	7.20%	8.30%	8.90%	8.40%
Total average lift to payroll	7.00%	7.20%	8.40%	8.80%	8.30%
Average consumer price index	6.4%*	5.8%	5.7%	5.0%	4.3%

Year-to-date average CPI as at August 2014
Sources: PwC Remchannel Biannual Salary and Wage Movement Survey, Stats SA

The increase in total employee costs was 8.4% (10.5% when excluding strike-affected Impala), which is again well above inflation. The frequency of industrial action across the mining sector means that 2015 will again reflect above-inflation labour cost increases.

Mining companies have to continue to evaluate various means to improve productivity and optimise output.

Consumables and mining supplies

The consumables increase was in line with inflation.

Utilities

Utilities, including electricity and water represent 10% of total operating costs. The 11.5% increase in the current year is lower than the prior year increase of 17.2%. The utilities costs, excluding Impala Platinum, reflected an increase of 12.2%.

In August 2014, NERSA agreed to Eskom recouping costs of R7.8 billion from its previous price period. This has resulted in tariff increases of 13%, which is more than twice the inflation rate. Unless companies are able to increase the efficiencies in the use of power, we can expect utilities costs to continue seeing double-digit increases year on year.

As utilities already represent 10% of total operating costs, it is essential not only from a power security point of view, but also from a cost-saving perspective, that companies focus on opportunities to decrease their power consumption.

Exploration costs

Exploration expenses have declined by 7.6% in comparison to the prior year. Although exploration costs are generally cut back in challenging times, it is pleasing to note that the cost increased for most companies that disclosed exploration costs. The decrease mainly relates to AngloGold Ashanti, which cut back on exploration as part of its Project 500 cost-cutting initiatives.

Royalties

Royalty expenses reflect existing contractual royalty payments as well as mining royalties paid to the fiscus. The increase is mainly as a result of higher royalties due to higher revenue and a higher royalty rate at Kumba Iron Ore.

Transportation costs

This cost component impacts the bulk commodity producers most. The increase relates mainly to volume increases at Kumba Iron Ore as well as higher rail tariffs.

Impairment provisions

Consistent with the global trend, there were significant impairments recognised. At R49 billion (2013: R20 billion), impairment charges were up 145% over the prior year. Impairments equates to 86% of the current year capital expenditure and 12% of the total mining assets.

The top-10 companies accounted for 91% of the total impairment charge, up from 62% in the prior year.

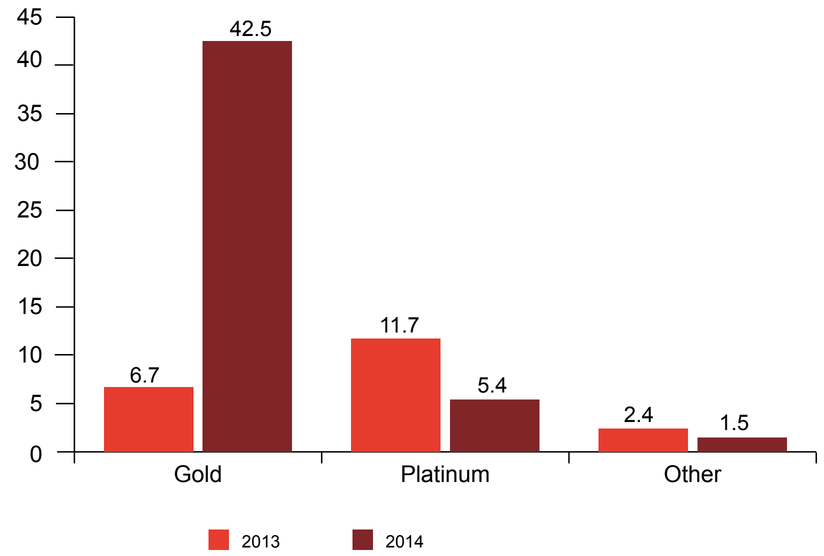
Gold companies impaired R42.5 billion in the current year. The bulk of the impairments recognised in the current year were as a result of R32 billion and R8.3 billion in impairment charges recognised by AngloGold Ashanti and Gold Fields respectively.

Only R3 billion of AngloGold Ashanti's impairments were from South Africa, with the remainder from its operations in the rest of Africa and the Americas.

Gold Fields' impairments were also largely as a result of impairments outside South Africa at St Ives, Damang, Tarkwa and the Arctic Platinum Project.

Platinum mines continued to feel the pressure in the current year as a result of the lower PGM basket price. The lower prices were partly offset by the weakening rand. A total of R5.4 billion was impaired by platinum companies. Notable of these is the R2.87 billion in impairments recognised by Anglo Platinum, largely on its Rustenburg operations.

Figure 25: Impairments per commodity (R'billions)



Source: PwC analysis

Depreciation

Lower depreciation is starting to reflect the lower asset base after the impairments of the last two years and lower capital investment as part of cash preservation strategies.

Net interest

The low level of finance costs reflects the traditionally low levels of gearing maintained by most South African mining companies. However, the 100% increase in finance costs, from R3 billion in the prior year to R6 billion in the current year, points to the increase in borrowings required by mining companies to fund operations. Not included in this cost is borrowing costs capitalised against the development cost of qualifying assets.

Taxation

The effective tax rate of 400% is well above the prior year effective tax rate of 54% and the statutory rate of 28%. This increase is as a result of non-deductible impairment provisions, where no deferred tax assets could be raised.

Net profit

Net profit reduced by 78% despite an EBITDA improvement of 10% on last year, owing to the R49 billion impairment that has been recognised in the current year. The EBITDA margin is 28% in the current year, consistent with the prior year.

Seven companies achieved an EBITDA higher than the average.

Companies with EBITDA above 28%

	Current year	Prior year
Petmin Limited	70%	74%
Assore	60%	76%
Kumba Iron Ore	56%	55%
AngloGold Ashanti Limited	35%	40%
Sibanye Gold	31%	30%
Royal Bafokeng Platinum Limited	31%	22%
Pan African Resources Limited	29%	58%

Source: PwC analysis

The picture is very different when considered on a commodity-specific basis.

EBITDA by commodity

EBITDA	Current year R 'billions	Prior year R 'billions	Difference R 'billions	% change
Gold	35	41	(6)	(15%)
Platinum	18	12	6	50%
Other	38	30	8	27%

EBITDA margin	Current year %	Prior year %	Difference %
Gold	28%	35%	(7%)
Platinum	17%	13%	4%
Other	40%	40%	0%

Source: PwC analysis

Although these margins seem to indicate that the industry is still profitable, the lower EBITDA puts pressure on companies' ability to reinvest for the future as apparent in the reduction of capital investments from R70 billion to R57 billion. The R35 billion gold EBITDA was merely sufficient to cover gold's capital investment and taxes, leaving no profits to settle its significant borrowings.

Platinum's improved profitability is potentially misleading as the comparative numbers of Anglo American Platinum and Lonmin were impacted by the 2012 strike action, while the 2014 strike action is not included in their current year results. The lower platinum capital expenditure meant that the EBITDA was more than sufficient to cover capital and tax needs, but not to service borrowings.

The bulk commodities performed very well. However, they will come under pressure for next year as a result of the significant decrease in commodity prices.

Net profit by commodity

	Current year R 'billions	Prior year R 'billions	Difference R 'billions	% change
Gold	(27)	11	(38)	(346%)
Platinum	(0)	(13)	13	(100%)
Other	33	29	4	14%

Source: PwC analysis

Foreign exchange impact

The impact of the rand exchange rate on performance is quite substantial when compared to global mining performance. The prolonged weakening of the rand against the dollar since the end of 2013 has continued to have a pronounced impact on the difference in performance based on presentation currency. With lower dollar commodity prices masked by a weaker rand, the performance in dollar terms will be weaker than in rand terms.

When converting the income statements of the aggregated companies at the average rates applicable to their specific years, there is a difference in performance. In dollar terms, revenue was lower by 8% compared to the notable 12% increase in rand terms.

Income statement in US dollars

	Current year USD 'billions	Prior year USD 'billions	Difference USD 'billions	% change
Revenue from ordinary activities	33	36	(3)	(8%)
Operating expenses	(24)	(26)	2	(8%)
Adjusted EBITDA	9	10	(1)	(10%)
Impairment (charge)/reversal	(4)	(2)	(2)	100%
Depreciation	(4)	(4)	0	(0%)
PBIT	1	4	(3)	(75%)
Net interest	(1)	(0)	(1)	100%
Tax expense	(1)	(2)	1	(50%)
Equity accounted income	1	1	0	0%
Discontinued operations	0	1	(1)	(100%)
Net profit	0	4	(4)	(100%)

Source: PwC analysis

Cash flows

Cash flows related to operating activities

	Current year R 'billions	Prior year R 'billions	Difference R 'billions	% change
Cash generated from operations	84	85	(1)	(1%)
Other	(1)	6	(7)	(117%)
Income taxes paid	(13)	(16)	3	(19%)
Net operating cash flows	70	75	(5)	(7%)

Cash flows related to investing activities

Purchase of PPE	(57)	(70)	13	(19%)
Purchase of investments	(4)	(6)	2	(33%)
Sale of investments	1	3	(2)	(67%)
Other	(2)	(7)	5	(71%)
Net investing cash flows	(62)	(80)	18	(23%)

Cash flows related to financing activities

Proceeds from ordinary shares issue	26	1	25	2 500%
Proceeds from interest bearing liabilities	78	65	13	20%
Repayment of interest bearing liabilities	(101)	(36)	(65)	181%
Distribution to shareholders	(19)	(29)	10	(34%)
Net financing activities	(16)	1	(17)	(1 700%)
Net increase/(decrease) in cash and cash equivalents	(8)	(4)	(4)	100%
Cash and cash equivalents at the beginning of period	36	40	(4)	(10%)
Cash and cash equivalents at the end of the year	28	36	(8)	(22%)

Source: PwC analysis

Cash flows from operating activities

Operating cash flow change (R' billion)	
Gold	(12)
Platinum	2
Other	5
	(5)

The ability to convert profits into cash is crucial for any company. Cash from operations was stable compared to the prior year but lower than EBTDA.

However, cash from operating activities decreased by R5 billion. The biggest reduction in cash from operations was experienced in the gold mining sector and the cash increases generated by Sibanye Gold were completely offset by cash outflows recorded by AngloGold and Gold Fields.

The cash decrease was partly offset by the cash generated by the diversified mining sector and more notably Kumba Iron Ore.

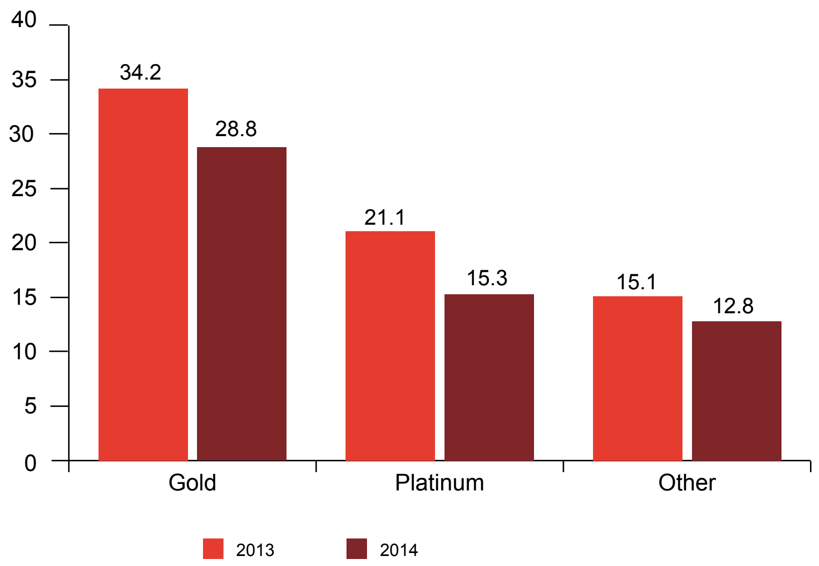
Cash flows from investing activities

The low-price environment caused companies to reconsider their capital expenditure and implement significant austerity measures.

Capital expenditure decreased by R13 billion (19%). It is not surprising that the gold mining companies have experienced decreases in capital expenditure given the impairments that have been recognised and the low commodity price environment.

The downward trend in capital expenditure in the platinum sector is unlikely to change in the short term as companies re-evaluate investments after the Rustenburg strike.

Figure 26: Capital expenditure per commodity (R' billions)



Source: PwC analysis

Of the aggregated capital expenditure, 80% was incurred by only six companies:

- AngloGold Ashanti (R15.7 billion, down from R16.3 billion);
- Gold Fields (R7.1 billion, down from R10 billion);
- Anglo American Platinum (R7.2 billion, down from R7.5 billion);
- Kumba Iron Ore (R6.5 billion, up from R5.9 billion).
- Exxaro Resources Limited (R4.8 billion, down from R5.3 billion); and
- Impala Platinum (R4.5 billion, down from R6.2 billion).

Given the uncertainty in commodity prices and announcements of reduced spending by companies, we expect levels of capital expenditure to be lower next year. This anticipated decrease in expenditure will negatively impact service providers to the industry.

Cash flows from financing activities

Equity

Proceeds from the issue of shares were up by R25 billion, from R1 billion in the prior year. Most notably, issuance of ordinary shares were the shares issued as a result of the unbundling of Sibanye Gold (R17 billion) and the Lonmin rights issue of R7.8 billion.

Borrowings

After the R29 billion inflow of borrowings in the prior year, companies had to start settling debt with a net decrease of R23 billion this year. Although these numbers are extremely high, R17 billion in both years related to the Sibanye unbundling and does not reflect a real change in financing trends.

Distributions to shareholders

The distribution to shareholders reduced from R29 billion in the prior year to 19 billion in the current year. The decrease is largely as a result of a decrease in distributions by Kumba Iron Ore (R4.3 billion), Gold Fields (R2.4 billion), Exxaro (R1.6 billion), Anglo Gold Ashanti (R1.3 billion) and Anglo Platinum (R560 million).

It is interesting to note that 99% of the distributions that were made were made by only nine of the companies within the top 37.

Financial position

Current assets

	Current year R 'billions	Prior year R 'billions	Difference R 'billions	% change
Cash and cash equivalents	33	37	(4)	(11%)
Inventories	60	52	8	15%
Receivables and other current assets	37	34	3	9%
Assets held for sale	3	21	(18)	(86%)
Total current assets	133	144	(11)	(8%)

Non-current assets

Mining and production assets	422	417	5	1%
Goodwill	9	10	(1)	(10%)
Investments	89	78	11	14%
Other non-current assets	41	38	3	8%
Total non-current assets	561	543	18	3%
Total assets	694	687	7	1%

Share capital and reserves

Share capital	298	250	48	19%
Reserves and non-controlling interest	126	144	(18)	(13%)
Total equity	424	394	30	8%

Current liabilities

Accounts payable and other liabilities	65	90	(25)	(28%)
Interest bearing liabilities	14	21	(7)	(33%)
Total current liabilities	79	111	(32)	(29%)

Non-current liabilities

Interest bearing liabilities	92	81	11	14%
Deferred taxation liabilities	64	67	(3)	(4%)
Other non-current liabilities	34	34	(0)	(0%)
Liabilities held for sale	1	0	1	100%
Total non-current liabilities	191	182	9	5%
Total liabilities	270	293	(23)	(8%)
Total equity and liabilities	694	687	7	1%

Key ratios

	Current year	Prior year	Global mine ratios
Net borrowings (R 'billions)	73	65	
Gearing percentage (percentage)	15%	14%	28%
Solvency ratio (times)	2.6	2.3	2.0
Current ratio (times)	1.7	1.3	1.5
Acid ratio (times)	0.9	0.8	1.1

Source: PwC analysis

Sound financial position

Solvency and liquidity ratios remained strong and have shown improvement since the prior year despite the weakening in commodity prices. The ratios indicate that the South African mining industry is less geared and less levered than the trends seen globally. This financial strength provides the industry with flexibility to operate and, where necessary, invest for the future.

These ratios are all derived from historical cost-carrying amounts and therefore do not necessarily reflect the true fair-value trends. A better indication of the weakening of the industry is a comparison between net assets and market capitalisation. The market capitalisation as a multiple of the carrying amounts strengthened marginally from 1.6 to 1.7. This improvement was unfortunately short lived, with a significant decrease after June 2014.

At an individual company level as at 30 June 2014, there were 16 (2013: 20) companies with net book values exceeding the market capitalisation of the company. This weakening from the prior year occurred despite the R49 billion impairments processed.

Ratios for only three of the entities included in the preceding year's list improved to such an extent that they were excluded from the current year. The market capitalisation for four entities weakened to the extent that they are now excluded from the list and the top 37.

Net asset value as a percentage of market capitalisation

	Current year	Prior year
Infrasors Holdings	535%	828%
Eastern Platinum	499%	871%
Coal of Africa	376%	174%
Village Main Reef	276%	223%
Zambia Coppper Investments	262%	116%
Harmony Gold	235%	219%
Wesizwe Platinum	175%	532%
BuildMax	160%	175%
Firestone Energy	154%	210%
Trans Hex Group	144%	140%
Lonmin	141%	94%
Gold Fields	133%	136%
Keaton Energy Holdings	131%	247%
Metmar	123%	185%
DRDGOLD	106%	69%
Merafe Resources	102%	153%

Source: PwC analysis

The preceding table shows a disconnect between the market perception of value for these companies and managements' perception of the fair value of the underlying assets. The reason for this difference may be attributable to incomplete information available to the market, differing perceptions over development successes and different long-term price assumptions. These companies face a tough task convincing the market of their value.

Working capital

Although there were 11 (2013: 10) companies with current ratios of less than one and 18 (2013: 18) companies with acid ratios of less than one, the aggregate liquidity and acid test ratios improved during the current year. The improvement in the aggregate current ratio has been largely as a result of decreases in short-term interest bearing borrowings at AngloGold and the unbundling and separate listing of Sibanye Gold by Gold Fields. Of the companies included, 17 improved their current ratios and acid ratios.

Financing for sustainability

As one would expect, the gearing ratio marginally increased from last year to 15%. This relative low level points to the fact that South African mining companies and banks have traditionally been conservative when it comes to funding mining projects. The gearing ratio is much lower than the global average of 28%.

Six entities had a higher gearing ratio than the global average with AngloGold Ashanti the most notable. In the wake of its attempted restructuring, it will be interesting to see how the company deals with its funding structure in a tough US-dollar gold environment.

Of the 37 companies aggregated, 24 (2013: 19) were in a net borrowing position. Of the top-10 companies, 80% (2013: 90%) were in a net borrowing position, as opposed to 56% (2013: 41%) of the remainder of the 37 companies reviewed.

The disparity in this ratio may indicate that financial institutions prefer to provide finance based on strong balance sheets rather than the project-specific finance required by mid-tier and junior miners.

Impact of accounting standard changes

This year's results were significantly impacted with the adoption of *IFRS 11 Joint Arrangements*, which more often than not requires incorporated joint arrangements to be equity accounted and not proportionally consolidated as was the practice previously. For this year it meant that, among others, the Assmang joint venture between Assore and African Rainbow Minerals was only included in the equity income line, removing R27.6 billion of revenue from the analysis with no impact on net profit.

This was also the first year for adoption of *IFRIC 20 Stripping costs in the production phase of a surface mine.* Its adoption did not have a significant impact on the current year results and only resulted in an increased of assets of approximately R1 billion on the balance sheet.

IFRS 15 Revenue from Contracts with Customers is likely to be the next accounting standard impact with a potential significant impact for mining companies. It is effective for annual reporting periods beginning on or after 1 January 2017. Entities will have a choice of applying the new standard fully retrospectively or retrospectively only to contracts that are not yet completed at the date of adoption of the standard.

Revenue recognition can present challenges for mining entities. Production often takes place in joint ventures, and entities need to analyse the facts and circumstances to determine when and how much revenue to recognise. Extracted mineral ores may need to be moved long distances and need to be of a specific type to meet smelter or refinery requirements. Entities may exchange product to meet logistical, scheduling or other requirements. The mining industry should consider how IFRS 15 will impact accounting.

A few considerations are discussed below.

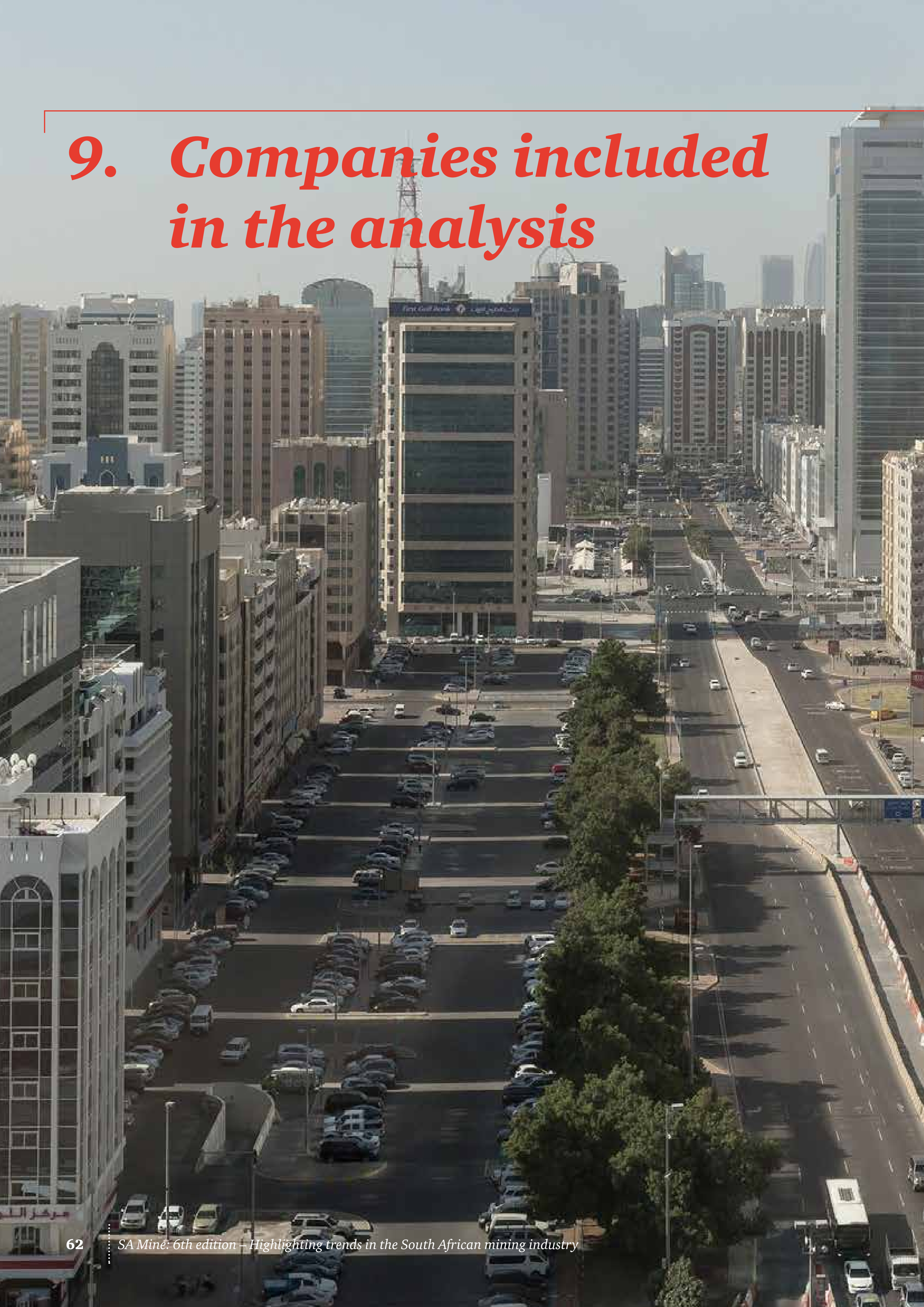
- **Delivery terms**
  Cost, insurance and freight (CIF) vs free on board (FOB). If the selling entity is responsible for carriage, insurance and freight, consideration must be given to whether the sale of goods and insurance and freight are separate performance obligations. If considered distinct (i.e. separate performance obligations), further consideration will be required as to whether the performance obligation for transport and insurance is satisfied over time.
- **Buy-sell arrangements**
  Mining companies may exchange mineral products with other mining companies to achieve operational objectives (for example saving transportation costs). Variations on the quality or type of the product can sometimes arise. Balancing payments are made to reflect differences in values. The settlement may result in gross or net invoicing or payments. Consideration needs to be given to whether these arrangements are in the scope of IFRS 15. Non-monetary exchanges between entities in the same line of business to facilitate sales to customers are specifically scoped out of IFRS 15. IFRS 15 also requires a contract if revenue is to be recognised. A contract only exists if there is commercial substance to the transaction.
- **Forward-selling contracts to finance development**
  The owner of a mineral interest sells a specific volume of future production from specified properties to a third-party 'investor' for cash. The owner will use the cash to fund the development. The investor assumes significant reserve, production, and price risk. If future production is inadequate, the seller has no obligation to make up the shortfall.

  Consideration needs to be given to whether the transfer of legal title to the mineral reserves in the ground and the promise to extract these minerals from the ground are separate performance obligations. The upfront payment may be seen as a significant financing component, which would need to be taken into account when determining the transaction price. Although the investor may not have physical control of the minerals upon entering into the forward sale, they could have legal control, which could result in earlier recognition of revenue.
- **Provisional pricing arrangements**
  Sales contracts for certain commodities often incorporate provisional pricing. At the date of delivery of the ore a provisional price is charged, the final price is generally an average market price for a particular future period. Consideration needs to be given as to whether the provisional pricing is within the scope of IFRS 15, thus treated as variable consideration, or outside the scope of IFRS 15, as its considered to be a derivative within the scope of IFRS 9/IAS 39.
- **Tolling arrangements**
  Certain companies involved in the industry provide value-added services to companies that mine ore or unprocessed mineral products. These companies may be involved in smelting, washing, refining or transporting products on behalf of a mining company. The mining company may have agreed the sale with the end user or be selling to the smelting or refining company, which will then sale to the end user. Consideration is required as to whether the smelter or refining company is acting as an agent or principal. IFRS 15 provides guidance on agent/principal considerations.

8. Glossary

Acid ratio	(Current assets less inventory)/Current liabilities
Adjusted EBITDA	EBITDA adjusted for impairment charges
Adjusted EBITDA margin	Adjusted EBITDA/Revenue
BEE	Black Economic Empowerment
CPI	Consumer price index, published by Statistics South Africa
Current ratio	Current assets/Current liabilities
DMR	Department of Mineral Resources
DTC	Davis Tax Committee
DWS	Department of Water and Sanitation
EBITDA	Earnings before interest, tax, depreciation and amortisation
EBITDA margin	EBITDA/Revenue
EITI	Extractive Industry Transparency Initiative
ETF	Exchange-traded fund
FDI	Foreign direct investment
Gearing percentage	Net borrowings/(Net borrowings plus equity)
HDSA	Historically disadvantaged South Africans
ICMM	International Council on Mining and Metals
IMF	International Monetary Fund
JSE	Johannesburg Stock Exchange
LTIFR	Lost time injury frequency rate
Market capitalisation	The market value of the company calculated as the number of shares outstanding multiplied by the share price
MPRDA	Mineral and Petroleum Resource Development Act
NERSA	National Energy Regulator
Net borrowings	Interest-bearing debt, less cash
NWA	National Water Act
NWRS 2	The National Water Resources Strategy 2
PBIT	Profit before interest and tax
PGM	Platinum group minerals
SLP	Social and Labour Plan

9. Companies included in the analysis



	Year end
African Rainbow Minerals Limited	June 2014
Anglo American Platinum Limited	December 2013
AngloGold Ashanti Limited	December 2013
Aquarius Platinum Limited	June 2014
Assore Limited	June 2014
Atlatsa Resources Limited	December 2013
BuildMax Limited	February 2014
Coal of Africa Limited	June 2014
DRDGOLD Limited	June 2014
Eastern Platinum Limited	December 2013
Exxaro Resources Limited	December 2013
Firestone Energy Limited	June 2014
Gold Fields Limited	December 2013
Goliath Gold Mining Limited	December 2013
Harmony Gold Mining Company Limited	June 2014
Impala Platinum Holdings Limited	June 2014
Infrasors Holdings Limited	February 2014
Keaton Energy Holdings Limited	March 2014
Kumba Iron Ore Limited	December 2013
Lonmin plc	September 2013
Merafe Resources Limited	December 2013
Metmar Limited	February 2014
Northam Platinum Limited	June 2014
Pan African Resources Limited	June 2014
Petmin Limited	June 2014
Randgold & Exploration Limited	December 2013
Resource Generation Limited	June 2014
Royal Bafokeng Platinum Limited	December 2013
Sibanye Gold Limited	December 2013
Tawana Resources NL	December 2013
Tharisa Plc	September 2014
Trans Hex Group Limited	March 2014
Village Main Reef Limited	June 2014
Waterberg Coal Company Limited	June 2014
Wescoal Holdings Limited	March 2014
Wesizwe Platinum Limited	December 2013
Zambia Copper Investments Limited	March 2014

Basis for compiling this report

We aggregated the financial results of mining companies with a primary listing on the Johannesburg Stock Exchange (JSE) and mining companies whose main operations are in Africa and that have a secondary listing on the JSE, for the financial year ends to June 2014. We used a cut-off market capitalisation of R200 million and excluded all companies with suspended listings.

Our selection criteria excluded global mining companies Anglo American, BHP Billiton and Glencore Xstrata. Although these companies have a significant South African footprint, their global exposure and size means that they do not necessarily reflect trends in the South African mining environment. A large number of the entities included also have international exposure. However, the bulk of their operations are in Africa.

The results aggregated in this report have been sourced from information that is publicly available, primarily annual reports or reviewed results made available to shareholders. Companies have different year ends and report under different accounting regimes.

Information has been aggregated for the financial years of individual companies and no adjustments have been made to take into account different reporting requirements and year ends. As such, the financial information shown for 2014 covers reporting periods from 1 October 2012 to 30 June 2014, with each company's results included for the 12-month financial reporting period that falls into this time frame.

Information for the previous year comprises information for the 37 companies selected in the current year, except where indicated otherwise.

All currency figures in this publication are reported in South African rand, except where specifically stated otherwise. The results of companies that report in currencies other than the rand have been translated at the average rand exchange rate for the financial year, with balance-sheet items translated at the closing rand exchange rate.

Some diversified companies undertake part of their activities outside the mining industry. No attempt has been made to exclude such non-mining activities from the aggregated financial information.

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10. About PwC

Our global footprint as a firm means we have the right people to support you everywhere

*Over **1 500** mining professionals across the globe located in all significant mining territories*

*More than **195,000** people who are committed to delivering quality in assurance, tax and advisory services*

*Professionals in **157** countries, working collaboratively*

Navigating the territory....

Our ability to quickly combine the right competencies, market knowledge and mining industry insights – uniquely for each client issue and territory – sets us apart from the rest.

We help organisations explore opportunities, navigate risk, achieve business goals and change business networks across Africa. Our professionals have financial and operational experience, knowledge of business processes, and industry insight which enables us to listen and understand your goals and the environment (competitive, economic and regulatory) in which you operate and provide you with a solution that's right for your organisation.

***Our promise** to you: 'Our relationship with you **creates the value** that you are looking for'.*

Our African mining practice actively recruits seasoned, multi-disciplined leaders with proven industry experience, a demonstrated ability to solve the most difficult business problems and a history of leading successful and sustainable continuous improvement initiatives from start to finish. We believe it's critical that our professionals can quickly understand your business, challenges and culture and then design and implement an effective solution for your organisation.

Apart from our extensive global reach and our deep level of industry experience and skills, building relationships with our clients is key to us. This is the core of what makes partnering with us effective and the return on your investment with us invaluable.

An extensive African Footprint

Our offices…

Africa is a vital part of our agenda…..

Our African mining practice focuses on delivering professional services to companies of all sizes across the region. We operate in 34 countries in Africa as a whole, with over 9 000 staff and more than 400 partners. This means that we're able to provide our clients with seamless and consistent service, wherever they do business on the continent. Our in-depth knowledge and understanding of African operating environments enables us to offer tailored tax, assurance and advisory solutions for every business challenge.

Mining Centre of Excellence

Globally, our PwC mining network has benefited from a more co-ordinated market approach through the Americas' Mining Centre of Excellence. In line with this approach, aimed at strengthening the collaboration of the mining teams in the Africa region, 2014 has seen the birth of the Mining Centres of Excellence (MCoE) in the South, East and West Market Regions in Africa. Our Africa MCoE assists with requirements and requests of companies operating within the mining industry. Our strategies are developed and matured to ensure that we support all companies operating throughout the African continent, which will be made possible with concerted co-ordination between the centres in all three regions.

Our primary mandate is to ensure that we develop strategies that will establish an integrated approach across lines of service and regions so that we deliver a seamless service to mining clients to enhance the returns on their operations – thus delivering to you the real value you are looking for.

Contacts

With mining experts working in each key mining area across South Africa, our teams are helping clients deliver on specific projects and organisational growth aspirations. We offer advisory, tax and audit services to global corporations and locally-listed companies.

We complement this with:

- A suite of niche mining consulting capabilities focused on optimising value across mining operations and effectively managing risk; and
- A comprehensive client feedback programme to ensure we are consistently delivering on individual client needs.

For any mining related queries, services or assistance required, please contact our Mining Centre of Excellence at mining.africa@za.pwc.com.

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