Accessing Finance in a Depressed Economy- Finance Options for the Mining Sector

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1. The Importance of the Mining Sector in Zimbabwe

Mining is one of the most important economic sectors of the Zimbabwean economy, contributing significantly to economic recovery since 2009, with an average annualized growth of more than 30% experienced in the sector up to 2011. However, growth of the sector has slowed down with projected growth being revised to 8% for 2012, 6.5% for 2013 and 11.4% for 2014.

In its latest economic blue print, ZimAsset, the government recognizes mining as one of the four critical sectors (Agriculture, manufacturing, mining and tourism) to drive medium term economic recovery (2013-2018). The importance of the mining sector can be deduced from its contribution to GDP and exports. The sector has been contributing greatly to broad macroeconomic aggregate including 47 percent to total exports in 2011 and 2 percent to total employment. These statistics reveal the relative importance of mining in the country hence the need for creative financing to spur the growth of the sector.

2. Constrained capacity of the local banking sector

Since the advent of the multi-currencies, the capacity of the local banking sector to finance the economic requirements of the various sectors of the economy has been a function of a host of interrelated factors: domestic deposits growth, credit lines and exports growth and regulatory or prudential guidelines. Funding in a multi-currency regime depends on a few sources and these include; export earnings, diaspora inflows, offshore credit lines, foreign direct investment inflows and capital transfers including grants.

Currently the Zimbabwean banking sector is characterized by slightly above US$4 billion dollars in deposits of which above 70 percent are transitory in nature. This on its own is a major handicap of the banking sector to be able to finance the mining sector. It is out of these little resources that all sectors of economy require a share. The local money markets have failed to take off meaningfully, with the local capital markets i.e. ZSE also failing to provide an adequate platform for fund raising for adequate economic development. This then calls forth for the economic players to strategize and look at means of accessing finance from outside the country. We have seen big corporates including Bindura Nickel Corporation taking this route.

3. Alternative Sources of Finance

Traditionally, the local mining sector has been financed via the following channels: Internal funding through revenue inflows; shareholders' equity (listed and unlisted ordinary and preference shares, partnerships, joint ventures etc.); debt financing from various sources including shareholders loans; structured financing from buyers and syndicated loans from various banks locally and internationally.
However in the liquidity constrained environment characterizing the country, Banks in Zimbabwe are not in a position to meet the capitalization needs of many players in the mining sector.

Therefore, there is need for a contextualization of the abilities of the local banking sector as well as having a clear understanding of the limitations of the local stock exchange in attracting sufficient levels of capital for the mining sector. It is imperative to look at the alternatives sources of financing to circumvent the liquidity challenges affecting the country.

Thinking outside the box becomes critical at this juncture of economic development in sourcing financing by the mining houses so that the goals of Zim-Asset are achieved. These alternatives should include pursuing non-traditional potential funders. Some of the methods of accessing finance are outlined below;

Issuance of Corporate bonds

A corporate bond is a bond issue by a corporation. It is a bond that a corporation issues to raise money effectively in order to expand its business.The term is usually applied to longer-term debt instruments, generally with a maturity date falling at least a year after their issue date. These can be structured in five, ten, fifteen and twenty year maturities depending on the mineral under consideration.

Joint venture partnerships

A joint venture is a temporary partnership that two companies form to gain mutual benefits by sharing costs, risks and rewards. In this case the mining companies need look outside the country for potential suitors brings in money, capital and relevant skills. The arranngement should have the exit strategy and should have a predefined lifespan.

Royalty funding

Royalty based financing is an innovative way to raise capital for mining businesses and has been used for countless decades in oil and gas reserves and other stream of income trusts. The interesting part about royalty based financing is that you can get the money you need while decreasing the amount of equity you have to give up

Off-take finance or contract financing

An agreement between a producer of a resource and a buyer of a resource to purchase/sell portions of the producer's future production. An offtake agreement is normally negotiated prior to the start of a mining project in order to secure a market for the future output of the facility. This type of arrangement is suitable for minerals such as chrome.

Escrow account arrangement

An Escrow account arrangement entails establishing a bank account with a reputable bank for purposes of managing working capital drawdowns for specific projects on the understanding that proceeds from the sale of resultant products are deposited with the bank that controls the account. In a depressed economy such as the Zimbabwean economy where the risk attending to the economy are high, an Escrow account can be established offshore with a tight legal agreement/arrangement possibly with offshore guarantees, in order to support working capital requirements for mining companies. This arrangement will give comfort to the financiers whose fears will be based on nonperformance.

Streaming arrangements

These are contracts for ongoing supply of mineral production under which upon advance payments of a premium, the buyer agrees to purchase at a fixed , discounted and predetermined price, all or part of the mineral to be extracted by a mining company during a certain period or throughout the life of a mine. The mining company receives an upfront payment, which enables it to develop, construct and or expand the mine.

4. Conclusion and Recommendations

The ability of the mining sector to access financing in a depressed economy like the one currently characterizing the country requires that the mining companies to be innovative and look beyond the borders. The ability of the sector to attract financing require that the laws governing mining in the country are transparent and investor friendly. Other issues that would require attention include; the current indigenization laws should be clarified; the Staff Monitored programme adhered to, the mining supporting infrastructure e.g. railway lines attended to.