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New model for risk reporting

Market regulators will have to get involved if miners are to explicitly address jurisdictional risk in presenting their investment prospects.

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A change in leadership, such as Jacob Zuma's substitution for Cyril Ramaphosa (pictured), will almost always bring a change in risk profile

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Over the past two weeks, my ‘From the Capital' columns have discussed various aspects of jurisdictional risk.

In one example - Danakali in Eritrea - a company with an outstanding mineral prospect is in a country with a reputation for being one of the most unfriendly places in the world for business. Danakali appears untroubled.

In another case - Nucoal Resources in New South Wales - everything went pear shaped for the company as a government far more highly regarded than that of Eritrea recanted all its prior approvals.

A plethora of publicly-funded and private institutes now regularly opine on the differences in real and perceived business risks across national and provincial borders.

In the past month, Transparency International and Canada's Fraser Institute have released survey results supposedly based on the opinions of the best informed about country risk. Both groups have recorded large variations in the quality profiles of different investment jurisdictions.

More anecdotally, industry executives readily express views in private about different jurisdictions and, when appraising potential investments themselves, claim to take account of the policies, track records and expected behaviours of governments under whose jurisdiction they might fall.

Despite the overwhelming evidence and widespread belief that jurisdiction matters, companies happily eschew objective analysis of jurisdictional risk once they have chosen their development projects or exploration targets and begin soliciting investment interest.

Even worse, companies run the risk of being captured by the governments on which they rely for their commercial well being. This is especially so when state-owned enterprises become joint venture partners. Feasibility studies, to be signed off by a government representative, are unlikely to analyse policy risk objectively.

> “ **A simpler solution might involve a requirement to benchmark a company's risk assessment against a recognised and credible source**

At one level, this may be considered of no consequence. The largest investors will be more than capable of analysing the risk characteristics of their investment destinations. Some may even specialise in placing capital in regions or countries which others avoid.

At another level, companies whitewashing public statements to avoid offending host governments or local partners are failing to meet market obligations designed for the day-to-day protection of ordinary investors.

A possible change of government, for example, always carries business risk. The risks may vary considerably but will never be zero.

Ask Highfield Resources, whose Spanish potash project with all the protections of EU law was stymied at a critical time by an inconclusive election result in December 2015.

Certainly, none of the iron ore miners in the Pilbara who faced the prospect of rejigged royalty arrangements after the 2017 state election in Western Australia would feel elections carry negligible risk.

Nucoal had the rug pulled from under its entire business after a change in government in New South Wales.

The transfer of power in a one-party state used to riding roughshod over constitutional process and unused to elections is at least as problematic as these instances.

Australia's corporate and market regulator says a company should present all the relevant information private investors or their advisers may reasonably require to make a decision about whether to invest.

Against that standard, can a company claim to have fulfilled its obligations if it fails to mention in its formal market disclosures anything about the country risks that it is incurring?

The least reasonable approach is for issues such as these to be swept aside as if they did not exist.

A consistent framework used across all companies facilitates a better understanding of the corporate risks to be confronted and the extent to which they might differ from company to company.

Already, companies are obliged to adopt reporting frameworks that address the most commonly asked questions about the technical and marketing aspects of their activities.

Presently, the JORC Code, for example, only tangentially addresses matters of country risk.

The code could be amended to include the many factors that together comprise a country risk appraisal. This potentially complicates the reporting requirements unnecessarily.

A simpler solution might involve a requirement to benchmark a company's risk assessment against a recognised and credible source. The Investment Risk Index within the Mining Journal World Risk Report (feat. MineHutte ratings) is an example of such a benchmark.

The JORC Code could require a company to address country-specific risks by referring explicitly to issues raised by the Investment Risk Index (or those of some other reputable and approved analytical source).

This is not to say that Danakali, for example, must concede that Eritrea is one of the most corrupt countries on the planet, as some surveys claim. Danakali directors might believe Eritrean risks are no different to the risks it might incur from mining in Western Australia or Saskatchewan. It would be open for the company to make that case. Or it could offer evidence that widespread negative perceptions about Eritrea do not apply to its specific circumstances.

Investors acquiring exploration interests in New South Wales may need to be told that the state's investment risk ranking is the lowest of any Australian state or territory. An exploration licence can be revoked, they should be told, and ministers may be obliged to test the market for better offers, in the case of renewals, if they are to meet the stringent definition of proper ministerial conduct enunciated by the courts.

The next Eritrean leadership transfer may prove uneventful. The Nucoal experience might be a unique historical aberration. The disparate jurisdictional qualities highlighted by groups as diverse as Mining Journal, Transparency International, the Fraser Institute, the World Bank or the Natural Resource Governance Institute might have no bearing on the conduct of future mining developments. We will only know after the event.

Whatever eventually happens, hindsight is not much help to investors who need to assimilate country risk into their thinking ahead of a decision.

Regulators will need to follow through on their noble statements of principle if investors are to get the tools to make the necessary judgements.

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