A COLLOQUIUM ON THE GLOBAL COMMODITY CRISIS AND ITS IMPACT IN AFRICA

HOSTED BY AMDC AND TJN-A

tax justice network- Africa

African Minerals Development Centre

United Nations
Economic Commission for Africa

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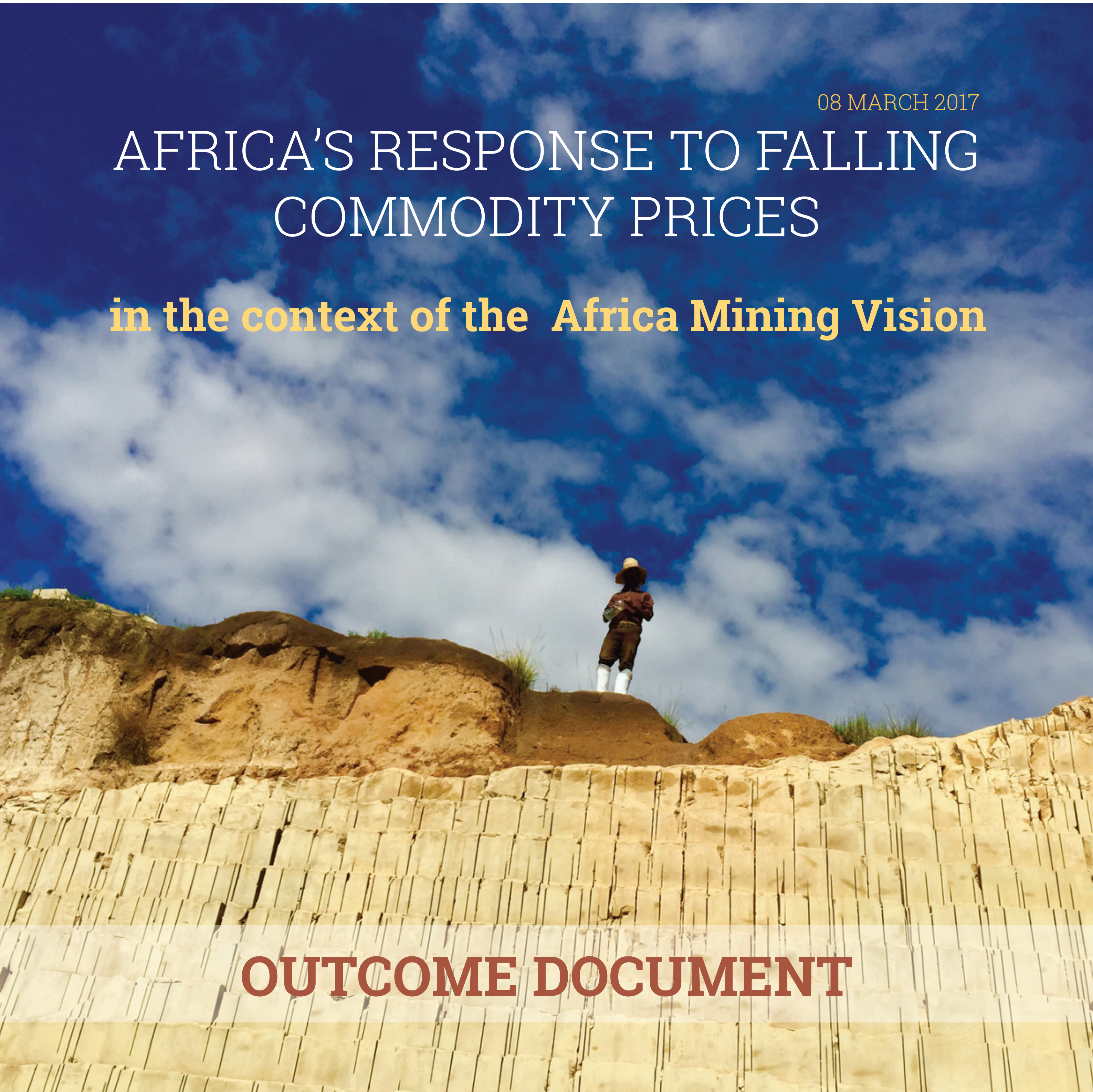
AFRICA'S RESPONSE TO FALLING COMMODITY PRICES

in the context of the Africa Mining Vision



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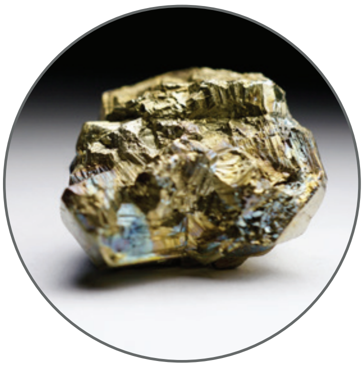

Kojo Busia, Acting Coordinator of the African Minerals Development Centre, welcomed participants and noted the significance of the Colloquium being held on International Women's Day. The partnership between AMDC and TJN in hosting this colloquium was also acknowledged with the reference to past work that the two institutions have engaged in together, such as Illicit Financial Flows (IFFs).

Dr. Busia noted that the Africa Rising narrative which has been adopted to describe the high growth for over a decade was driven by the commodity price boom, with fuel and minerals fueling exports and foreign exchange earnings. Countries were ill prepared for the subsequent fall in commodity prices which brought this boom to an end.

Fortunately, the Africa Mining Vision (AMV) was adopted as a forward-thinking framework which recognizes this boom-bust cycle of mineral prices and highlighted the need to buffer economies from harmful volatility by linking minerals with other inclusive, value-added economic activities. In addition to falling commodity prices, IFFs from Africa are also a major hindrance to the potential of African economies' transformation with at least half of the $50 billion in annual IFFs attributable to the extractives sector.

Given this environment, Dr. Busia suggested that sober reflections are now needed as per the narrative of the AMV on how African economies may finally end their vulnerability to commodity price booms and busts. AMDC is already assisting countries to develop Country Mining Visions (CMVs) which onboard the AMV goals to make minerals a driver of development and economic transformation. A facilitator of this is value addition and related upstream and downstream activities along the mineral value chain. Indeed, AMDC support extends to ASM, GMIS, economic linkages and other areas of assistance provided to member States.

These discussions come at the right time to address structural issues across Africa before this boom-bust cycle repeats itself, and the prevailing low prices provide more incentive to pursue related but alternative economic activities. On this note, Dr. Busia wished participants successful deliberations.

Mr. Alvin Mosioma, Executive Director of Tax Justice Network – Africa (TJN-A), re-iterated the significance of International Women's Day and noted how the meeting room was somewhat reflective of how male-dominated the mining and minerals sector remains, and that this narrative should surely be changing fast by now.

Mr. Mosioma also acknowledged the strides that have been made by TJN-A and AMDC especially considering TJN-A's involvement when the AMV started during the International Steering Group (ISG). As tax experts, TJN-A's view of the extractives industry was one of untapped potential for true fiscal transformation, and the fact that the AMV has made strides to being domesticated via CMVs is a massive shot in the arm for the development of African economies and the continent as a whole. Further informing this perspective is the research commissioned by TJN-A within Ghana, Tanzania and Zambia and their respective sub-regions in terms of fiscal governance with respect to the AMV.

In that same vein, the High Level Panel on IFFs Chaired by H.E. Thabo Mbeki points out that the extractives sector presents the biggest challenge on illicit outflows at both the domestic and global levels for African economies. At the national level, tax incentives, with the dynamics of the race-to-the-bottom amongst African economies, lead to the erosion of the tax base. Globally, transfer pricing continues to inhibit progress. This ultimately leads to insignificant contributions to development. The extent to which IFFs can stunt growth and development is evident form the UNCTAD report and Panama leaks, amongst other sources.

Mr. Mosioma concluded by confirming that this colloquium thus comes at a very welcome point in time that ensures that re-invigoration of AMV tenets highlights how falling commodity prices will not be as severely detrimental for African economies once the AMV is domesticated.

"Sober reflections are now needed on how African economies may finally end their vulnerabilities to commodity price booms and bust"

SESSION 1

The impact and response to falling commodity prices by African governments

The commodity price decline and its macroeconomic consequences – Komi Tsowou, ECA

Mr. Tsowou began with the global context of the commodity price decline, with the United Nations Conference on Trade and Development (UNCTAD) mineral, ores and metal index losing 45 per cent between 2011 and 2016.

Commodities account for over 80 per cent of exports of over half of African countries, which increased their vulnerability to markets. Falling prices have increased fiscal deficits, increased debt vulnerability, worsened current account deficits and depleted foreign reserves of mineral producers in particular. For example, Zambia's fiscal deficit increased from 1.8 per cent of GDP in 2011 to 9.1 per cent in 2015. Debt stock increased by nearly 75 per cent of GNI in Mozambique between 2011 and 2015.

China has a significant impact on global commodity markets, accounting for example for 60 per cent of global iron demand. The US and EU have spillover effects.

Overall, there is continuing uncertainty in commodity markets, warranting an overhauling of commodity policies in Africa with a focus on economic and fiscal diversification. Examples can be drawn from Gabon with a recently inaugurated metallurgical manganese processing complex.

Responses of African governments: Short-term and long-term perspectives using the regional lens – Abdulai Darimani, Institute of Local Government, Ghana

Dr. Darimani highlighted the bountiful mineral and commodity endowments by country and sub-region in Africa, and indicated some global and regional trends, drawing attention to commodity price shocks throughout history such as in the 1940s, 1970s, 2008 and 2015, in which intervening global economic and other events had various effects. These commodity shocks affect national revenues, budget deficits and currencies. Potential government responses to these are monetary, budgetary and fiscal.

In the case of Ghana, the government introduced measures to boost revenue given falling mineral rents through other fees and measures. Expenditures did begin to fall after 2012.

It will be important to move beyond traditional economic measures and include diversification and transformation in African countries' policy priorities for the long-run, to lessen vulnerability. We also need to shift our financial resource mobilization strategies away from FDI and incentives and towards local enterprise development. A regional approach will help in establishing standards and unified approaches in this.

Dr. Paul Jourdan, an independent consultant in resource-based development, noted that the issue of IFFs intervenes with the impact of commodity prices. Tanzania's Minerals Audit Agency and Chile's stability fund present best practice scenarios for African countries in addressing the scale of IFFs, and responsibly applying the benefits of commodity booms. These alternative methods of raising and applying revenue are needed as FDI inherently creates value for offshore shareholders, not governments and citizens.

Dr. Jourdan noted that in fact the 2008 global financial crisis was not spurred by the financialization of commodities but rather the roughly US$6 trillion that was lost due to toxic assets in the United States.

Talks of a commodity price rebound are premature and should be tempered by various factors in global commodity markets. He confirmed that China's influence as a major minerals consumer has driven global commodity prices, particularly through its growth deceleration. Over-capacity exists across several minerals, for example iron.

This moment is in fact ideal to invest in downstream value addition, as it is cheaper now to set up plants than in the past 5-10 years. For example, power plants are half as expensive to establish as during the commodity boom. Industrial minerals for development should be a key area of focus for Africa, given the endowments of industrial minerals, the role they could play in other sectors and across the economy, and their nature as a relatively lower cost low hanging fruit for transformation. These strategies should be financed domestically.

Fatima Fernandes Mimbire, Coordinator of research, Centro de Integridade Pública, Mozambique, agreed that another commodity boom may not be imminent. Mozambique was caught unaware during the price rise and fall and the focus should now be on re-organizing and preparing for the next boom. Yet, there are limited capacities to negotiate and insufficient institutional overlap – for example between parliament, the revenue authority and other bodies. Limitations also exist in financing capitalization of downstream manufacturing.

To prepare for future booms, resource rent tax negotiations should capture windfall rents. Low prices are leading to a re-think on fiscal regimes, particularly to take a regional view and approach. Going forward, we need to ensure we do not mortgage on our development during periods of low prices. Social responsibilities need to be taken onboard in mineral development policy. And African nationals need to be better involved in the economy and future economic diversification activities.

SESSION 2

Fiscal regimes governing commodities in Africa

Curbing the race-to-the-bottom: towards a dynamic approach to harmonizing fiscal regimes in Africa's mineral sector – Charles Akong, AMDC

Mr. Akong began his presentation by noting the importance of natural resources for revenue, which contribute about US$381 billion of the total US$461 billion taxes collected in Africa. Tax contribution from resources has been falling due to low commodity prices. Effects of the commodity price downturn have, however, varied depending on the minerals in question.

Regarding fiscal regimes applied to the minerals sector, most African countries employ a contractual system, in which fiscal tools vary depending on the writing of individual contracts. Licensing systems, on the other hand, feature tax and royalty issues embedded in legislation and uniformly applied. This system is more comprehensive and institutionalized, and would be preferable.

In general, African fiscal regimes remain patchy, incoherent and inconsistent, giving firms an upper hand in negotiating preferential clauses and risking a race-to-the-bottom in mineral contracts.

Fiscal harmonization would ensure a united policy framework to prevent this. Levels of harmonization include standardization, alignment, coordination, cooperation and convergence. Alignment provides significant harmonization while also taking country and mineral specificities into account. This approach is supported by AMDC. Fiscal harmonization is also closely linked with promoting regional mineral value chains.

African countries have generally employed three types of royalty regimes – ad-valorem royalties based on fixed percentages are the most common and easiest to implement, but are regressive and not sensitive to market conditions. Unit-based royalties are generally not sensitive to profits. Profit-based regimes provide a good alternative but are complex to administer. In practice most African countries employ mineral-specific royalties rather than standard royalties for all minerals.

Due to limited capacities, countries have been unable to put in place more complex mechanisms, which has prevented them from reaping benefits of past commodity booms. Countries also have significant loopholes and oversights which allow illicit financial flows to arise. Legislation in fact does not even address these IFFs.

Overall, Mr. Akong proposed that a hybrid approach involving institutionalizing fiscal mineral tools in policy, while harmonizing with a view to aligning fiscal regimes, would prove most beneficial for African countries. In this sense, harmonization is like an orchestra – it does not involve every country hitting the same note but rather different notes that fit together.

Taxation and the state of AMV domestication in Ghana, Tanzania and Zambia - Kwesi Obeng, TJN-A

Mr. Obeng's presentation showcased findings from country studies undertaken by TJN-A in order to illustrate experiences of different mining countries in domesticating the AMV, showcasing what kind of progress has been made seven years after adopting the AMV. Overall, there has been national-level progress but not as much as hoped for, and there has been little regional progress.

These studies focused on the AMV pillar of fiscal regime and revenue management, using the 2011 AMV Action Plan as a benchmark.

The findings indicated that all countries have made progress, including in monitoring and auditing of minerals exports and negotiating of contracts, and there are capacities to engage in these. Yet, there is inadequate awareness and visibility of the AMV, and IFFs present a significant challenge, with weak systems in place to evaluate tax regimes and safeguard leakages. Overall, there has been rising tax revenue in these countries – not necessarily due to better systems but for other reasons.

At regional level, the AMV calls for the continent to review its fiscal environment, develop mineral taxation guidelines, and guidelines for revenue management. But very little has been done, particularly in the EAC.

We need to increase awareness of the AMV and concrete guidelines for AMV domestication, and the AMDC can play a central role in this and in other country-level support, as it has provided to Tanzania, for example.

Enhanced capacities of institutions at national levels are needed to address these fiscal issues. Bilateral treaties and double tax agreements need to be revisited, to ensure these serve the interests of African countries, and that they adopt a regional approach. Stabilization funds can help cushion against low commodity prices and safeguard the interests of future generations.

Dr. Ola Bello of Good Governance Africa commented that in fact not all mineral producers and resource countries have high tax-to-GDP ratios – for example, it is low for both Nigeria and Angola.

African countries have been moving to legislation rather than contract-based approaches in the wake of the commodity price fall. In order to address IFFs, we need to focus not only on the tax regime, but capacity to implement. A profit-based system, for example, would require significant capacity to audit firms. Regionally, there is a role for Regional Economic Communities (RECs) and for the AMV to lead to regional mining visions, with the assistance of AMDC.

Dr. Bonny Matshediso of the University of Botswana noted that while Botswana may not have been as badly hit by the downturn as other countries, it has still faced negative repercussions such as job losses. Diversification efforts have gone on for some time but have not borne fruit.

The points discussed during this colloquium need to be carried forward by civil servants in order to ensure that our recommendations are implemented.

Successes in industrialization and structural transformation are few and far between across the continent. And yet, in addition to being more counter-cyclical, we should also be able to benefit more when prices are high.

Regional integration will be key in order to build on competitive advantages and develop a select few centers of processing (such as smelters), fed into by various mineral producing countries.

SESSION 3

The way forward - panel discussion

Vanessa Ushie, Pan-Africa Extractive Advisor, Oxfam, noted that we have seen several negative effects of the commodity crisis, such as budgetary challenges. There are global and regional approaches to addressing this, including the Sustainable Development Goals (SDGs) and the AMV, so there is a track record in this we can build on. International institutions can support this (providing alternatives, policies, capacities etc.). There is a pressing need to include commodities in regional and national industrialization strategies.

Sovereign wealth funds and other instruments give African countries the opportunity to save, empower future generations and deal with perennial volatility in commodity markets. There have been mixed results with this so far in Africa but opportunities can be better harnessed going forward.

H.E. Albert Yankey, Ambassador of the Republic of Ghana, listed some questions on this topic that come to mind, and which illustrate the urgency of the issue: do governments view these issues as urgent as the experts do? How often do responsible government ministries sit down to discuss these issues? Tanzania's success may shed light on the importance of leadership – taking a stand and doing things. He highlighted examples in problems in West Africa's regional approach: pipelines exist, resources exist, but there are still energy shortfalls. Why? What has gone wrong? We need to put these issues on the agenda of African ministers of finance and economic planning every year, by first proposing this to the Ministers of Mining and having them push their peers and colleagues. This issue rarely features so centrally, in fact.

Alvin Mosioma, Executive Director of TJN-A, asked if this discussion amongst experts is "preaching to the converted" – we all know the importance of the issue, the question now is what to do? Our governments knew what was coming but did nothing – whether in famine due to the failure of rains which could have been foreseen, or the commodity crunch due to foreseeable low prices. The problem was not a lack of knowledge of what to do – it just didn't happen. There are vested interests preventing progress on preventative measures. We also need to address our tunnel-vision focus on FDI, but how do we promote domestic capital and increase existing domestic investment in order to keep our money in Africa? There are positive domestic examples such as Dangote. There are also domestic solutions to IFFs, such as reducing the debt-equity-ratio. Overall, this may be less an issue of capacity and more of political will. Indeed, there are already African experts on these tax issues.

Biniam Behre, First Secretary-Political Officer at the Permanent Mission of the State of Eritrea to AU and UNECA, explained that while a newcomer to industrial mining, Eritrea is mineral-rich, and wants to learn from the experience of others in order to optimize benefits such as employment, technology transfer and linkages. Eritrea's 1995 legislation was similar to the AMV. The Government is a major actor in the sector, with active participation through ENAMCO and at all levels of decision making, diminishing the problems of transfer pricing and misinvoicing. Thus far, 17 local and foreign companies are engaged in exploration and mining. There is a need to develop monitoring capacity in order to expand this number of companies. Eritrea is cooperating with the AMDC, and the country's mining sector has featured growth and success. Revenue from mining is invested in diversification, infrastructure and human capital development. These efforts are needed across the continent so that if resources are depleted, we do not go from poor and mineral rich, to poor and mineral poor. Africa's resources are helping to industrialize others – we need to be the ones who benefit from our endowments.

Policy Recommendations

Based on the presentations, discussions, and examples highlighted from specific member States, a number of recommendations emerged from the colloquium for African policy makers, think tanks, CSOs and international organizations to take forward in harnessing mineral resources to transform economically and socially. These include the following:

1. Mineral-based industrialization and diversification

Volatility and boom-bust cycles are here to stay – Africa cannot affect this, but it can address its economic reliance on primary commodities. Global commodity markets are inherently volatile and affect employment, incomes and exchange rates – not only in Africa but for wealthy commodity producers such as Australia and Canada as well. Diversification and beneficiation are critical to lessening this effect somewhat. Mineral--based industrialization through both upstream inputs and downstream beneficiation should underpin economic development in commodity producers, particularly given the reliance of the "Africa Rising" narrative on commodity boom cycles. This can be pursued first through mundane minerals – steel, polymers, fertilizers, and other realizable activities. Country examples note the importance of this as well. While Cote d'Ivoire is not a big mining exporter, it has raw material experience in agriculture, and also experience negative effects of the price downturn. Value-addition and diversification are recognized as the ways forward to reduce vulnerability.

2. Political will for change and building institutions

Deliberations during the colloquium noted that these exact issues have been discussed for generations. We as stakeholders in African development need to focus on why this has not yielded positive results. One reason identified is that despite expert and technocrat conclusions, there has been a poor record of implementation and little political will amongst those in power to radically re-shape the structure of Africa's mineral economies. In the end, technocrats can only get so far without a political agenda.

Indeed, political will and corporate will are both essential to reach our goals in transformation. Active involvement of both public and private sectors can help link existing markets with potential domestic supply through processing of Africa's own natural resources, such as the case of oil in Nigeria.

A further challenge at the political will is deciding on what type of industrialization Africa wants to pursue. It could, for example, emulate South Korea, which chose specifically which strategic sectors to move into. South Korea defied its endowments and technical advice of outsiders in order to process steel and move into high value activities such as ship building. For this, however, strong and assertive leadership was needed to defy conventional wisdom.

The institutional aspect of mineral resource governance cannot be ignored – how can we pre-empt detrimental commodity market changes with stronger and more coherent institutions in Africa governing the sector? Clear platforms and coordinated roles should exist for this. National institutions for extractives can potentially take the needed steps based on rigorous analysis and quasi-independent of political influence. Tanzania has successes at the national level but some, such as Mozambique, have witnessed opposition to an extractives supervisory body.

It is the role of AMDC, ECA and the AU to promote active and implementable policy making in its member States.

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~ Biniam Behre, First Secretary-Political Officer at the Permanent Mission of the State of Eritrea to the AU and UNECA

Policy Recommendations

3. Regional Cooperation and Integration to spur Pan-African mineral transformation

All of the positive policy prescriptions revealed during this colloquium work better in the regional sense than at the national level alone. There are several reasons for this, namely the cooperation needed to reach the ambitious goal of mineral-based transformation, and the fragmentation and small size of individual markets.

Regional integration is not a new initiative across Africa, but it has had mixed successes in different cases. It is, however, emerging as an imperative for mineral-based economies, for example as a platform to push for Regional Value Chains (RVCs). Building up regional markets can lower vulnerability to global developments. Indeed, industrialization efforts can only succeed if production and markets are of a large enough scale. For example, one steel blast furnace in China produces more than entire demand of any African REC, including COMESA, highlighting the need to pool markets and production to reach more productive economies of scale.

Analyses are needed of what investments should be made regionally, for example whether one regional gas plant can serve a sub-regional market, rather than several small and inefficient national plants. Of the three primary minerals needed to produce fertilizer, no one country in Africa has all three, but most have one or two – thus regional cooperation will help, based on empirical analysis with realistic policy recommendations. AMDC should conduct specific studies such as this, and continue to encourage countries to come together to find common solutions to mineral price volatility.

Regarding fiscal policies and combating IFFs, while it is difficult to harmonize across borders, this is the only way to ensure that strong national policies are not circumvented. For example, despite developments in Gabon banning the export of raw wood, neighboring countries do not have similar laws, leading to smuggling in the absence of a strong regional approach. Political engagement at the REC-level should focus on deepening RVCs and fiscal harmonization while also protecting national economies and preventing regionalization from devolving into a predatory hub-and-spokes system.

4. Capacity building, human capital and enabling technology advancements

It is clear that the interventions suggested here will require enhancing the skills, technology and bureaucratic capabilities at play in order to facilitate a move from low-skill, low-technology extraction into more advanced activities.

The building up and sharing of knowledge is envisioned by the AMV, with commensurate political will to ensure the development of a knowledge-based mineral economy. Indeed, one area of progress of the AMV has been geo-mapping. The issue of access to and onboarding of technology is also crucial in establishing linkages, moving into new economic activities and moving towards transformation.

Despite many problems, progress has been made in some areas around the AMV, such as geo-mapping. It may be useful to have an indaba-style platform to share experiences and to particularly address the issues of sustainability and linkages in industry. There also needs to be more engagement of academic institutions on this subject for insights and data.

Strong capacities do exist across Africa, for example on technical, geological and fiscal issues, and we need cross-country capacity building and sharing in order to learn from each other.

Meanwhile, the stockpiling of mineral reserves, particularly of rare earths, can decrease accurate knowledge of endowments and supply, and increase the risk of future volatility. This is furthered by the emergence of synthetics, and requires more detailed studies of the levels and implications of reserves.

The knowledge needed across the continent can come in as simple a form as operational definitions on common terms. For example, we all agree that we need regional integration but this term evokes different definitions from different actors.

AMDC already engages in capacity building as one of its key activities, and can support these recommendations and build towards long-term transformation through a number of short-term actions, including: identifying and sharing best practices by subject (auditing, governance, contracts, sovereign wealth funds etc.), location (Tanzania with auditing, etc.), and mineral-specific studies.

5. Harnessing development financing for mineral-based transformation

Utilizing domestic resources for development is a key tenet of the Addis Ababa Agenda for Action, and it plays an important role for financing the costly investments in upstream and downstream mineral activities.

Ending fiscal leakages will help harness more lost revenues throughout the mineral value chain. The case of Tanzania illustrates a well-functioning mineral auditing system that involves all agents (mines, processing, exporters etc.), which can provide lessons to other countries. While it employs a contractual approach, this in fact reflects what exists in legislation. Regime stability is most important. New ventures in oil and gas are learning from past mistakes made in mining.

Financially, laws allowing the outflow of funds or keeping of currency in off-shore accounts provide structural limitations on promoting domestic investment. Sovereign Wealth Funds (SWFs) can help minimize effects of commodity price shocks, but we need to define what we will use SWFs for – they should not come at the expense of capital for local economic activities. Other innovative domestic sources of financing should be vigorously pursued as well.

Now is the time for action, as mining MNCs do not yet lobby as much in Africa as they do in Australia and Canada. Organizations such as AMDC can convene different tax stakeholders in order to address the discrepancy between tax policy and implementation and build a coherent cross-sectoral framework.