

## South African Precious Metals Sector

### Recap of Strikes: Who Has Lost What

- **Snapshot** — Press reports on illegal strikes in the SA gold and platinum sectors have been plenty and have dominated headlines over the past two months. In this note, we provide a snapshot of events and summarize the impact on production, revenue, profit, salaries and tax.
- **Losers all around** — We estimate that 185k ounces of gold and 602k ounces of PGMs have been lost due to illegal strikes y-t-d. Combined, we estimate this has cost the gold and platinum sectors R9.6bn in revenue and R7.2bn in profit. Employees have lost R2.4bn in salaries, the Government R2.1bn in taxes. LON, IMP, AMS, ANG and GFI have been most affected, NHM, AQP, RBP and HAR least.
- **No end in sight** — Our discussions with CEOs and industry experts (refer: “[SA Labour Crisis – When and How will it End?](#)”) suggest that a speedy resolution to strikes is unlikely. We maintain our preference for the metals over the equities. Within equities, we prefer IMP (Buy) as it is the beneficiary of current industry restructuring. We remain bearish on SA gold stocks. A resolution to the strikes may result in a near-term rally in these equities; we recommend selling into the rallies.

#### ■ Industry Overview

##### Johann Steyn

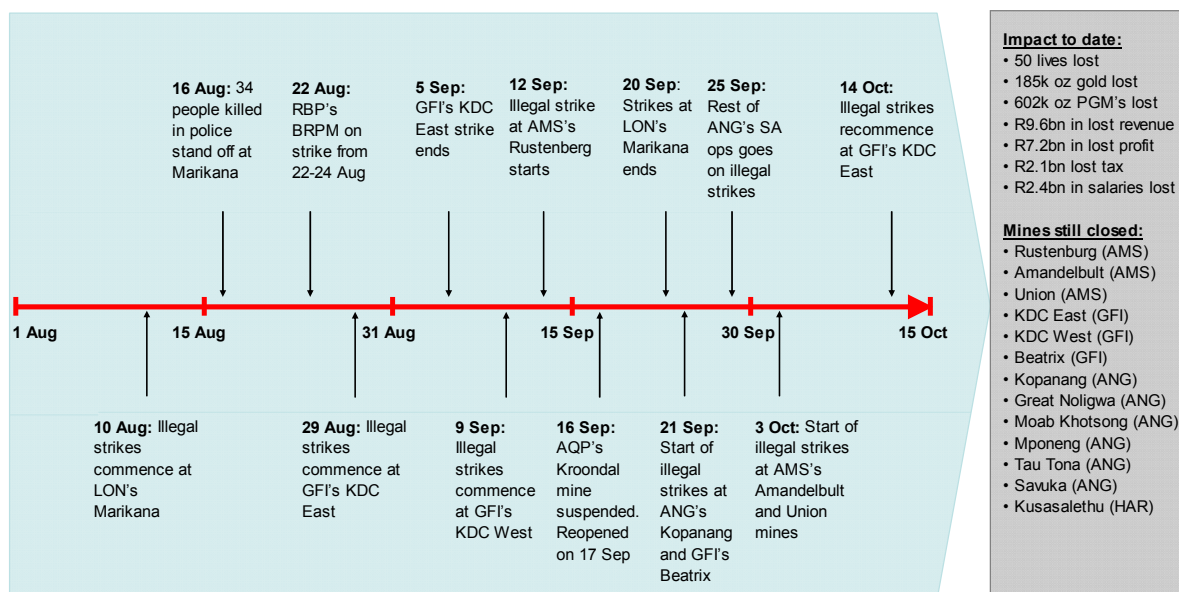
+27-11-944-0087

johann.steyn@citi.com

##### Craig Irwin

craig.irwin@citi.com

Figure 1. Time line and impact of illegal strike action in the SA precious metals sector (excluding illegal strikes at IMP during Feb-Mar 2012)



Source: Company reports, Citi Research estimates

#### See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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## Impact of Strikes

### R9.6bn lost revenue, R7.2bn lost profit

We estimate that illegal strike action has cost the SA gold and platinum sectors R9.6bn in lost revenue and R7.2bn in lost profit. We also estimate that employees have lost R2.4bn in salaries and the Government R2.1bn in tax revenues.

### No end in sight, mass dismissals likely

Our discussions with company CEOs and industry experts (refer: "[Feedback From: SA Labour Crisis – When and How will it End?](#)") suggest that these illegal strikes are unlikely to be resolved any time soon. In fact, it looks increasingly as though companies have exhausted all options and are now resorting to mass dismissals.

An example of this is GFI stating on 16 October 2012 that it has no option but to issue a final ultimatum to 15,000 out of 23,500 striking workers to return to work by 14:00 on 18 October 2012 or face dismissal. AMS also recently dismissed 12,000 workers at its Rustenburg operations.

We fear more dismissals may follow. Whether this will end the current crisis is unclear, as dismissed employees at Rustenburg have continued to protest at AMS's mines.

Figure 2. Impact of strikes to date

	Weeks lost to strikes	Lost production (koz, 4E, Au)	Revenue lost at spot* (Rm)	Profit lost at spot* (Rm)	Tax revenue lost at spot* (Rm)	Current status**
<b>Gold sector</b>						
ANG	3.5	110	1684	1263	379	All SA mines suspended
GFI	6	65	1200	900	270	KDC & Beatrix on strike
HAR	1.5	10	153	115	34	Kusasaletu on strike
<b>Total</b>	<b>11</b>	<b>185</b>	<b>3037</b>	<b>2278</b>	<b>683</b>	
<b>Platinum sector</b>						
AMS	4.5	130	1510	1133	340	Rustenburg, Amandelbult & Union
IMP	6	250	2500	1875	563	Resolved
LON	6	222	2575	1931	579	Operating at ~50% capacity
NHM	0	0	0	0	0	Unaffected
RBP	0	0	0	0	0	Unaffected
AQP	0	0	0	0	0	Unaffected
<b>Total</b>	<b>16.5</b>	<b>602</b>	<b>6585</b>	<b>4939</b>	<b>1482</b>	
<b>Grand total</b>	<b>27.5</b>	<b>787</b>	<b>9622</b>	<b>7217</b>	<b>2165</b>	

Source: Company reports, Citi Research estimates

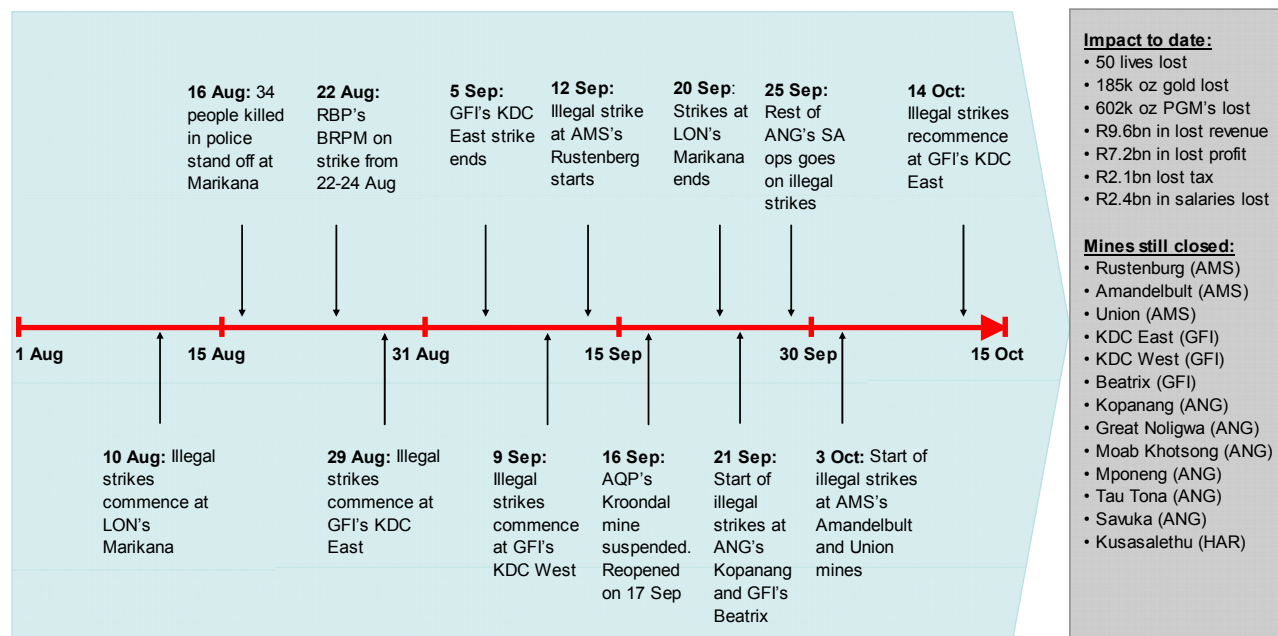
\* Spot prices: Pt \$1,650/oz, Pd \$640/oz, Rh \$1,225/oz, Au \$1,740/oz, 4E basket price R11,616/oz

\*\* 15 October 2012

## Current situation

As at 15 October 2012, we estimate that 71% of SA gold production, and 37% of SA PGM production, is offline due to the effect of illegal strike activities.

Figure 3. Time line and impact of illegal strike action in the SA precious metals sector (excluding illegal strikes at IMP during Feb-Mar 2012)



Source: Company reports, Citi Research estimates

Mines currently on strike in the SA platinum sector include AMS's Rustenburg, Amandelbult and Union operations. Combined, these mines produce 2.4m ounces of PGMs (4E) and 1.4m ounces of platinum p.a. Mines currently on strike in the SA gold sector include GFI's KDC East, West and Beatrix. All of ANG's SA mines are closed due to strikes. Kusaalethu is HAR's only mine affected by strikes. Combined, these mines produce 3.1m ounces (4E).

Figure 4. Mines currently closed / suspended due to strikes

Mines currently closed due to strikes	Annual production rate (koz, 4E, Au)	Lost Production (koz, 4E, Au)	Revenue lost at spot* (Rm)	Profit lost at spot* (Rm)	Tax revenue lost at spot* (Rm)
<b>Platinum</b>					
Rustenburg (AMS)	1,040	67	774	581	174
Amandelbult (AMS)	830	39	454	341	102
Union (AMS)	515	24	282	211	63
<b>Total</b>	<b>2,385</b>	<b>130</b>	<b>1,510</b>	<b>1,133</b>	<b>340</b>
<b>Gold</b>					
KDC East (GFI)	490	22	406	304	91
KDC West (GFI)	612	27	506	380	114
Beatrix (GFI)	348	16	288	216	65
Kopanang (ANG)	307	23	354	266	80
Great Noligwa (ANG)	94	7	108	81	24
Moab Khotso (ANG)	266	20	307	230	69
Mponeng (ANG)	500	38	577	433	130
Tau Tona (ANG)	244	18	281	211	63
Savuka (ANG)	49	4	57	42	13
Kusaalethu (HAR)	180	10	153	115	34
<b>Total</b>	<b>3,090</b>	<b>185</b>	<b>3,037</b>	<b>2,278</b>	<b>683</b>

Source: Company reports, Citi Research estimates, \* Spot prices: Pt \$1,650/oz, Pd \$640/oz, Rh \$1,225/oz, Au \$1,740/oz, 4E basket price R11,616/oz

**37% of SA's PGM production offline**

In addition to mines currently on strike, mines that have resolved strikes (i.e. IMP's Lease and LON's Marikana) are struggling to ramp up production. As a result, we estimate that 37% (3.1m 4E ounces) of the SA platinum sector's annual production is currently offline (*Figure 5*).

This is as 55% of AMS is currently not producing, whilst LON is only operating at 50% capacity and IMP's Lease at 85%, on our estimates.

**Figure 5. SA platinum sector current utilization rate (annualized)**

Capacity utilisation	Normal mining rate (koz, 4E)	Current mining rate (koz, 4E)	Utilisation %	Production offline due to strikes (koz, 4E)
<b>AMS</b>				
Khomanani	180	0	0%	180
Khuseleka	246	0	0%	246
Siphumelele	165	0	0%	165
Thembelani	206	0	0%	206
Batophela	243	194	80%	49
Dishaba	290	0	0%	290
Thumela	540	0	0%	540
Union	515	0	0%	515
Mogalakwena	676	676	100%	0
Modikwa	312	312	100%	0
Mototolo	446	446	100%	0
Kroondal	235	235	100%	0
AMS total	4054	1863	45%	2191
<b>IMP</b>				
Impala Lease	1583	1346	85%	238
Marula	117	117	100%	0
Two Rivers	242	242	100%	0
Zimplats	313	313	100%	0
Mimosa	273	273	100%	0
IMP total	2528	2291	91%	238
<b>LON</b>				
Marikana	1250	625	50%	625
LON total	1250	625	50%	625
<b>NHM</b>				
Zondereinde	300	300	100%	0
NHM total	300	300	100%	0
<b>RBP</b>				
Boschkoppie	280	280	100%	0
RBP total	280	280	100%	0
<b>SA platinum sector total</b>	<b>8412</b>	<b>5359</b>	<b>63%</b>	<b>3054</b>

Source: Company reports, Citi Research estimates

**71% of gold production offline**

Similarly, we estimate that 71% (3.1m ounces) of SA's annual gold production is currently offline due to illegal strikes (*Figure 6*).

**Figure 6. SA gold sector current utilization rate (annualized)**

Capacity utilisation	Normal mining rate (koz)	Current mining rate (koz)	Utilisation %	Production offline due to strikes (koz)
<b>ANG</b>				
Kopanang	307	0	0%	307
Great Noligwa	94	0	0%	94
Moab Khotsong	266	0	0%	266
Mponeng	500	0	0%	500
Tau Tona	244	0	0%	244
Savuka	49	0	0%	49
ANG SA total	1,460	0	0%	1,460
<b>GFI</b>				
KDC East	490	0	0%	490
KDC West	612	0	0%	612
Beatrix	348	0	0%	348
South Deep	273	273	100%	0
GFI SA total	1,723	273	16%	1,450
<b>HAR</b>				
Kusasaletu	180	0	0%	180
Other HAR SA assets	1,000	1000	100%	0
HAR SA total	1,180	1,000	85%	180
<b>SA gold sector total</b>	<b>4,363</b>	<b>1,273</b>	<b>29%</b>	<b>3,090</b>

Source: Company reports, Citi Research estimates

# Valuation and Risks

## Valuation

**IMP our favoured pick in platinum sector, AMS least**

We maintain our preference for IMP (Buy) within the SA platinum sector. As highlighted before (refer: "[Steering the Ship through Stormy Waters](#)", "[Tiring Balance Sheets](#)" and "[Hospital Pass](#)"), IMP's low-cost asset allows it to spend capex to access high-yielding Merensky ounces, while most of its peers have to cut capex to protect balance sheets. It is also the main beneficiary of current industry restructuring (e.g. that of AQP, AMS and LON) as it has the benefit of both sustaining its production profile while profiting from higher PGM prices. AMS (Sell) is our least favored stock.

**Remain bearish on SA golds, with ANG most favored, HAR least**

We remain bearish on the SA gold sector. Even though a resolution to the strikes in SA may result in a near-term rally in these equities (given the 10% rally in the rand gold price of late), we recommend selling into any rally. This is as we maintain that the market's input assumptions in valuing these stocks are too favourable as they reflects a trend of rising production, stabilising costs and falling capex. These assumptions are normally based on company guidance. However, they go against strong trends of falling production, and spiraling costs and capex. We therefore caution downside risk to production, cost and capex guidance from both existing operations and new projects. ANG (Neutral) remains our favoured pick in the sector as we believe it has less execution risk relative to its peers. This is due to its higher-quality assets, generally more conservative guidance, and a more advanced stage project pipeline. HAR (Sell) is our least favored stock.

Figure 7. CitiE global mining valuation comparatives sheet (calendarised)

	TP Curr.	RIC code	Rating	Current price	TP	CY12e DY (%)	ETR* (%)	Current P/DCF	P/E			EV/EBITDA			FCF yield (%)	
									2011	2012e	2013e	2011	2012e	2013e	2011	2012e
Aquarius	GBP	AQP.L	Buy	0.38	0.59	0.0	55.3	0.6	16.3	-12.2	12.2	3.1	11.1	4.9	-12.2	6.2
Barrick gold	USD	ABX.N	Buy	39.82	56.00	1.9	42.5	1.1	8.5	9.2	7.7	5.9	6.7	5.5	0.9	-4.1
Northam	ZAR	NHMJ.J	Buy	30.46	38.00	0.3	25.1	0.8	29.8	26.8	15.6	16.3	13.7	8.5	-7.7	-13.6
Impala Platinum	ZAR	IMPJ.J	Buy	151.65	185.00	1.7	23.7	0.7	14.1	18.5	16.0	6.8	8.9	7.8	-0.2	0.8
Anglo American	GBP	AAL.L	Neutral	18.09	21.00	2.8	18.9	0.5	6.0	13.2	10.2	3.5	5.5	4.3	9.3	1.2
BHP Billiton	GBP	BLT.L	Buy	19.49	22.00	3.7	16.6	0.8	8.6	11.2	11.3	5.1	6.1	6.1	8.1	3.2
Exxaro	ZAR	EXXJ.J	Neutral	167.00	180.00	5.4	13.2	0.8	6.9	8.3	8.8	9.9	12.0	14.4	12.3	0.0
Randgold	GBP	RRS.L	Neutral	77.05	85.80	0.9	12.3	1.5	30.5	21.8	16.4	19.0	13.8	10.1	1.0	0.2
Lonmin	GBP	LMI.L	Neutral	4.91	5.47	0.1	11.5	0.8	10.5	3532.2	28.6	2.5	6.1	4.7	-12.9	-11.3
Rio Tinto	GBP	RIO.L	Neutral	30.61	33.00	3.6	11.4	0.6	5.9	10.0	8.0	2.9	4.6	3.7	9.6	-4.9
RBPlat	ZAR	RBPJ.J	Neutral	48.50	53.00	0.0	9.3	1.1	24.1	42.3	25.5	8.9	13.5	10.4	-1.5	-4.1
African Rainbow	ZAR	ARIJ.J	Neutral	170.26	180.00	3.2	8.9	0.8	8.9	12.2	14.2	3.8	5.0	5.4	1.7	1.3
Anglo Platinum	ZAR	AMSJ.J	Sell	401.50	420.00	0.0	4.6	1.1	24.5	93.1	38.1	7.0	18.3	12.4	4.8	-0.2
Newmont	USD	NEM.N	Neutral	55.88	57.00	2.6	4.6	1.3	13.0	14.0	11.9	10.1	7.2	6.7	2.8	1.0
AngloGold Ashanti	ZAR	ANGJ.J	Neutral	304.50	300.00	1.6	0.1	1.8	10.4	10.4	9.8	5.1	5.1	4.5	9.8	5.2
Newcrest	AUD	NCM.AX	Neutral	27.62	26.00	1.5	-4.4	1.2	18.5	19.2	14.6	10.5	10.0	7.8	-3.1	-2.7
Gold fields	ZAR	GFIJ.J	Sell	107.76	93.00	3.1	-10.6	1.9	8.9	9.5	9.3	3.7	4.2	3.8	8.6	8.7
Harmony	ZAR	HARJ.J	Sell	70.30	57.00	1.2	-17.7	2.0	15.6	13.4	15.8	8.1	5.7	5.0	0.6	5.9
Kumba Iron Ore	ZAR	KIOJ.J	Sell	504.85	350.00	7.4	-23.3	1.1	7.9	11.7	10.6	4.2	6.0	5.8	13.6	9.7
Assore	ZAR	ASRJ.J	Sell	332.00	240.00	2.1	-25.6	1.3	8.9	11.0	14.2	6.3	8.1	10.3	5.5	6.7

Source: Powered by dataCentral      Priced as at 17/10/2012

## Risks

Upside/downside risks to our view include weaker/stronger operating currencies (ZAR, AUD), a higher/lower gold and PGM price, and a better/worse-than-expected operating performance.

## Input price assumptions

Figure 8. Citi input price assumptions

December year end	FY09	FY10	FY11	FY12e	FY13e	FY14e	FY15e	FY16e	LT real	LT Nominal
<b>US\$/oz</b>										
Platinum price	1,173	1,610	1,722	1,534	1,565	1,650	1,700	1,750	1,500	1,722
Palladium price	246	525	734	660	700	800	850	775	600	689
Rhodium price	1,444	2,678	2,000	1,336	1,250	1,350	1,500	1,800	2,250	2,582
Gold price	960	1,226	1,585	1,645	1,695	1,655	1,540	1,350	1,050	1,205
3PGE+Au basket price	907	1,348	1,441	1,409	1,483	1,513	1,526	1,494	1,295	1,486
ZAR/USD exchange rate	8.37	7.33	7.23	8.27	8.81	8.92	9.27	9.64	10.00	10.00
<b>R/oz</b>										
Platinum price	9,812	11,808	12,450	12,686	13,788	14,718	15,759	16,870	15,000	17,220
Palladium price	2,054	3,851	5,307	5,458	6,167	7,136	7,880	7,471	6,000	6,890
Rhodium price	12,077	19,633	14,460	11,049	11,013	12,042	13,905	17,352	22,500	25,820
Gold price	8,028	8,993	11,460	13,604	14,933	14,763	14,276	13,014	10,500	12,050
3PGE+Au basket price	7,589	9,884	10,418	10,431	11,342	12,257	13,221	13,968	12,690	14,568

Source: I-net, Bloomberg, Citi Research estimates



## Appendix A-1

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