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ZCCM-IH CONVERSION OF DIVIDEND AND EQUITY STAKE INTO ROYALTY

ZCCM-IH has entered into a transaction with FQM where it will convert its dividend rights and 20 percent equity value in Kansanshi Mining Plc (KMP) into a life of mine royalty. The key features of the transaction are as follows:

1. The royalty rate will be pegged at 3.1 percent of the gross value of royalty products (e.g., copper, gold, and all other metal products) to be mined from KMP pursuant to the royalty agreement to be executed on the transaction closing date.
2. The payment will be made quarterly
3. Post-transaction, the economic value of ZCCM-IH's 20 percent equity stake in KMP will be realized through the VAT refunds
4. At closing, ZCCM-IH will de-recognize its equity stake in KMP as an investment in associate and recognize the acquired royalty as a financial asset.
5. The varied rights attached to the ZCCM-IH Class A shares in KMP will be amended and prescribed in the amended KMP Articles of Association (“New KMP Articles”) to be adopted at Closing.
6. ZCCM-IH Class A shares will entitle the Company to nominate 2 Directors to the KMP Board each with voting rights.

This move will ensure the stability of revenue inflow into ZCCM-IH coffers. This is because the royalty will be based on the gross value of production as opposed to dividends which are centered on profit. Rationally, the production value is less volatile than the profit value because of the cost element in the latter and the fluidity of the dividend policy framework that is at play. The royalty will be less susceptible to transfer mispricing because it will be based on gross earnings. Secondly, royalty will be incurred on all extracted products, mainly gold and copper. Considering copper prices are currently high and looking at the fact that gold is a high price mineral, ZCCM-IH is expected to financially gain from their gross value through the payment of a 3.1 percent royalty.

Although the rationale of this transaction is clear, it is still mind-boggling to a common Zambian. Firstly, the terms of the transaction speak to the conversion of *dividend rights* and *equity stake* into a life of mine royalty. The former undertaking is progressive. However, *point four (4)* under the key features of the transaction (*i.e., as expressed in this article*) points to

the fact that ZCCM-IH will also de-recognise its equity stake in KMP as an *investment in associate* and will recognise the acquired royalty as a *financial asset*. An *investment in associate* simply means an investment in an entity in which the investor has significant influence but does not have full control like a parent and subsidiary relation. This occurs when a party owns 20 – 50% of shares. By extension of this definition, it means ZCCM-IH will relinquish its significant influence and partial control in the asset at the price of a 3.1 percent life of mine royalty. This being so, it is not clear why ZCCM-IH has gone this route. An *investment in associate* equity stake by ZCCM-IH ensures a certain level of government involvement in the running of mining enterprises. With this new undertaking, we are afraid that we will see a mining sector where all the critical large-scale mines are run by multinational enterprises with maximum influence. This is contrary to the 2023 national budget where government intends to increase its golden shares in the sector. The least expectation was for ZCCM-IH to convert its dividend rights and not necessarily its equity stake in the Mine into a royalty. The call over these years has been to transform the ZCCM-IH docile equity participation in these ventures into an active one and not necessarily to relinquish or covert them for a certain price.

The economic value of ZCCM-IH's 20 percent equity stake in KMP will be realized through the VAT refunds. In other words, post-transaction, the KMP burden of paying ZCCM-IH will be converted to a VAT refund when received by ZRA. It is still not clear why ZCCM-IH agreed to this mode of financing the 20% equity stake. What is expected in this regard is for the 20 percent stake to be raised through other financing methods. This is because this will further generate intricacies in the disbursement process. A critical question that needs to be answered in this transaction is whether late payment of VAT refunds to KMP by ZRA will delay the raising of the economic value of the 20% equity stake.

Mineral resources are the strategic assets that we have for our country. Therefore, they must be exploited for the benefit of the citizenry to steer socio-economic development. This transaction offers some leverage to extract maximal benefits through the conversion of the dividend rights and equity stake into a life of mine royalty on extracted mineral products at KMP. However, CTPD is concerned with the continued reduction of ZCCM-IH control or influence in critical large-scale mines. A certain level of involvement improves the governance process of these assets. Therefore, some active equity interest must be retained. If this transaction is finally completed, it should serve as a litmus test for further undertakings in other assets.

Issued by:

Webby Banda (Mr.)

Research Associate

Centre for Trade Policy and Development (CTPD)

Editor's Note

Contact: Mwaka Nyimbili
Centre for Trade Policy and Development
Phone: +260 211 264409 | +260975876038
Fax: +260 211266234
Plot 3823, Manda Hill Road, Olympia Park
www.ctpd.org.zm

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For more information you can Email: info@ctpd.org.zm. or Visit our web site [www.ctpd.org.zm] You can also follow our TWITTER Account -@CTPDZambia

Address: office Plot 3823, Manda Hill Road, Olympia Park ,