



Is a Tax Controversy the Last Straw for Investors in First Quantum Minerals Ltd. and Barrick Gold Corp.?

Description

It has been a rough start to the year on the TSX with a collapse in energy, and retail investors have been searching for other alternatives. It appears the pool of potential returns will continue to shrink as new woes in the mining industry are crippling two of the country's top producers.

The issue isn't even here at home in Canada, but across the ocean in Zambia, which has imposed a new aggressive tax structure on mining companies. On first glance, many people will not see the significance of Zambia in the overall mining picture, but the country is the eighth largest producer of copper in the world.

The country is also a major source of income for **Barrick Gold Corp.** ([TSX:ABX](#))(NYSE:ABX) and **First Quantum Minerals** ([TSX:FM](#)), which generated almost a third of its 2013 revenues from Zambia. In turn, Zambia took in \$83 million in taxes from First Quantum, a tax bill that could almost triple in 2015.

The rationale for the Zambian government's new tax regime is the falling price and demand for copper. The conductive metal makes up 70% of the country's export earnings and its fall has led to rampant inflation, an 18% drop in currency value, and a budget deficit equal to 5.5% of GDP.

The only people who seem to be in favor of this new tax structure are the government of Zambia (which has just been re-elected over the weekend). Several unions, corporations, and even the IMF have come out in opposition to the rate hikes.

Mining companies fighting back

In retaliation for the tax hikes, both Barrick Gold and First Quantum have threatened to either slow or completely shut down production in the country. Barrick is already gearing up to begin laying off the 4,000 workers at its Lumwana copper mine in March, and plans to cease the mine's operations by June 2015.

This shutdown would complete a dark chapter for Barrick Gold as it originally acquired the mine in

2011 from Equinox Minerals. The acquisition cost Barrick \$7.3 billion and little to no returns have been seen. In the long run, the deal may be one of Barrick Gold's biggest failures.

Barrick now has to hope that the \$7 billion it has spent recently in Panama and Argentina can compensate for its shutdown in Zambia without bankrupting the company.

Over at First Quantum Minerals, plans were already in place to delay over US\$1 billion in capital investments in Zambia, thanks to the \$600 million in value-added tax repayments being withheld by the government. With the higher taxes now in effect, First Quantum is in a more precarious position than Barrick Gold because of how much Zambian copper adds to its revenues.

There is also the fact that First Quantum just opened a new \$850 million smelter in Zambia in December, which can process 300,000 to 350,000 metric tons of copper a year. If First Quantum were to take the same hard line as Barrick, it could lose out on this new smelting capacity and the 270,000 to 300,000 tons of copper metal concentrate it produces from its Sentinel Mine.

A price to be paid

For Zambia, this tax plan could end up costing the country 12,000 jobs in 2015, and 30% of its GDP. For investors in these companies, this is just another sour note with little hope for a short-term turnaround. Both First Quantum and Barrick Gold are trading near the low end of their 52-week ranges, with First Quantum closing Friday at \$12.67 and Barrick Gold closing Friday at \$15.43.

Average price targets on both companies offer little comfort as well. The average price target on First Quantum is \$19.40, with the most recent reports setting prices of \$16.30 and \$18.75; this is a far cry from the company's 52-week high of \$27.29. Things are about the same for Barrick Gold with the average price target set at \$14.90, compared to a 52-week high of \$23.78.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

1. NYSE:B (Barrick Mining)
2. TSX:ABX (Barrick Mining)
3. TSX:FM (First Quantum Minerals Ltd.)

Category

1. Investing
2. Metals and Mining Stocks

Date

2025/08/25

Date Created

2015/01/26

Author

cameronconway

default watermark