Greece – Armageddon or New Dawn

With the global financial markets watching tentatively to see if Greece finally goes over a metaphorical "Niagara in the barrel" I must confess to feeling a certain calm. As I have noted before I have been there done that when Argentina (a much larger economy) went into a spiraling devaluation (and corresponding inflation) in 2001. However none of this is particularly novel, just novel in recent years. In 1997 we had the simultaneous Asian and Russian crises. In 1994 we had the Tequila meltdown in 1994 which washed across the Latin markets.

Greece as an "Emerging" Market

One of the problems in recent years when Greece is that so many have been mistakenly talking of it as a "developed country". Just becoming a member of the Euro mechanism does not make one developed. If asking the question "what does Greece make?" brings back the response "olive oil" then you have there your answer. A small mono-culture nation with no great service industry (beyond tourism and ship-owning) combined with a reticence to develop mining and a rather arid climate, sounds like a developing country rather than a developed one. Greece anywhere else would be developing. Geography does not dictate how developed a country is…

Curing what Ails It

Starting with the premise that Greece is really a pseudo-developing country makes the economic doctor's task in prescribing medicine all the easier. There is one cure for every illness that looks like Greece's and it's called devaluation. Frankly if Greece had not been in the Euro mechanism, it would have taken its lumps back in 2008 and be in the pink of economic health now.

Then how might this play out? The difficult thing is the “denial”. Denial results in a Greek central bank not having a vault overflowing with freshly minted drachma notes to start distributing on Devaluation Day +1. Somehow it will muddle through, bank notes can be flown in en masse. The populace will also start bringing back their flight capital to take advantage of the bargains on offer (Greeks are still Greeks after all!). It also helps that this all happens at the start of the summer tourist season when the country receives a surge of tourists loaded to the gills with their own currencies and disposed to spend them. That whole part of the Greek service sector will be able to operate in a multi-currency manner. Banks will probably have an extended holiday and may even be nationalized.

The mechanism for changing from one currency to another overnight is not that complex and not really unknown territory. Brazil shifted from Cruzeiros to Reais in the 1990s after having previously had Cruzados.. Argentina shifted from Pesos to Australes in the 1980s then back to Pesos in the 1990s.

It is worth recalling also that Greece has spent more than half the time since its independence in the 1820s in a state of default so whatever might shortly happen is a case of “been there done that”.

The Implications for Mining

To the surprise of many, Greece is Europe’s largest producer of bauxite, however to put that in perspective, the USGS report on Greece in 2012 put its share of global bauxite production at 1%. In the same report it was noted that Greece was the world’s second ranked producer of perlite after the United States and the world’s sixth ranked producer of pumice.

It also was estimated to have produced about 9% of the world's bentonite.

The bauxite producers were Delphi-Distomon S.A., Hellenic Mining Enterprises S.A., and S&B Industrial Minerals S.A. (S&B). All Greece's major bauxite deposits are located in central Greece within the Parnassos-Ghiona geotectonic zone and on Evvoia Island. The leading bauxite producer was S&B, which had an output capacity of two million tpa exclusively from underground sites located in the areas of Amfissa and Distomon.

However, one percent of the global bauxite market does not really move the dial. Devaluation though would make the country's production cheaper and maybe drive volumes higher.

When looking at gold it is interesting to go back to a Bloomberg article on the wave to come that said: "Gold mining is gathering momentum after Greece began what it called a "fast-track" approvals program. The Canadian and Australian companies said their projects will add about 425,000 ounces by 2016, worth $757 million at the Oct. 5 spot price, to the 16,000 ounces the country produced in 2011". However an ominous sign was that the article began with a photo of TVX Gold's abandoned its Olympias mine with the caption that TVX: "..repeatedly clashed with local government officials and courts and eventually abandoned Greece in 2003 after its permits for Olympias were declared illegal and annulled". That should have been a warning in itself. Curiously TVX Gold had been controlled by the fallen Brazilian billionaire, Eike Batista, whose travails in Colombia we wrote about recently.

In a way that history turns out to be rather circular, the Olympias asset ended up in European Goldfields and then Eldorado Gold (NYSE:EGO) took that over for $2.4bn only to now find.

Glory Resources Ltd. of Australia announced in 2012 that it had identified mineral resources at its Sapes gold project with a Joint Ore Reserves Committee (JORC) estimate of measured and indicated resources of 2.6 million metric tons (Mt) grading 9.8 grams per metric ton (g/t) gold. Then in October 2013, Eldorado moved on Glory also and took it over.

This means that Eldorado Gold theoretically has four projects on the go in Greece but the emphasis is on theoretically as opposition to mining has been fierce from vested interests. It is surely a symptom of the "Greek disease" that the country was so comfortable on the EU's handouts that it thought it had the luxury of rejecting some of the most carefully thought out environmentally sound mining projects on the planet on a mere whim.

Curiously, looking at Eldorado's portfolio of Greek properties it does not list the underground silver-lead-zinc Stratoni Mine located on the Chalkidiki Peninsula. Back in 2012 this was operating at a mining rate of about 18,000 metric tons per month of ore and produced lead, silver, and zinc concentrates. The Stratoni mineralization was classified as lead-silver-zinc carbonate replacement type mineralization, with galena, pyrite, and sphalerite as the main ore minerals. Resources at the Stratoni Mine were contained within the Mavres Petres ore body and had estimated proven and possible reserves of 1.8 Mt grading 8.5% zinc, 6.3% lead, and 177 g/t silver. The mine produced a lead-silver concentrate and a zinc concentrate by a conventional underground drift-and-fill method. The concentrates were shipped by sea to European facilities using either the Stratoni or the Thessaloniki port facilities. Clearly the overvalued Euro and high costs in Greece put paid to this operation which certainly looks sexy to us with its Lead-Zinc component.

Then looking at the gold projects the surprising thing is that Olympias (despite TVX having spent $250mn on developing the mine) is in a holding pattern and Eldorado's focus is on Skouries. This is a high-grade gold-copper porphyry deposit also located in the Chalkidiki Peninsula in northern Greece.

The mine will operate in two phases. The initial phase consists of a small, open pit, with production expected in 2016. In the following phase, production will come from the underground. The project benefits from a simple metallurgical process and will produce a clean copper-gold concentrate via flotation as well as doré from a gravity circuit. The project was moving along nicely until March of this year when <<sigh>> the government revoked a permit required for the Skouries processing plant.

These travails are one of the reasons that Eldorado’s share price has been one of the least responsive to upward stimuli in the market in 2015.

The problems at Skouries can be linked back to erratic action from the new Left-wing Environment Minister. If devaluation and default come to pass then Syriza might also blow up or the government might see the light on the need to hunt under every stone for new sources of export earnings and economic growth. Not everyone can be an olive picker or a waiter.

Conclusion

My basic premise is that Greece falling out of the Euro zone will not be a disaster but a blessed relief for all concerned. Sure there will be ructions but better to get it over with. If previous experience in Argentina is anything to go by the Greek equities market will become a massive buying opposition on Devaluation Day +1… (excepting banks, which will be ravaged). Everything else will have a giddy surge. Other markets around Europe and globally will heave a sigh of relief and also rally.

The intriguing thing will be to see how fast drachmas start to circulate again… indeed, if they appear immediately then it will be a sign that the government always knew this was going to happen and had made a big stash of notes for the eventuality. After all how can Greece devalue against the Euro if it has nothing to devalue with?

On the mining front, well might we ask whether Greece will see the light on its less than warm reception offered to foreign miners. The amount that Greece will owe to creditor banks (particularly the ECB, IMF etc) will mean it will need to become an export generator (or at least a foreign currency earner) fast and with an "all hands to the pump" attitude, gold mining will seem like easy pickings. However the Greeks have shown in recent times that practicality is not one of their strong suits.