

# Argentina Unshackled

Observers from outside Argentina have gone on a frenzied romp of self-congratulation hailing the change in the Argentine Presidency in last week's elections as something akin to a Revolution. Once again though we find that simplistic formulas are being used and the nuances of what has happened being ignored. The situation still has the potential to be a wild ride for investors.



For a start the victory of Mauricio Macri is being hailed as a “right-wing” victory. To put that in context, firstly he leads a Rainbow Coalition that stretches from the Left across to the Right and the party he beat, the Frente Para la Victoria, is in fact the old Peronist Party, which was a fascist/corporatist construct in its original roots. So to claim that a wealthy businessman (in fact I would venture one of the five wealthiest in the country) that leads a Coalition including the Left is a “Right-wing” victory is stretching it a bit.

Secondly we would note that the victory was surprisingly narrow. While the first votes in showed a 9% lead for Macri, as the night wore on the margin slipped and it ended up being 51.4% for Macri and 48.6% for his Kirchnerite opponent, Daniel Scioli. It should also be noted that the first round of elections last month delivered stinging losses to the Kirchnerites but they just barely hung onto control of the Senate meaning that, if they stay cohesive, they still have potential to block reforms. That said, with their patroness gone, the rats tend to disperse into the woodwork to regroup. We may end up seeing the phenomenon apparent under the De La Rúa government in the late 1990s of Bribes for Votes when a hostile majority in the Senate had to be paid off, literally.

## **The New Lay of the Land**

As we have repeated endlessly mining is controlled in Argentina by the provinces, in much the same way as it is in Canada or Australia. The national government in Argentina has NO approval or denial power over mining projects. So everything you have heard of “Cristina Kirchner blocked our project” is a load of codswallop. In all cases blockages occurred because of ornery provincial governments.

It is interesting therefore to look at the map of the electoral results. The blue areas are provinces that voted for the Kirchnerite candidate. The yellow are those that voted for the winning Macri-led ticket. Oops, for those who know the only province with mining of note (Silver Standard's Pirquitas mine) that voted for Macri was Jujuy. La Rioja has been an on-again, off-again mining favorable area and La Pampa and Mendoza have been graveyards for miners.



The provinces where mining is currently active are Catamarca, Santa Cruz (the Kirchnerite province par excellence now run by the outgoing president's daughter), Salta and San Juan.

If there is anything to be read from this map it is that the marginalized distant provinces with the smallest populations (excepting Buenos Aires which was only won marginally by Scioli and that was because of the sprawling urban slums voting for him) supported the Kirchnerite program which gave them a greater share of the goodies. The provinces that trended for Macri were those with the largest populations (and strong agricultural export economies) that were actively persecuted and discriminated against for the last 12 years.

## **Implications for Mining**

Having said that mine approvals are in provincial hands, some matters are still in the Federal purview. Amongst these that

have relevance are foreign exchange allocations. Miners have been griping for years now that they could not bring in the capex items they wanted in an unrestricted way due to import restrictions and could not remit profits or dividends as and when they wished. These restrictions were part of the increasingly draconian and bizarre forex rules that the Kirchnerite regime was imposing as Argentines tried to head for the exits and buy dollars to protect themselves against the rapidly deflating peso.

Moreover to say the forex regime was complex was an understatement. Here is the table of exchange rates for today for a leading Buenos Aires newspaper, La Nacion:



So on the left we have the official rate, on the far right is the so-called Dolar Blue which is the back-alley rate. In the middle are various official rates administered by the Central Bank for different purposes. Dolar Ahorro is a savings rate, Dolar Tarjeta/Turista is the rate that locals can use credit cards for (when travelling abroad) and that bona fide tourists within the country can use to change money. The Dolar Soja is the very prohibitive rate forced upon farmers selling their crops (effectively a 30% tax on the official rate and a 150% tax on the unofficial rate). Finally the Dolar Bolsa is a conversion rate for transactions in the Stock Exchange.

Byzantine is obviously not too strong a word to describe this bizarre system. Miners will be hoping that this system loosens up, though the new government will be wary of letting this go too soon or there will be a dollar buying spree that will decimate Central Bank reserves. One suspects that Dolar Turista and Dolar Soja will be the first to go. The government will then aim to draw the Dolar Blue and the official rate together somewhere in the middle. Who knows? Maybe the wonderful Convertibility regime of the 1990s might be revived.. Certainly Argentina had never experienced such good

times since the 1920s as under that arrangement.

Despite the mining provinces largely being of the Kirchnerite ilk, they are the provinces that have shown themselves to be most pro-mining. With less subsidies coming from the Federal government more of the provinces will have to look to mining to keep their local economies buoyant.

If one wants to muse with some names in Argentine mining those to consider are:

- Patagonia Gold Plc (AIM: PGD)
- Hochschild Mining (LON: HOC)
- McEwen Mining Inc. (NYSE: MUX | TSX: MUX)
- U308 Corp. (TSX: UWE | OTCQX: UWEFF)
- Pan American Silver Corp. (NASDAQ: PAAS | TSX: PAA)
- Silver Standard Resources Inc. (TSE: SSO)
- Yamana Gold Inc. (TSX: YRI | NYSE: AUJ)
- Argentex Mining Corporation (TSXV: ATX | OTCQB: AGXMF)
- Orocobre Limited (ASX: ORE | TSX: ORL)
- Western Lithium USA Corporation (TSX: WLC | OTCQX: WLCDF)
- Galaxy Resources Limited (ASX: GXY)

One might also see those who have downplayed their Argentine prospects dusting them off or racing back to restake them.

## **What Next**

After exchange rates there are a vast swathes of regulations constraining all aspects of economic life that could be cast into the dustbin of history. Some of these measures being rescinded should help miners. One that might not though is the bizarre fuel subsidies. These were introduced after the collapse of 2000/1 and the spike in inflation. To “protect the poor” massive subsidies were introduced which have bled the Treasury dry. They have been reduced and some have been made to pay world parity prices for oil but many have not. This could be the big budget winner but also a tough policy to bite

on first.

One could see a strong inflow of FDI though and this might actually reverse the exchange rate so delays in freeing remittances might actually work out better for miners when they are eventually freed.

The whole construct of Kirchnerism was so bizarre and distortive that untangling it is akin to unraveling the Gordian Knot. Like Alexander the Great, sometimes it's better to just draw one's sword and chop the knot in one fell swoop than spend years testing one's Boy Scout skills trying to untie it..

## **Conclusion**

After 12 years of Kirchnerite "policies" (more like populist bootstrapping) the Argentine economy is emerging from a long dark tunnel into the glare of daylight. Frankly it's better out of the tunnel rather than being in it and foreign miners for better or worse face a brave new world. We can say with confidence that the rules will NOT be more onerous and the forex regime WILL be more flexible. Growth should kick up and frankly Argentina looks like a better bet than the deeply troubled Brazil these days.

As a New Yorker would say "What's not to like?"

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# **The Tesla Beauty Contest**

☒ Tesla has confirmed that it will proceed with plans to build the battery 'gigafactory', choosing Nevada as the location. Now, it will have to secure the critical raw materials to launch production and keep the plant running.

There has been much focus on the lithium supply requirement, but for the initial period, Tesla does not need to secure a lithium offtake agreement as there are two or three major suppliers in the western United States (such as Western Lithium – TSX: WLC – in Nevada), which have expansion capabilities. Three new lithium mines have also opened in the last couple of years and at least another is ready to proceed subject to financing. However, it is unlikely Tesla could go ahead without a secure source of graphite which is needed to make the anode material in the battery.

Batteries contain some 10 to 12 times more graphite, by weight, than lithium. Losses in the manufacturing process end up consuming 30 to 40 times more graphite than lithium. China produces 70 to 80 per cent of the world's graphite and its industry has serious environmental and resource management challenges. The associated resource nationalism and the preference for selling value added products rather than cheap natural resources suggests that the supply chain could be compromised and unreliable. Tesla's domestic sourcing ambitions are not a secret and the Gigafactory will source such materials as cobalt, graphite and any other critical material it needs in North America in order to establish as tight a supply chain as possible with an aim to keeping low costs and low environmental impact.

Who will win the Tesla graphite beauty contest? There is only one company that can meet Tesla's volume and timeline requirements some contend. It is also located in North America and has the best location/infrastructure and the lowest capital cost of any new graphite project – that company is Northern Graphite (''NGC', TSXV: NGC | OTCQX: NGPHF).

NGC is planning on producing about 44,000 tons of graphite concentrate per year. 90% is battery grade and the yield of anode material (called "spherical graphite" or "SPG") is 50%, both the highest in the industry. This would put its annual SPG production at 20,000 tons and the company has already

defined the resources to expand beyond this. Tesla's initial requirement is 27,500 tons in 2017/2018. Other companies with similar sized projects have 40-70% battery grade material and a yield of 33% or less which make their potential annual SPG production less than 10,000 tons. What will they do with the high percentage of non-battery grade material that must be sold to maximize projects economics?

NGC has completed a bankable Feasibility Study and has also secured its most important environmental permit. The company is ready to start construction next year and reach the production phase before the end of 2016. The competition is well behind in the engineering/permitting process. NGC also has one other huge advantage over its peers...

It is not enough to just be able to produce graphite. It must be purified to 99.95%C for use in lithium ion batteries. The Chinese wet chemical approach, a veritable environmental nightmare, and the thermal method, too expensive and inefficient, are not options. The only company that already has a proven, proprietary purification technology also happens to be NGC. In part, this is due to the pristine nature of its flake graphite which makes it easier to remove impurities. Even if its peers knew the process, it is unlikely it would work on their concentrates due to different mineralogy. Initial testing also indicates that this high quality flake results in greater battery capacity but further testing and validation is required.

We don't know when or what Tesla will decide to do about its graphite supply, but those who would venture a gamble in the graphite beauty contest would clearly have to place NGC at the top of this list.

Of course, there are also questions as to whether the Gigafactory will actually be built; indeed, even Tesla's sales targets of 500,000 EVs by 2017/2018 are rather ambitious. However, few would venture to bet against Elon Musk.

Alternatively, it seems highly probable that the production of EV's from all car companies will exceed 500,000 units per year by 2017, considering that every major manufacturer already has an electric or hybrid vehicle on offer in 2014. This is less than 1% of the annual new car market. Regardless of the outcome, Tesla will need more graphite than lithium and NGC is in the best position to supply it.