



Socialist Tide Won't Wash Apex Away Bolivian Election Not Affecting San Cristobal Development

By Anthony Vaccaro

December 12, 2005

Uyuni, Bolivia -- Driving into Uyuni, an outpost city high in the remote mountains of Bolivia, bright colours jump off of the shabby wall of the city's most peripheral building.

The left side is painted vivid blue and white with the letters MAS -- the acronym for the left-wing political party, Movement Towards Socialism. Clashing with it, on the right side, is the bright red and white representing MAS' opposition, Jorge Quiroga -- or, as the people and the wall call him, "Tuto."

The wall embodies where Bolivia now stands. After a year of protests and barricades that had the government teetering on the brink of collapse, Bolivians are turning to the Dec. 18 elections and the two leading parties -- Tuto on the right, and Evo Morales' MAS on the left -- for a way out of economic and social turmoil.

Denver-based **Apex Silver** (SIL-X) will feel the outcome of the election, too, as the 100% owner of what is likely to become one of Bolivia's largest mines, San Cristobal -- an hour's drive from Uyuni.

While business affairs and politics intertwine in every country, here in South America's poorest country they are inseparable.

With many citizens dissatisfied with 20 years of the neoliberal politics that encouraged privatization and foreign investment without substantively addressing the nation's poverty, Bolivia is the latest South American country to witness a surge of pro-socialist sentiment.

Bolivian socialism is largely rooted in the indigenous population, which is proportionally the largest in South America. Indeed, the front-runner in the election -- MAS' Morales -- could become the continent's first-ever indigenous president. (Peruvian president Alejandro Toledo being of mixed European-indigenous heritage.)

Morales, or simply "Evo," is running on a platform that includes the nationalization of the hydrocarbons industry as a priority -- and some wonder if the mining industry could be a longer-term target.

For its part, Apex says it looks forward to having a dialogue with whoever wins the election and is more focused on pushing ahead with its massive construction efforts at San Cristobal than with guessing how the political landscape in Bolivia may change.

"We've been at San Cristobal for ten years and we've worked with all kinds of leaders," says Apex's vice-president of investor relations and corporate development, Igor Levental. "We're committed to the success of the project and the country, whoever wins the election."

The American government -- while it won't say so officially -- isn't so accommodating. While the U.S. embassy has long been the seat of great influence in Bolivia, it has learned recently to be more circumspect with regard to commenting on elections.

In the previous election, Morales, who was at that time a long-shot to win, inadvertently benefited from comments by then-U.S. ambassador Manuel Rocha that were aimed at scaring voters away. Rocha said the U.S. would reconsider all aid to Bolivia if Morales were elected. In an act of defiance by the voters, Morales subsequently shot up the polls, going from long-shot to legitimate contender.

The U.S. is widely believed to be just as opposed to Morales now as it was then, and its refusal to even meet with him is telling. Evo's support for coca-leaf growing, and his friendships with Cuba's Fidel Castro and Venezuelan president Hugo Chavez, are often cited as Washington's main concerns.

"The U.S. government won't engage him on any level," says Ivan Rebolledo, president of the Bolivian-American Chamber of Commerce, a body that represents foreign business in Bolivia, and has World Bank support. "And we've always questioned that logic."

Rebolledo, whose organization has met with Morales several times, says Morales is becoming more pragmatic as he evolves from his coca-leaf union-leader roots, to politician.

"Morales is moving somewhere toward the centre," Rebolledo says. "His position on foreign direct investment is changing slowly -- not as quickly as we would welcome -- but it is changing."

Rebolledo points to two key factors that bode well for a foreign mining company like Apex.

One is that Bolivian companies and the Bolivian government don't have the capital needed to exploit their own resources and therefore must rely on foreign investment in some capacity. Rebolledo says that while a Morales government would likely change the formula for how much revenue foreign nationals would be required to share, it would not banish them altogether.

The second factor is the long history that mining has in Bolivia and the high standing it enjoys here.

"Evo will stay away from nationalizing the mining sector," Rebolledo says. "He himself is originally a miner and the mining sector has generally been well regarded."

Bolivia has already had a failed experiment with nationalizing the mining industry. >From 1952 until 1985 the country's tin mines were government-run. But when tin prices collapsed in 1985 -- effectively killing the industry -- the

government rethought its policy and pulled out. A new mining code, which is still in effect, was drawn up and foreign investment encouraged.

San Cristobal

While the election results and consequences are outside of Apex's hands, the building of the mine and the massive processing plant are well within its grip.

Once construction is completed in the second half of 2007, Apex is slated to process 40,000 tonnes of ore per day from proven and probable reserves of 219 million tonnes grading 64.69 grams silver per tonne, 1.60% zinc and 0.59% lead, or a contained 456 million oz. silver, 3.5 million tonnes zinc and 1.3 million tonnes lead.

The impressive pace of production is expected to last 16 years, making for annual output of 19.5 million oz. silver, 187,000 tonnes zinc and 63,000 tonnes lead -- numbers big enough to make San Cristobal the world's third largest silver mine and sixth largest zinc mine.

When completed, the on-site processing plant would turn out zinc, silver and lead in three separate sulphide flotation concentrates of: zinc concentrate, lead concentrate and bulk or low-grade lead concentrate. Silver is expected to make up 39% of the lead concentrate, 31% of the zinc concentrate, 6% of the bulk or low-grade lead concentrate.

And while the "Silver" in Apex Silver's name may suggest otherwise, San Cristobal's main source of revenue will actually be zinc. According to one analyst's numbers, at today's zinc, silver and lead prices, 54% of revenue is anticipated to come from zinc, 30% from silver and 16% from lead.

Once processed, the concentrate would be transported by rail some 650 km to the port of Mejillones in Chile, where it would then be shipped in bulk to smelters around the world.

The geology

San Cristobal is actually 15 separate mineralized anomalies, and with a feasibility study completed in 1999, Apex has had ample time interpret the area's geology.

The orebody at San Cristobal is hosted in an irregular, bowl-shaped sedimentary basin, roughly 4 km in diameter. Sediments dip toward the centre of the depression, and the orebody itself is also bowl-shaped, mimicking the volcanic depression.

To date, two-thirds of the basin has been drilled extensively. Apex says there is sufficient drill-hole data for the remaining one-third to infer the shape of the orebody.

Open-pit mining is scheduled to proceed in three stages. In the first five years, two separate pits, one on either side of the Don Jose dome -- an intrusive plug crosscutting the orebody -- will be mined, after which the two will be collapsed into one all-encompassing "ultimate" pit. The strip ratio for the operation is expected to be a low 1.56:1.

Quiet beginnings

When Apex first arrived in the desolate mountain village of San Cristobal -- an Apex geologist made the discovery in 1995 -- the 70 odd villagers living there used the barren landscape to grow potatoes and graze their llamas.

And while llamas still scale the rocky slopes around San Cristobal, cranes, dump trucks and bulldozers now fill the valley below.

Currently, Apex has 1,900 workers on-site; employment will peak at roughly 3,500 workers before construction is completed. The company has put 4.2 million man-hours into construction since July 2004.

Work taking place in the valley includes the re-bar and concrete forming of what will be the primary crusher, and blasting into the mountainside for a 1.2-km conveyer belt that will carry ore to the semi-autogenous grinding (SAG) mill, two ball mills and flotation tanks -- all also under construction.

In all, the company will sink US\$650 million into the project -- a substantial infusion into the Bolivian economy. The company says the mine will account for 40% of Bolivia's mineral exports and will bring in an additional US\$100 million in indirect investments.

To help fund the mine, Apex is closing a deal for US\$225 million in bank financing. While the bank loan did require the company to hedge some of its future production, with 3.5% of silver production, 12.6% of zinc production and 14.7% lead production hedged, the hedge book is not burdensome.

In a press release, Mark Lettes, the company's senior vice-president and chief financial officer, said Apex had two objectives in securing financing: first, to hedge the minimum amount of metal necessary to secure bank financing, and second, to expose shareholders to the benefits of rising silver prices.

Lettes said both objectives have been met as Apex is sufficiently exposed to potentially escalating prices of zinc, lead and especially silver.

Such a huge investment in capital when combined with Apex's strong efforts on the sustainable development side -- the company has invested US\$10 million in local communities thus far -- serves as insurance against possible nationalizing tendencies in the capital. But such spending is not without a potential downside: As local workers see more money being put into the project, their demands on the company can become more onerous.

In the last month, workers have protested at the site twice -- no small matter considering protesters in Bolivia are as likely to hoist sticks of dynamite as picket signs. The most recent march took place on Nov. 30, when workers claimed that too many foreign workers were being hired at the site (Bolivian law dictates a certain proportion of Bolivians must be hired).

Apex's Levental describes the recent labour dispute as a "storm in a teacup." He says worker ire was directed at a sub-contractor hired by Apex and that the company resolved the matter in a day, without assistance from government officials. Apex says its workforce is currently 95% Bolivian.

Still, Bolivia's recent history has been dominated by the awakening of indigenous pride -- making protests and barricades an almost automatic tactic for voicing dissent.

The popularity of Morales' candidacy is in many ways tied to such sentiment.

And while even a victory at the polls does not guarantee that Morales will become president -- in Bolivia, the president is chosen after behind-closed-door alliances are formed on the basis of election results -- the populist voice he represents will be a factor in any new government.

While Apex and its investors will have a clearer picture of how the political landscape will or will not affect the mine after the election, management at San Cristobal isn't choosing sides. Instead it's just hoping for renewed stability in the country -- regardless of which political party brings it.