Exploration and Mining Activity in Central America

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INTRODUCTION

Central America is currently enjoying a surge of exploration activity and mineral investment. Interest in precious metal prospects is high and base metals are once again attracting attention.

Some attribute this surge to the falling rate of discovery and increasing regulatory burden in North America. Although these factors certainly play a role, it is important to also recognize numerous improvements in the political and business climate of Central America.

MINING LAW

Mineral development in the area has only recently been governed by legislation. Nicaragua adopted a mining law in 1965, Honduras in 1970, Panama in 1979, Costa Rica in 1982, and Guatemala in 1985.

Current mining codes, although often patterned after a U.S. model, typically treat mineral resources as state property. The lease held by any concession holder, foreign or domestic, is always subject to review and approval by the government. Some countries created a state-owned mining company which has the option to participate in new mines as a joint venture partner, thereby insuring participation by the government in development of its mineral resources.

The general failure of this approach to attract foreign investment is now widely recognized by governments as well as by mining companies. Panama is the first Central American nation to adopt significant revisions to its mining code (January, 1988). These revisions include reduction of a 9 percent gross production royalty to 2 percent, and declaration of a 6 year staged income tax break for new mining ventures. Mining firms active in Costa Rica welcomed the 1988 reduction of a 6 percent export tax to 1 percent and reduction of maximum corporate income tax from 50 percent to 30 percent. The state-owned mining companies of both countries will probably be dissolved. Nicaragua announced plans in 1992 to privatize its mining industry. Overall, changes in mining law in Central America and the Caribbean are increasingly favorable to mineral investment and development.

DISCOVERY RATE

An important and difficult-to-quantify figure in mineral exploration is the odds in favor of discovery. First world countries, where mineral exploration is mature, are currently suffering from a falling return on the average invested exploration dollar. Comparisons such as those by the Mineral Investment Group of Colorado show that a mineral discovery is two to three times more likely in third world countries.

COMPETITOR ACTIVITY

The historic lack of competition for property in Central America is changing. Roughly half of the existing concessions in Panama nave been granted during the past two years. Minnova opened an office in Panama City in 1991; Phelps Dodge, Rayrock and Placer Dome opened offices in San Jose in 1989, 1991 and 1992, respectively. Battle Mountain, Noranda, Phelps Dodge, Independence (Minorco), Cyprus, Newmont, Gold Fields and Boliden have been participants in recent joint ventures in Panama or Costa Rica. Fischer-Watt has been active in Honduras (in joint venture with Kennecott) as have Cominco and Melinga Resources. Greenstone and Boliden are active in Nicaragua.

The discussion which follows describes highlights of the mining law for each country in order to provide a framework in which geologic opportunities can be evaluated. There is also discussion of the political climate and a few comments on competitor activity.

PANAMA

MINING LAW

Panama is currently the most favorable place to develop new gold deposits in Central America. This statement is based on the following observations:

1) Holders of exploration concessions are guaranteed the right to put a discovery into production. The transition from exploration phase to exploitation phase is often a stumbling block to mineral development elsewhere in Latin America.

2) Panama has a dollar-based economy and no restrictions on currency transfer into or out of the country. The government receives a 2 percent gross production royalty and there are no import or export taxes.

3) A staggered income tax discount is in effect. Mines brought into production prior to 1998 will receive a 30 percent life-of-mine income tax discount (on the current 50 percent maximum corporate rate). Depletion allowances are applied annually and accelerated methods of depreciation are permitted for physical assets.

4) Officials responsible for overseeing mineral development favor mining.

I would choose to work in Panama, rather than Costa Rica, Honduras or the rest of Central America, given prospects that are equally attractive in terms of their geologic characteristics.

POLITICAL CLIMATE

Panama's status as favorable country to invest in has improved since General Manuel Noreiga was removed by U.S. armed forces in December, 1989. Guillermo Endara, who won Panama's popular election, is now in office.

The agency responsible for environmental protection in Panama is INRENARE (Instituto Nacional de Recursos Naturales Renovables). New mining projects are evaluated jointly by INRENARE and the DGRM (Direccion General de Recursos Minerales, part of the Ministry of Commerce and Industry).

The issue of indian versus hispanic authority in Panama is a long-standing one. Guaymi indians make up over 90 percent of the local population in much of the Chiriqui and Boca del Toro Provinces of western Panama and the Comarca San Blas of northeastern Panama has a legally recognized indian administration.

Indian authorities in Panama are not against mining. They seem willing to accept concessions if benefits also accrue to the indian population. Cerro Colorado, the largest mineral project in Panama, is on land inhabited by the Guaymi indians. Panama's office of indian affairs is responsible for resolving disputes involving mineral development on indian land.

COMPETITOR ACTIVITY

Codemin, the state-owned mining company, is largely inactive and has been for several years. It will probably be disbanded once it sells its interest in the Cerro Colorado porphyry copper project. Other companies holding active concessions in Panama include, Noranda, Cyprus, Minnova, Greenstone and Boliden. Local exploration and consulting groups include Consultores Geologicas, Transworld and IXTAPA.

The major mining project in Panama for the past several years has been the Santa Rosa hot spring gold deposit. Minas de Santa Rosa, a joint venture of Boliden International Mining (51 percent) and Greenstone Resources(49 percent), has announced a mineable reserve of 7 million tonnes of 0.051 opt gold.

The only gold mine currently operating in Panama is the Remance deposit, an underground mine which commenced operations in October, 1989. Minas de Remance is owned by a Pachapaqui, a Peruvian company, and processes 140 tons per day.

Minnova is the only major company to open an office in Panama (early 1991) other than Freeport, which explored in Panama from 1985 to 1990. Minnova and joint venture partner, Adrian Resources, are drilling at the Cerro Petaquilla porphyry in northern Panama. Cyprus is in its second year of drilling at Cerro Quema, on the Azuero Peninsula.

There has been increasing interest in porphyry copper and gold targets, which are abundant in Panama. Porphyry concessions granted in 1991 include Rio Pito (Greenstone) and Petaquilla (Minnova). Other porphyry targets include Cana, a former gold producer drilled for copper in the 1970's, and Cerro Colorado, which is surrounded by numerous stream sediment gold anomalies.

COSTA RICA

MINING LAW

Costa Rica's 1982 mining law provides for a 2 percent gross production royalty plus a 1 percent export tax on gold not sold to the Central Bank. Proceeds from the sale of bullion must be converted back to local currency (colones). Procedures exist for repatriation of profits, after payment of a 15 percent withholding tax, but, dollars are not always available. Yearly inflation rates during the past five years average 25 percent. The maximum corporate tax rate is 30 percent. The mining law of Costa Rica also specifies benefits such as a tax holiday and exemption from import taxes.

Currently, there is a state-owned mining company, Minasa, which holds concessions and participates in joint ventures. According to the mining law, Minasa is entitled to a 33 percent participating interest in any mine in Costa Rica. This option has never been exercised and, according to a former minister of mines, is not meant to apply on other than Minasa concessions.

POLITICAL CLIMATE

There is an entrenched opposition to mining in the National Liberation Party, one of the two major political parties in Costa Rica, which dates back to the days of bauxite exploration. Opposition to open pit mines is especially strong, in part due to a strong national committment to protect forested lands. Both of the two open pit gold deposits in Costa Rica have been accused of polluting the environment. Neither deposit is currently in operation.

Roughly thirty percent of the land area of Costa Rica is closed to mineral entry. Exploration is not permitted in national parks, indian reservations and wildlife preserves. Exploration and mining are permitted in national forests.

In addition, Costa Rica "froze" (restricted for mineral entry) inactive claims in the summer of 1989. Included in the frozen areas are anomalous areas identified by a 1987 Los Alamos stream sediment survey and "inactive" concessions (yearly fees unpaid, annual reports of labor not submitted, etc.). A total of 3000 km2 had been frozen by the middle of 1992. Ground can be unfrozed but, the requirements are more demanding relative to filing for a concession on "unfrozen" ground.

The freezing of ground is intended to eliminate the acquisition of concessions by companies or individuals who lack financial resources to explore and develop the property. In the past, some companies have applied for concessions, raised money for development through the sale of stock, and then disappeared. On frozen ground, the government will evaluate each company's application and financial status prior to granting a concession. Much of this frozen land will, I think, be transferred in debt-for-nature swaps rather than be reopened to mineral entry.

The Costa Rican legislature is considering a constitutional amendment guaranteeing all Costa Ricans a safe and healthy environment. Penalties would be imposed for companies which damage the environment and land would have to be restored to its original condition. This legislation, and other environmental bills offerred in the past several years, would effectively preclude mining.

Much of the Talamanca area is an indian reserve protected by the Indigenous Peoples law of 1977. The national park which straddles the border with Panama has been named a World Biosphere Reserve by the United Nations. An estimated 18,000 Bri Bri and Cabecar indians live in the region.

COMPETITOR ACTIVITY

Costa Rica has been visited by numerous major mining companies over the past few years. Rayrock opened an office in San Jose in the early 1980's followd by Phelps Dodge in 1988 and Placer International in 1992. A joint venture between Phelps Dodge and Independence Mining has applied for over 50 exploration concessions, mostly in the Talamanca region.

Rayrock continues to hold the Bellavista deposit (13.6 million mineable tonnes of 1.67 ppm gold) near the town of Miramar. Development of the deposit is on hold, pending improvement in the gold price. Negotiations over the terms of an export contract were successful, resulting in an agreement which allows Rayrock to keep a majority of the proceeds from the sale of bullion in an offshore account.

HONDURAS

MINING LAW

Honduras is an attractive place to develop new mines. The 1982 mining law encourages foreign investment and the 1987 tax code added additional favorable provisions. One hundred percent foreign ownership is permitted; there is no state-owned mining company; and, imported mining equipment is tax exempt. However, mining projects in Honduras suffer difficulties of currency exchange. Proceeds of the sale of mineral products go to the state bank which takes the dollars and pays in local currency (lempiras). Up to 30 percent of credited lempiras may be converted back to dollars to pay for outside obligations and materials.

Each new mine negotiates its own export contract, leaving substantial room for negotiation. Price Waterhouse reports that it is possible to keep proceeds offshore.

Honduras receives a gross production royalty of 2 percent until invested capital is recovered (maximum of 5 years). The royalty then increases to 3 percent and finally to 5 percent if annual proceeds exceed 3 million lempiras (US 1.3 million). Tax credits are issued if the combined effect of royalty payments and dividend taxes exceeds 55 percent of taxable income. Maximum corporate income tax is 50 percent. Withholding tax is 10 percent.

POLITICAL CLIMATE

Honduras continues to operate under a democratically elected government subject to a strong military. The two major parties are the Liberal Party and the National Party. Honduras received a triple A rating from the IMF in 1991 based on progress with a structural adjustment program begun in 1990. Inflation in 1991 was 40 percent.

The Honduran constitution (1957 and 1982) grants control of the military to the Chief of the Armed Forces, not to the President. The military sets its own budget and has its own court system. The Legislature has no control over the military budget and civil courts have no jursidiction over members of the military, even in crimes involving civilians.

COMPETITOR ACTIVITY

There are two operating gold mines in Honduras, Clavo Rico and San Andres. San Andres is currently processing close to 500 tons per day of heap leachable ore.

Fischer-Watt began an agressive exploration program in Honduras in 1990. They have acquired seven new concessions and in August, 1991 acquired the rights to explore at the San Andres deposit. Fischer-Watt and joint venture partner Kennecott are in their second year of drilling on the Minas de Oro property.

Mochito continues to operate under American Pacific Resources although the mine was shut down for a period during the fall of 1991 by striking miners. Thirty people were injured and one killed in a confrontation between miners and the Honduran military.

GUATEMALA

Guatemala passed a mining law in 1985 but, its provisions specifically exclude precious metals. Proposed changes, including provisions for extraction of precious metals, are stalled in the legislature. The country has no active gold mines and is one of the least stable countries in Central America. Topographic maps are classified, the local geological survey is run by the military, and field work in parts of the country is dangerous. Over 100,000 people have died over the past 30 years in an ongoing struggle between government and civilian militias (Institute for Central American Studies). The current president (Serrano) was elected by popular vote but, has limited control over police and military functions.

The government is soliciting bids on the Cerro Pato concession in southeastern Guatemala. Cerro Pato is a granodiorite-hosted vein with visible gold. There are several active and numerous fossil geothermal areas plus alluvial gold and lode antimony deposits in the Motagua fault zone. Exploration potential is very good.

The United Nations Development Program moved its offices from Tegucigalpa to Guatemala City in 1989 and is assisting the government with its assessment of mineral resources, particularly in the Trifinio district, which overlaps Honduras and El Salvador.

EL SALVADOR

El Salvador has some attractive gold deposits (e.g. San Sebastian). However, these deposits are in the Morazan and Chalatenango provinces, territories that, until recently, were controlled by rebel forces. Approximately 75,000 have died since 1980 in fighting between the government, paramilitary death squads and the rebel FMLN (Farabundo Marti National Liberation Front). Figures are from the Institute for Central American Studies (1991).

Peace talks between ARENA (National Republican Alliance), winners of the last general election, and rebel leaders of the FMLN were moderated during 1991 by former UN Secretary General Javier Perez de Cuellar. An agreement was reached for a cease fire to begin February 1, 1992. The agreement calls for a reduction in the military, disbanding of the rebel forces, registration of the FMLN as a political party and creation of a police force to be composed of former troops from both sides of the conflict. Land reform, a long-standing demand of the FMLN, is not addressed.

NICARAGUA

Nicaragua under a Sandinista administration was off-limits to private investment. That situation is changing since Violeta Chamorro assumed the presidency, winning the first free election since Somoza was ousted in 1979. However, the National Sandinista Liberation Front (FSLN) continues to be a major political force. It is certainly unclear at this point whether Nicaragua will develop a favorable climate for mineral investment. Nonetheless, some companies (e.g. Boliden) are exploring in Nicaragua, building on the work done by the Swedish government during the Sandinista regime. CORNAP, the agency responsible for privatization in Nicaragua, opened a bidding process during 1992 for a number of Nicaragua's largest gold deposits (El Limon, La India, Bonanza and Siuna).

Geologically, Nicaragua has excellent potential for new gold discoveries. There are a number of important epithermal gold and skarn districts with over a million ounces in past production (e.g. Limon, Siuna and Bonanza).

The World Bank and the Inter-American Development Bank have resumed loans to Nicaragua after a 7 year haitus. Inflation has fallen from 55,000 percent in 1990 to 6.6 percent since economic reforms were instituted in March, 1991. The government has reduced spending by 24 percent and 108 state-run enterprises have been shut down or privatized.