

Investors, beware the preliminary assessment

By **Roger Dixon** - July 22, 2020



THE dire state of the global economy may be prompting the considerable number of preliminary economic assessments (PEAs) that I see being published.

The problem is that PEAs are no foundation for production decisions in mining projects, and serve little purpose in detailed value-creation forecasts. For these reasons, investors should be reminded that there is not much value in the detailed value projections that often accompany these assessments.

Many PEAs include calculations on envisaged production levels, capital costs, operational costs and even net present values (NPVs) and internal rates of return (IRRs). Setting out these indicators in exact dollars and cents tends to belie the many assumptions that must be made at this stage in a project.

At best, it is a somewhat fruitless exercise to attach such exact numbers to a PEA – while at worst it could be highly misleading. There are just so many assumptions that are being made at this stage in a development, which have yet to be tested scientifically by technical studies.

It is true that stock exchange regulators do make special provision for PEAs, and that they do have a role in the project planning pipeline. These regulators highlight, however, that PEAs have severe limitations. For instance, they tend to be overly reliant on converting Inferred Resources – representing the lowest level of confidence in geological estimation – to Indicated Resources. They may also be misleading if they treat Inferred Resources as Mineral Reserves.

Reading media reports of mining project PEAs brings home this risk; some projects show that a third or more of the mineralised material they employ in their models is in the Inferred Resource category.

PEAs also tend to underestimate the costs and complexities of a project, and create expectations for indicators like NPV and IRR that may not be achieved in later studies – such as Prefeasibility and Feasibility studies. They also often use overly optimistic metal recoveries and metal price assumptions.

PEAs were not intended to be the basis for production or investment decisions. Rather, they are stepping stones in a much longer and more focused scientific and engineering process. In reality, a PEA does little to demonstrate economic viability, and projects at this stage of development typically have a high risk of economic or technical failure.

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