



Winner Take All: China and the Global Race for Resources



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1 Comment

In the summer of 2007, a Chinese company bought a mountain in Peru. More specifically, it bought the mineral rights to mine the resources contained in it. At 15,000 feet (4,600 meters) – more than half the height of Mount Everest – Mount Toromocho contains two billion tons of copper, making it one of the largest deposits in the world. For a hefty fee of U.S. \$3 billion, Mount Toromocho’s title transferred from Peruvian to Chinese hands.

Over the last decade, China has been buying up mountains and mines, agricultural land and oil fields, thus ensuring that it will have the upper hand in the future struggle for the world’s resources. Scarce, finite, and rapidly depleting global supplies of land, water, energy and minerals – the inputs to foodstuffs, automobiles, mobile phones, computers, and other

products of higher living standards – cannot match the demand emanating from a rising world population, rapidly increasing global wealth, and urbanization.

Despite the recent declines in commodity prices, the consequences of long-term fundamental supply and demand imbalances remain; the two most serious are substantially higher commodity prices and the rising risk of violent resource-based conflict. In the aftermath of the 2008 financial crisis, commodity prices increased 150 percent, and already there are around 25 conflicts raging around the world with their origins in commodities, with many more likely to occur over the next decade.

Thus far, national governments have tended to adopt a unilateral approach in order to retain control over scarce commodities, drawing on a mix of military force, higher taxation on commodity suppliers, and export bans on key resources. Across the world, policymakers are imposing similar inefficient policies that hamper global production, exacerbate shortages, and could, over the longer term, force commodity prices higher. For example the Australian mining tax laws introduced in March 2011 imposed a 30 percent tax on iron and coal companies; these are a stark reminder that such tendencies are not just the domain of emerging market politicians, particularly as developed countries continue to face biting fiscal constraints. The motive of many governments is not only to raise cash but also to retain and exercise control over resources, thus securing a steady domestic resource supply. The fact that commodity assets are increasingly falling into the inefficient hands of government compounds the problems posed by resource scarcity.

Despite existing unilateral approaches, commodity shortages are a multilateral problem, in that the people of the world will all face higher commodity prices again as well as the consequences of more political instability and conflict. In this regard, China alone seems to recognize the

need for a multilateral strategic approach to securing global resource supplies. China's multi-pronged commodity campaign relies on a variety of tools, including trade, investment, resource swaps, and financial transfers

The program has three key facets. First, China has systematically befriended the "Axis of the Unloved"; countries and regions of the world that have largely been ignored as destinations for investment by Western economies. Places such as Brazil, Argentina, Mongolia, Kazakhstan, and numerous countries throughout Africa have vast sums of mineral deposits, oil wells, and tracks of arable land. China's strategy builds on symbiotic relationships with such resource-rich host countries, who gain much needed capital inflows, infrastructure, and a large market for exports, in exchange for mortgaging their resources. Across the emerging world, where in some cases over 60 percent of the population is under the age of 24, investment and job creation are critical to stave off political volatility (such as that seen with the Arab Spring), to ensure sustained economic growth, and to meaningfully reduce poverty. In this regard, China's resource campaign offers a clear benefit.

Second, also central to China's global rush for resources is its vast treasure chest of over \$4 trillion in foreign exchange reserves, enabling it to pay substantial amounts of money for commodity assets around the world. China's global commodity campaign began in earnest in 2005. Since then, China's accumulation across the full commodity complex and all continents has been breathtaking. Between 2005 and 2014, China's foreign direct investments were valued at more than \$870 billion, or almost \$2 billion per week over the nine year period.

Some market participants have accused China of "overpaying" for assets – that is, paying greatly in excess of fair market value, distorting the commodity markets and rendering potential competition for commodity assets impotent. But China's willingness to go on this spending spree reflects the dogged determination of the Chinese political class to pursue economic growth, which relies on commodities as inputs. More generally,

in order to prevent a crisis of legitimacy, China's leaders must continually move the population to better living standards. Ultimately, China's cash pile and its broad political-economic goals mean China has a virtually zero cost of capital and seeks to secure resources at nearly any price. What looks like overpaying to the western-trained eye actually reflects China's broad utility function to improve the livelihoods of the Chinese population.

Third, China's aggressive and systematic approach has made it the "go to buyer" for almost all commodities. This renders it the marginal price setter in the commodity markets, giving China unprecedented influence on prices. Put another way, Chinese demand now crucially determines whether prices rise or fall across the commodity complex. Already many market traders believe China has become the marginal price setter for commodities such as copper and coal.

While China continues its multilateral approach to addressing the coming commodity headwinds, and fundamental supply-demand imbalances, much of the rest of the world appears disengaged. In fact, despite the risks of global commodity shortages, no unified international body exists to address the commodity challenges the world faces. Yet a cohesive, coherent, and explicit global framework that defines and manages competing resource interests and explores strategies for cooperation could help mitigate the risks of conflict and help rebalance the market.

In the absence of such an international body, China's multilateral approach to the commodity problem is sensible and, by giving host countries what they want, places China in a unique position with the upper hand in the future struggle for global resources. In a world of finite resource supply, and thus a zero-sum equilibrium, a less symbiotic/more unilateral stance raises resource prices, stokes conflicts, and is detrimental to global welfare. The predilection for military incursions in resource-rich regions such as Iraq and Afghanistan almost always disrupts production and forces prices

higher. For example, political clashes and military disruptions like those seen in Iraq, Nigeria, and Libya can often add at least \$10 to the price of a barrel of oil.

China's approach to securing resources is not without its critics. However, allegations of exploitation, worker abuses, and systematic labor and environmental transgressions in China's projects are routinely subject to over-simplification and exaggerations. China's motives are, in fact, transparent, and the evidence overwhelmingly points to symbiotic partnerships that see the resource-rich host countries greatly benefit. Around the world, China's efforts are broadly welcomed. According to a Pew survey of 10 sub-Saharan African countries, for example, Africans support Chinese investment by very large margins, with the balance of opinion of those surveyed regarding China and its inroads as decidedly positive and constructive. And despite damning charges that Chinese prisoners are used to staff projects across Africa, Sri Lanka, Bangladesh, and elsewhere, hard evidence is scant; the lack of evidence is surprising given that such transgressions should be easy to document in this age of smart phones.

As there are legitimate questions about the way workers are treated in China, the labor hurdles China seeks to clear abroad could be lower. But the charge that China is abusing workers and degrading the environment in wide-scale fashion, at least in a way that is much more aggressive than other foreign investors, is unfounded. Of course, China should not have a free pass to run unfettered and unchecked around the world, and allegations of labor, human rights, environmental abuses, corruption and financial misconduct deserve serious and objective investigation. But to finger-point and paint China's approach detrimental and, on balance, as negative bears little truth in reality and is patently unfair.

Nevertheless, given the fact that China's investment is in depleting resources, host countries are minded to manage the Chinese investment inflows as temporary revenues that will last as long as the resources exist,

rather than assume that they are open ended inflows that will last in perpetuity. With this in mind, many governments of petroleum-producing nations, for example, have created sovereign wealth funds, built up with the savings of oil-based revenues.

In reflecting upon what should be done to address the problems of access to resources and escalating commodity prices, a number of options are available. Aggressive government meddling in commodity markets (such as banning commodity speculators from the markets) has, on balance, tended to do more harm than good. Rather than skirting over the fundamental factors that are driving commodity prices higher and raising the risk of global conflicts by offering such band-aid solutions, policymakers need to put in place more fundamental policies that address the structural supply (based on caps of potable water, arable land, minerals and traditional sources of energy) /demand (driven by growth and wealth effects, urbanization and population growth) imbalance.

At the macro-level, for example, policies such as higher taxes on consumption can curb commodity demand. Supply-side policies like subsidies can also alter the supply/demand equilibrium by encouraging greater investment in R&D and exploration into alternatives, such as shale. More specifically, there is also scope to focus on various commodities in a targeted way.

Take food, for example. Policies that address waste, misallocation, and inefficient food subsidies could directly and meaningfully alter food imbalances. U.S. households throw out 14 percent of their food, wasting roughly \$75 billion dollars a year, while one billion people across the globe go hungry each day. More efficient allocation of portions and management of the inputs would go a long way to alter food imbalances. Multi-billion dollar food subsidy programs such as the U.S. Farm Bill and the European Union's Common Agricultural Policy distort the market by encouraging overproduction of food in some countries and underproduction elsewhere. The net effect of these policies is to keep food prices artificially high, to the

detriment of consumers. In 2010, the United States paid \$6 billion in commodity subsidies, with OECD countries spending over of \$220 billion on agricultural subsidies each year. Meanwhile, the EU's Common Agricultural Policy represents 45 percent of the total EU budget, with some 40 billion euros spent on direct farm subsidies annually.

On water, there remains significant scope to encourage investment in programs such as desalination. Although 70 percent of the earth is water, less than one percent is easily accessible fresh water that can be used to sustain human life, including for drinking and sanitation. The fact that a February 2012 report by the U.S. National Intelligence Council cautions that the world will face water shortages, social disruptions, political instability, and the use of water as a weapon to further terrorist objectives over the next 10 years suggests that significant investments in new technologies for fresh water production and distribution is time and money well spent.

Higher taxes on energy consumption could help reduce demand if they increased energy prices enough, but this remains a largely politically unpalatable solution. Energy conservation and efficiency measures may hold more promise. For example, pricing structures that reward consumers for saving energy (and penalize those who don't) could reduce and manage demand. Incentives for innovation and investments in energy efficient technologies could also help. However, technological innovations such as fracking and shale gas can be subject to aggressive environmental challenges which suggest technological innovations might not be as much a reprieve as one might hope, although worth exploring nonetheless.

Demand-side policies have their limitations, given that it is difficult to dissuade the newcomers to the growing global middle classes to curb their demand for "white goods" such as computers, televisions, refrigerators, washing machines, and mobile phones, each of which act as a draw on the world's mineral supplies. Here recycling is at least part of the solution. According to a United States Geological Survey analysis, for example, the

810 million cell phones in use, retired, or obsolete and awaiting disposal contain more than 13,000 metric tons of metal– the same amount contained in fifty 747 jumbo jets and enough to fetch a price of more than \$500 million. Such analysis suggests there may be a lot of scope for programs that provide an economic incentive for recycling or repurposing outdated metal-intensive consumer products.

More fundamentally, there is the argument that even a small reduction in the levels of U.S. military spending could help reduce the risk of conflict over commodities. Total U.S. military expenditure in 2014 was around \$610 billion (or roughly 3.5 per cent of GDP), making the United States the largest military spender by a long shot. If a portion of the money the United States spends on military incursions was directed to R&D for long-term solutions to commodity shortages, it is not at all clear that this would be detrimental to U.S. security; in fact, it might reduce the country's propensity to engage in resource related conflicts. This would help accomplish the country's purported military objective of keeping the peace.

Notwithstanding the challenges of China's commodity campaign its strategy – of giving host countries what they want – gives it the edge in the future struggle for global resources. This remains true even as the global economy (led by a slowdown in China, where economic growth has plummeted from double-digits to 7 percent per annum) has slumped in recent years, and virtually every commodity across the composite – metals, minerals, energy, and foodstuffs – has suffered a notable decline in price over the past year.

In a world of finite resource supply, a unilateral, “every nation for itself” stance leaves all countries as losers, and the world population suffering the costs of higher resource prices, declining living standards, and the proliferation of violent conflicts.

Response Essays

- **A Case for Calm about China** by Justin Logan

Justin Logan is considerably more skeptical that China constitutes a grave threat in a resource-hungry world. He looks at several Chinese economic projects and finds their results haven't been as successful as anticipated. Political and military tensions may well exist between China and the United States, but, he writes, they do not appear to be driven by economics. Commodity shortages have not been as damaging as feared, and China's response to them has been less fearsome as well.

- **China's Growing International Role** by Ian Bremmer

Ian Bremmer agrees that China's international economic policies are driven by the need to soften domestic opposition. He laments that there is no single international institution that regulates investment competition and scarce global resources. But China's actions have to be understood both as attempts to secure commodities and as attempts to find new markets for its industrial products. Like the United States and others before it, China may find itself increasingly committed to managing world conflicts in the process. Finally, the most important vulnerability that China poses to the rest of the world is not that it will continue to rise, but that it may fall: Should the people turn on the country's leadership, China's future would be highly unstable.

- **China Overpays: Still In Thrall to Failed Ideology of Central Planning** by Ronald Bailey

China would do well to abandon its attempts to manage world resources: they aren't paying off, says Ronald Bailey. He invokes data from the study of economic supercycles, during which the world economy deploys new technologies in response to new and changing resource demands. This data suggests that the world economy has now priced in China's rise as a manufacturing power - and even managed to supply more or less the mineral resources it will need. Commodity prices were high at the peak of the cycle, but they have since fallen, and there is no reason to think that things will change very soon.



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Westmiller · 10 days ago

Some useful observations in this essay, but it's plagued by the rhetorical ghosts of Paul Ehrlich and other failed prophets of doom.

In your lead example, a prominent "expert" forecast that we would run out of copper by 1944. It was a total rout:

<https://en.wikipedia.org/wiki/...>

Nevertheless, I concur with your view that the *worst* resource managers are governments, including those who profit enormously from their natural resources.

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