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Asia Summary

China and the Resource Boom: Comparative Insights from Latin America and Australia

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INTRODUCTION

This document is a summary of Dr Adrian Hearn's presentation on China and the Resource Boom delivered on 18 October 2013 at Chatham House. The event was chaired by Dr Tim Summers, Senior Consulting Fellow in the Asia Programme at Chatham House.

Dr Hearn examined China's increasing demand for resources from Latin America and Australia, and compared the structural challenges and opportunities this demand has produced in both regions. He focused on different strategies to manage taxation in the mining sector, and on the issue of Chinese land acquisition. He argued the China, Australia and Latin America all would benefit from comparing approaches to these common challenges.

The presentation was held on the record. The views expressed are those of the participants and do not represent the views of Chatham House.

CHINA AND THE RESOURCE BOOM

Dr Summers began by welcoming Dr Hearn to Chatham House and introducing his work on China and Latin America.

Dr Hearn explained that his interest in this subject has developed around the Track Two dialogue between Australia and Brazil. As major resource exporters, both countries share a deepening relationship with China. Dr Hearn became interested in comparing the ways that countries around the world have attempted to deal with some of the challenges of China's growing demand for resources, including managing resource prices, the taxation of mining and carbon emissions, improving dialogue with local communities, and handling investment from state-connected Chinese enterprises, especially sensitivities around their purchasing of agricultural land.

Before going into detail on the questions of taxing mineral exports and the issue of Chinese land acquisition, Dr Hearn gave some statistics. Raw commodities are now 60 per cent of Argentina's exports, 47 per cent of Brazil's, 75 per cent of Chile's and 40 per cent of Latin America's exports as a whole. Trade between China and Latin America has grown from $10 billion to $255 billion between 2000 and 2012. Mining and agriculture account for 90 per cent of this trade.

Australia has 70 per cent of the world's iron ore. China overtook Japan as Australia's largest trading partner in 2009, and Australia is the largest recipient of Chinese foreign investment.

How to manage the profits of the resource boom

Dr Hearn explained that China is interested in reducing its dependence on foreign exports and increasing internal consumption. Urbanization, especially in its Western provinces, means China still has a huge demand for mineral resources and will continue to look for these in other parts of the world.

In the recent Australian elections, the two main parties said that a priority would be to diversify the economy and become less dependent on resource exports. This will be complicated, especially as it will require retraining workers as the mining boom shifts from construction to less labour-intensive production. A pressing policy question for Australia and for other resource-exporters is how to act in the broad national interest and preserving the environment while allowing mining companies to run profitable businesses, and at the same time using a portion of those profits to diversify the economy.

Dr Hearn pointed to several useful examples from Latin America. Chile's Copper Stabilization Fund (CSF), similar to a sovereign wealth fund, has allowed investment in infrastructure, tax cuts for small businesses and counter-cyclical stimulus. Chile is often criticized for its reliance on copper, but the Organization for Economic Cooperation and Development has praised the CSF as a model for other resource exporters. Brazil levies a 25 per cent participation tax on mining companies, and has experimented with state taxes. The latter are used to build and protect local manufacturing, by giving exemptions to companies that invest in local capacity.

In Australia, several tactics have been tried, but there is no overall policy. In 2010, a government proposal for a 40 per cent tax on mining profits was criticized by mining companies of being discriminatory; the controversy played a role in Prime Minister Kevin Rudd's removal from office that year. In 2012, a 22.5 per cent tax on profits was passed, but this has failed to bring in the expected revenue – partly due to lower iron ore prices, but also because of a number of loopholes. A carbon tax was passed in 2012 but political changes may lead to this being eliminated.

The question of land acquisition

Dr Hearn then turned to the issue of agricultural exports, and China's interest in acquiring land overseas. China has nine per cent of the world's arable land and 40 per cent of the world's farmers; as it urbanizes, pressure to feed the population is intensifying. At the same time, international exporters looking to diversify their economies have identified agriculture as a promising sector – especially in light of growing interest from Chinese investors.

Dr Hearn first gave an example of a proposed agricultural investment in Argentina that turned out badly. A deal was negotiated between the Chinese corporation Beidahuang State Trade Group and the Argentine state government of Río Negro to supply soy products for 20 years from 230,000 hectares of land. The agreement was criticized on several fronts, including for the introduction of genetically modified crops without the required approvals, the proposed use of untested irrigation methods, the likely influx of Chinese labour and lack of consultation with locals. The deal was eventually scrapped, and in the aftermath the Argentine congress introduced tighter criteria for foreign land ownership (1,000 hectares or 15 per cent of a property). This outcome, said Dr Hearn, demonstrates that prospective investors must take into account the political and cultural sensitivity of land.

Land is problematic in many countries where China would like to do business. In Brazil, where it is the number one trading partner (since 2009) and gets 40 per cent of its soy, the government revived a land registry system, enabling it to place limits on foreign investment (5,000 hectares or 25 per cent of a property). Concerns about land are prevalent in Australia as well, and Chinese investments in the Ord Valley and the Cubby Station complex have become hot political issues. Interestingly, Chinese investment has evoked emotional reactions while much larger investments from other countries have not. China accounts for only four per cent of FDI in Australia while the United Kingdom accounts for 14 per cent and the United States 24 per cent.

Why the concern? Some argue that the land market has unique implications for food security, especially considering the fact that many of the Chinese firms involved in agriculture are state-owned enterprises (SOEs). Liberal democratic governments have maintained the position that agricultural produce should go to competing markets, not to a single customer at a concessionary price. Dr Hearn said that more research needs to be done to discern the differences between SOE and private investment, since as yet there is no hard evidence to show undue influence from the Chinese government on the supply and pricing of commodities.

CONCLUSION

Dr Hearn finished with several questions that he said Australia and Latin America would benefit from discussing. Can revenue from resource levies subsidize tax relief for other sectors and help to diversify the economy? Would taxation drive away investment? Do SOEs differ from other kinds of firms, and do their political connections pose a security threat? Finally, can multilateral or global forums such as Asia-Pacific Economic Cooperation and the G20 play a role in building shared understanding of emerging challenges and harmonising responses?

Dr Summers thanked Dr Hearn, and opened the floor to questions.

QUESTIONS AND ANSWERS

In answer to whether there have been attempts in Latin America to deal with China on a multilateral basis, Dr Hearn explained that there is no consolidated framework, though the nascent Pacific Alliance (consisting of Chile, Colombia, Costa Rica, Mexico and Peru) has stated its orientation to Asian markets. In 2013 President Nicolás Maduro of Venezuela visited China and he and President Xi Jinping agreed to work toward a China-Latin America Cooperation Forum. In the Caribbean, where the stakes are smaller, a group called the China-Caribbean Joint Business Council was established in 2007.

On the question of whether China has learned from its experiences to date, Dr Hearn mentioned how Chinese companies have begun to use better public diplomacy, including building schools, sponsoring sports teams, and getting involved in environmental protection schemes in the areas where they work. However, some Brazilian reports indicate that beyond high-level projects like joint satellite production for environmental monitoring, community engagement programs have been short-lived. In Australia, following Chinalco’s failed attempt to become a majority stakeholder of Rio Tinto, Chinese companies have turned to lower stakes deals, and begun to work more horizontally with local companies.

On the question of bilateral trade agreements with China, Dr Hearn cited the two existed agreements with Chile and Peru. These have led to deeper trade, but also increased the reliance of these countries on exporting raw materials, since eliminating tariffs has meant that their manufacturing sectors have struggled to compete with Chinese imports.

Dr Hearn also discussed the question of China's own resources, mentioning the difficulty it has had in exploiting its own iron and coal reserves, as well as its serious attempts to build its own agricultural sector, hoping to become 90 per cent self-sufficient in grain production. However, the inefficient agricultural system will take tremendous political effort to reform. Though China would like to be free of foreign dependence in strategic sectors, its leaders are also aware that many countries depend on exports to China, and that turning away from those trade relationships would generate political problems. To an extent this effect could be offset if foreign service providers are invited to play a greater role in China's increasingly urban and consumer-driven economy.