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Winner Take All: China's race for resources and what it means for us

A discussion with Dambisa Moyo

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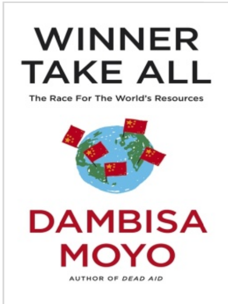
Dambisa Moyo

About the book



Dambisa Moyo discussed her latest book at Schroders Secular Market Forum; Winner Take All: China's race for resources and what it means for us. The book aims to cut through the misconceptions and noise surrounding resource scarcity, with a penetrating analysis of the commodity dynamics that the world will face over the coming decades. China has embarked on one of the greatest commodity rushes in history. Moyo asks what will be the financial and human effects of this – and is a large-scale resource conflict inevitable or avoidable?

Dambisa Moyo is the critically acclaimed author of *How the west was lost: Fifty years of financial folly – and the stark choices ahead* and *Dead Aid: Why aid is not working and how there is another way for Africa*. She was chosen as one of Time Magazine's 100 Most Influential People in the World in 2009. She holds a PhD in economics from Oxford University and a Masters from Harvard University Kennedy School of Government, and has worked for the World Bank and Goldman Sachs. She was born and raised in Lusaka, Zambia.

In the summer of 2007, a Chinese company bought a mountain in Peru. More specifically, it bought the mineral rights to mine the resources within it. Mount Toromocho is an imposing landmass, measuring more than half the height of Mount Everest. Within it lies two billion tons of copper; one of the largest single copper deposits in the world. For a fee of US$3 billion, Mount Toromocho's title transferred from the Peruvian people into the hands of the Chinese. China's commodity campaign is breathtaking.

A world ill-prepared

Moyo argues that the world remains largely ill-prepared for the challenges of resource scarcity and the evolving dynamics around China's central role. Commodities permeate every aspect of modern daily living. They are the inputs used to produce the goods and services that we rely on: the energy that powers our cars and electricity grids; water for the sustenance of all life forms; arable land that yields grains and other foodstuffs; and a long list of minerals used in everything from mobile phones to telephones, and as inputs to all sorts of machinery. Yet for all the importance of commodities and the markets in which they trade, our knowledge of this essential component of the global economy – and the largest asset class in the world – is hazy at best.

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"It is astonishing that there is no global agency that focuses on commodity headwinds" said Moyo. For trade there is the World Trade Organisation, for the environment we have the Copenhagen consensus, and for financial regulation we have the G20. Moyo believes that the absence of a global commodities agency comes down to the schisms that exist between many different countries, particularly between those in the emerging and developed world. In emerging economies access to water is highly politicised, whereas in the Western world energy is paramount. Here in London, we take it for granted that that clean water flows from the tap, but in many countries around the globe water rationing already exists, even in urbanised areas.

What is at stake?

'At a minimum, acute resource scarcity will lead the world into a period when the average prices for commodities – arable land, water, minerals, and oil – will increase to permanently higher levels', says Moyo. Higher prices will, inevitably, lead to worsening living standards across the world.

In the extreme case, and as resource scarcity really bites, Moyo thinks that commodity shortages could lead to outright war. Since 1990 at least eighteen violent conflicts around the world – many of them ongoing – have had their origins in resource shortages and access. Beyond this, numerous other countries in commodity-scarce regions are vulnerable to violence and clashes.

The supply and demand dynamics for commodities

To put her arguments in context, Moyo outlined the resource state of play as she sees it.

Demand

- **Population.** Growth from around seven billion today to nine billion by 2050. The ferocious rate of population growth is unique in human history – and many leading demographers believe that after 2100, it will never happen again. Commodity prices are inextricably linked to this anomaly.

- **Increasing wealth in emerging markets.** Emerging markets account for 90% of the global population, and it is expected that 3 billion people will become middle class.

- **Urbanisation.** As the most efficient way for governments to deliver infrastructure (such as healthcare and education) to citizens, many countries around the world have a deliberate policy of urbanisation, including China. Today, there are one hundred cities in China with population of one million or more, and they plan to build eight cities with populations in excess of twenty-five million. By comparison, the US has nine cities with a population of one million or more, whilst Europe has eighteen.

Supply

- **Land.** There are 13 billion hectares of land on the planet, but only 11% of that is arable. The other 89% is prohibitively hard to exploit for food production. Arable land is also not evenly distributed. China has a population of 1.3 billion, but only 12% arable land. Compare that to India, also with a population in excess of one billion, but with 50% arable land. In addition, cities tend to be built on fertile land, so as they grow this puts further pressure on land area per capita. Against this backdrop China has undertaken land purchase and lease schemes beyond its borders, particularly in South America and Africa.

- **Water.** Although at first glance China looks like it has sizable 'home' access to renewable water sources, in practice many are contaminated and not safe for human use. Therefore, a large part of China's water rush relates to securing access to water for its population. This includes not only investments in desalination technology, but also more aggressive policies that include re-routing rivers. The availability of fresh water per capita in both China and India is below the global average.

- **Energy – debunking the myths.** The world's major oil fields – whether on land or beneath the sea – have been discovered. In fact, the last major discoveries were made between the 1950s and 1960s, and today we are living off the production of these dated discoveries. This is the case even as oil hunters' efforts, using the latest technology, have intensified. Indeed, forecasts out to 2050 indicate that large oil discoveries are tapering-off fast. Oil discoveries, currently at around five billion barrels per year, will progressively decline to about two billion barrels annually by 2050 – reverting to discovery and production levels last seen in the 1930s. Since the early 1980s total new discovery volumes have consistently fallen below annual production. To make matters worse, many of the largest fields are now over 50 years old, and post-peak production their capacity to supply oil declines at an accelerating rate. Today, the world consumes oil at a rate of 85 million barrels per day (the USA consumes 20%, China consumes 10%). If nothing else happens, Moyo believes that natural declines from existing fields will see 2010's daily oil supply of 85 million barrels fall to 30 million barrels a day by 2030.

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Shale gas or hot air?

Moyo dismisses the notion that the US could become energy dependent via shale gas. She argues that the resistance from environment groups to shale gas production is fierce and, perhaps more importantly, that data from a number of energy agencies suggests that that yields from shale gas deposits are significantly over estimated. "While there may be some reprieve, shale gas will not cause a significant decline in the amount of oil that the US consumes".

The economic implications of China's ascendancy

Moyo believes China has developed a very systematic and deliberate strategy of accessing resources, and that it is the only country that is adopting a multi-lateral approach.

In just a few decades, China has become the most sought-after source of capital infusions. Rich and poor countries alike do not just wait for China to come calling; they actively court and seek out Chinese investments. China funds foreign governments (providing loans and buying their bonds), underwrites schools and hospitals, and pays for infrastructure projects such as roads and railways (particularly across the poorest parts of the world). In Moyo's opinion, this makes China an altogether more attractive investor than international bodies such as the World Bank, which often tie harsh policy restrictions to loans. China's economic influence on places as far-flung as the USA, Africa, Eastern Europe, and South America is incalculable. China's increasing global influence has mirrored its economic rise and, invariably, a concomitant rise in demand for resources.

China as a price setter

Across the gamut of commodities (but particularly coal and copper, and even non-publically traded assets such as land), China has become the dominant buyer, purchasing global resources in such disproportionate volume that it increasingly has price-setting power. Moreover, state-led capitalism means China is able to overpay for assets – and it has very deep pockets.

But who is China?

China's success relies on three different agents: individuals, corporations, and the Communist Party state. But Moyo agued that ultimately they all pull together – public and private – under one unifying force with a single agenda: the betterment of China. China's ambitions are similar to many other governments; the difference lies in China's ability to execute its agenda through its centrally planned command-and-control system of the economy. China's Communist Party sponsors and influences the behaviour of mammoth state-owned enterprises, including banks, energy firms, transport and logistics businesses, and resource companies.

As the government makes its financial muscle felt, the line between private and public can appear deliberately blurred. For example, the Chinese state retains sizable equity stakes in many publically traded companies, and almost all the top 30 Chinese multinational enterprises are state-owned. In 2009, for example, Wuhan Iron and Steel, China's third largest steelmaker, was extended a line of credit amounting near to $US12 billion by the state owned China Development Bank. A primary goal of the loan was to finance 'overseas resource base construction', which incudes the roll-out of large iron mines and steel plants that would produce these commodities. Such loans became common as the Chinese government encouraged state owned banks to lend in order to stimulate the economy in the wake of the 2008 financial crisis.

The strategy of providing China's network companies access to cheap money, state endorsements, and preferential access to foreign government contracts seems to help steer China's developmental agenda. And because this approach is proven to work well for Chinese government and the command-and-control method of the Communist Party, it is unlikely to change anytime soon.

Three reasons why the commodities super-cycle has not come to an end

1. **Convergence.** Moyo argues that China's system of state-sponsored capitalism buttresses its efforts to bring its people into the middle classes. Consider that it took China just 12½ years to double its per capita income, compared with 53 years in the USA and 154 years in the UK. Consider that today the USA has 800 cars per 1000 people, whereas China has 75. While Chinese policy-makers are concerned about a resources bottleneck, they have shown that they are willing to be very aggressive to meet their demands. One caveat to this is China now has more roadway than the USA, which could lead to lower demand for iron in the future.

2. **Intensity of mineral use (and the lack of substitutes).** For copper and oil the amount used per unit of output is now flattening out – we are no longer seeing significant improvements. Moyo accepts that the arguments for improvements in the intensity of use may come to pass, not least through innovations in technology, but at present there is no evidence of this. In fact, for aluminium and coal, use per unit of output is increasing in China.

3. **Reservation price and demand destruction.** In the US, the sluggish economy has led to downward pressure on oil's reservation price (the maximum price a consumer will pay or the minimum price a producer will sell for). Before the financial crisis it was above US$100 per barrel, whereas today it sits around US$90 per barrel. This means that above US$90 per barrel demand is eroded as people alter their habits, which acts as an automatic stabiliser for commodity prices. In emerging markets the polar opposite is happening: the reservation price is rising, which is closely linked to increasing per capita incomes. Data suggests that oil could reach US$200 per barrel before demand is eroded in China, although government subsidies do play a role.

> China appears to be determined to pull all available levers and, because China's resource undertaking is global and the most aggressive in history, it has economic consequences for us all."

Moyo's conclusions

China's global charge for hard and soft commodities, and the infrastructure that facilitates their extraction and delivery, is meant to guarantee the continuation of its already remarkable story of economic development. In a world where cash is king, China's cash stockpile of over US$3 trillion in foreign currency reserves allow it to do what other countries cannot do, and go where other countries cannot go. As a result, Moyo argues that China's voracious appetite for commodities is unlikely to abate significantly, even if economic growth rates cool. To that end, Moyo asserts that the Chinese appear to be determined to pull all available levers and, because China's resource undertaking is global and the most aggressive in history, it has economic consequences for us all.

Against this backdrop, Moyo believes that Western governments need to engage with China more on the global stage – perhaps by inviting China to play a far more central role in the global development agencies. A more co-ordinated global approach towards the commodity headwinds we face is vital if we want a just, balanced and peaceful global economy in the 21st century.