



The Red Dragon Spreads Its Giant Wings – China's Resource Acquisitions

Introduction

China's investments in natural resources have increased recently. Chinese companies are backed by the government to acquire stakes in natural resource companies and are encouraged to sign long-term contracts for oil and minerals. In addition, the Chinese government provides loans to mining and petroleum investors for both domestic and overseas investments.

Resource Procurement Strategies

China is investing in foreign companies through domestic companies, the government or enterprises (in which stakes are held by both the government and private companies). These institutions are procuring resources by:

- Acquiring an equity stake with a producer
- Acquiring an equity stake with a competitor
- Providing loans to a producer (that are to be repaid in output)
- Providing loans to a competitor (that are to be repaid in output)

The Chinese government has provided loans to domestic companies for the acquisition of natural resources in Central Asia, the Middle East, Africa, Latin America and the South Pacific

Expansion of Chinese Companies – An Overview:

	Methods	Examples
Organic Growth	<ul style="list-style-type: none"> • Exports • Greenfield Investments 	<p>Haier Group</p> <p>Huawei Technologies</p>
Alliances/ Partnerships	<ul style="list-style-type: none"> • Joint ventures to invest abroad 	<p>Chery agreed to build small cars under Chrysler brand for sale in the US</p>
Mergers & Acquisitions	<ul style="list-style-type: none"> • Acquire overseas natural resources • Acquire overseas brands • Acquire companies for know-how and technology transfer • Cater to companies need for capital 	<p>Lenova's acquisition of IBM's PC Division,</p> <p>Shanghai Automotive Industry Corporation's acquisition of Rover Technology</p>



Impact of China's Acquisitions:

If the agreement reached during the procurement of resources is only a legal claim to the production or supplies, then it has no implications for other customers. However, if the agreement is with respect to increasing output, then consumers benefit due to the increase in production.

Additional Investment Activities:

Chinese investment activity is increasing; this trend is expected to continue in the future.

- China's substantial trade surplus (which totalled USD 272.5 billion as of 2010), its FOREX reserves and gold (which totalled USD 2,622 billion as of 2010) and its high savings rate (45% of GDP) will encourage China to increase its investment activity.
- China is expected to move away from parking a substantial percentage of its reserves in US bonds and invest in other foreign nations.
- China's plans to acquire natural resources, high technology, emerging technologies and firms with global financial expertise will drive its investment activity.

RAND Corp.'s Charles Wolfe Jr. has predicted that Chinese investments and acquisitions will double in the next five years and possibly quadruple by 2020. If the country's investments and acquisitions grow at this rate, China will become the largest global investor or, at the very least, near the United States' ranking. Currently, China is ranked sixth.

Factors Driving China's Increasing Demand for Resources:

- The price of commodities is expected to increase because the global economy is showing signs of improvement. As a result, China is taking measures to gain greater access to natural resources to mitigate future price hikes.
- China is using FOREX reserves to acquire natural resources and oil reserves to ensure future supplies.
- China is acquiring natural resources to cater to its current domestic demand as well as its long-term interests.

The Chinese Investment Corporation (CIC) provides a substantial amount of credit to state-owned companies for overseas resource acquisitions.

Economic Growth	Urbanization
China is the fastest growing economy. Its average growth rate is 10%.	More than 350 million households will have an annual disposable income of more than USD 3,200 by 2020-2025.
Economic Growth	Modernization
China has been increasing its manufacturing activity to maintain its market share in exports and cater to the rise in domestic demand.	Large investments have been allocated for the upgrading of telecommunications, transportation and energy sectors.

Rare Earth Metals – An Exception

China controls 95-97% of the global supply of rare earth minerals. China reduced the export quotas for rare earth elements used by the consumer technology, clean technology and high technology industries for 2011. The country also stopped the export of some rare earth metals to the US during the last quarter of 2010. This move gave China greater control in international markets and is expected to drive more foreign investment in China's rare earth industries.

Challenges Ahead for China

The challenges that could disrupt China's investment plans are:

- China's foreign investment plans could result in increased tension between the country and other nations due to its restrictions for foreign acquisitions within China.
- Host countries may resist China's investment plans to protect their national economic interests.

Chinese metal company Chinalco planned to invest in Australian ore giant Rio Tinto in 2010. However, this plan was opposed by its shareholders and the Australian government and never reached fruition.

In 2010, China's Anshan Steel planned to invest in the steel mill under construction in Amory, Mississippi. This mill would be China's first domestic foothold in the US steel industry. US steel producers initially resisted the investment; however, the deal is now moving forward.

Regions under China's Resource Acquisition Radar:

Canada

China has started focusing on acquiring natural resource companies in Canada. A wealth fund from China (an investment vehicle of the Chinese government) announced its plans to open an office in Toronto to invest in companies operating in Alberta oil sands.

Europe

China has been investing in Europe's infrastructure. The country provided funding for ports in Greece and Italy and highways that link Eastern Europe to Germany and Turkey. China's investments in Europe's infrastructure are expected to increase, which would help China expand its presence in the European distribution and production chain. With these investments, China hopes to garner Europe's support regarding its currency and trade disputes with the World Trade Organization (WTO).

Africa and Latin America

To safeguard its future supply of energy and commodities, China is focusing on new oil producers in Africa and Latin America (irrespective of the operational risks involved).

Venezuela, Iran, Russia, and Brazil

China plans to utilize its reserves of more than USD 2 trillion to acquire oil and gas producers in Venezuela, Iran, Russia and Brazil or to enter into long-term supply agreements with suppliers from these nations.

China's Strategic Shift

China has been focusing on the acquisition of raw materials and energy to ensure future supplies for its capital intensive heavy industries. However, China is now striving to increase the popularity of its domestic brands and improve its production technologies. This shift is expected to drive the emergence of innovative and branded Chinese products, which could capture the domestic and international markets.

Takeaways

- China has been acquiring metals and energy commodities.
- China has been increasing its control over the rare earth metals market
- China is converting its USD reserves into physical assets
- China is increasing its iron ore supplies to support the development of domestic infrastructure.



Conclusion

The economic downturn was viewed by the Chinese as an opportunity to expand investment and access to natural resources. As economic recovery continues to happen in developed nations, Western nations would also look to expand their natural resources. The thirst for resource acquisition could result in either co-operation or resentment among nations. However, this would play a major role in shaping up a relation between nations in the future.

Sources: voxeu.org, thebeijingaxis.com

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