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Stronger growth needs innovation

A forecasting consensus about the weakness of 2020s economic growth is retarding new mine capacity.

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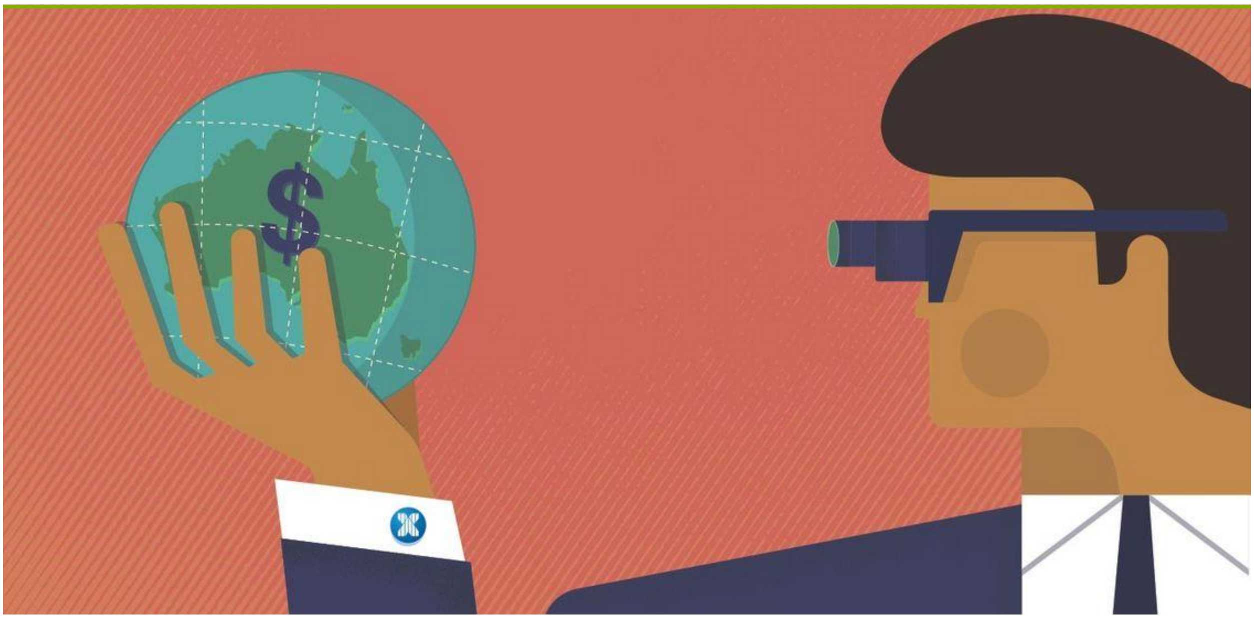

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Mining company presentations, citing industry analysts, almost universally show metal usage outstripping mine capacity during the 2020s. A stronger consensus would be hard to imagine.

The bullish prospects presented by the industry are at odds with many instances of stalled projects and underfunded exploration.

No single explanation accounts for the divergent views. Some self-serving analysts might be steering miners in the wrong direction. That is one possibility. Investors, on the other hand, could be spoiled for choice with an abundance of nearer term investment opportunities with better risk-adjusted returns on capital.

Industrial users of metals might also be sending out the wrong signals. If the manufacturers of motor vehicles, for example, are unperturbed about the availability of industrial raw materials, why should others worry? Valuations would quickly change if Volkswagen felt compelled to buy a couple of cheap nickel projects to secure their strategies.

No money managers have failed in the last three decades by ignoring the mining industry. Historical neglect of mining has been a winning investment strategy. Old habits die hard. Miners might have to wait for the 2020s to run their course before being able to say, "we told you so".

Differing views of future growth patterns provide more fundamental reasons for the divergent judgements about the need for new mines.

Underpinning the dominant mining industry world view is an assumption of steady ongoing growth in demand supplemented by new uses to intensify the impending market deficits. Investment strategists with an eye on the longer term, on the other hand, see global growth slowing.

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Demographic forces were going to be a drag on growth for another 30 years. Global population growth is on a downward trajectory from about 1.5% near the turn of the century to 0.5% by 2050, according to the United Nations. Within the slowing growth profile, the number of people over 65 years of age is expected to double, contributing to lowered productivity, a rundown in savings and added public welfare demands.

China's population, so critical to the pace of raw material consumption for the past 30 years, will be contracting after having grown at 2% in the latter years of the twentieth century. China's other important sources of abnormal historical growth, namely, liberalisation of private property laws and cultivation of market forces more generally, also appear to have run their course.

Meanwhile, a reduction in China's globally significant savings will constrain growth, not simply through the country's lowered investment potential.

Advanced economy budget deficits, funded by Chinese savings, have fuelled spending on Chinese goods. Propping up that nation's employment and income base has, in turn, sustained the pool of savings on which western countries have come to rely for their deficit funding and consumption expenditure.

Freely flowing capital and unhindered movement of goods have been at the heart of this benign circle of economic life. Even before the new coronavirus hit, these mutually beneficial trade and financial arrangements were crumbling.

The coronavirus has increased pressure to diversify supply chain risks. Governments, attempting to restore employment numbers, will be keen to repatriate manufacturing activities. Fragmentation of supply chains established to maximise efficiency will have a detrimental effect on growth outcomes.

The accumulation of coronavirus related government debts will force governments to adjust spending priorities through the 2020s, to the detriment of productivity enhancing investment. Even without any rise in interest rates, a larger proportion of government budgets and national income will be directed to debt servicing.

Massive central bank interventions over the past few months will have raised the risk of poor capital allocation decisions. Prioritising central bank support for companies at greatest financial risk disadvantages newcomers or those with more innovative products better tailored to future conditions. The bias against innovation potentially detracts from longer term growth prospects.

Massive unqualified support for asset prices implicit in central bank securities purchases exacerbates wealth and income inequalities. Social tensions arising from perceptions of income injustice were already fertile grounds for radical policy proposals with an anti-growth tinge. That pressure will intensify.

While economic growth is facing strong headwinds, the COVID-19 pandemic has demonstrated a readiness to adapt to changed ways of conducting business and living daily lives. The dark cloud does have a silver lining.

The shift from city to home offices, if sustained, will have important economic consequences. Investment in central city office space could be redeployed more productively. Transport infrastructure needs will have been reduced. Outsourcing and new income opportunities will better match employee needs and contribute to a more flexible work force.

Working from home has dramatically upped the demand for easy to use digital technologies. Broadband suddenly looms larger as a basic need as well as a tool for sophisticated high end manufacturing processes. US House of Representatives majority whip Jim Clyburn has recently spoken about reprioritising the national rollout of broadband over roads and bridges in infrastructure spending proposals.

Extricating themselves from Chinese dominated supply chains will lead companies to look aggressively at labour saving options to maintain their profitability. Robotics and automation to enhance productivity will sustain higher living standards for workers drawn back to manufacturing in Europe and the USA.

Resource utilisation will not constrain activity. The combination of unusually high levels of unemployment and the nascent business and social trends coming out of the coronavirus lockdown raises the prospect of an unprecedentedly long period of recovery and economic expansion.

The world could be on the brink of a previously unanticipated innovation boom leading to a sustained rise in global growth.

A growth slowdown, still the most favoured outcome among economists, is not a foregone conclusion. But unimpeded innovation is needed if the slow growth path, with its accompanying negative impact on mining investment flows, is to be avoided.

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