Mining Journal

Better than nothing, but not enough

China's One Belt One Road regional development initiatives may prove too modest to change the cyclical landscape for the mining industry.

John Robertson* | 25 May 2017 | 5:43 | Opinion

China planned infrastructure spend will move the needle on commodity pricing, but not by much

The fortunes of the mining industry have depended historically on periods of highly elevated growth in metal intensive investment spending.

Between 2003 and 2007, for example, as miners experienced a surge in industry prosperity, global investment spending rose at double-digit rates for five consecutive years.

Chinese annual investment growth averaging over 20% propelled a spending increase from around US$400 billion to $4 trillion a year between 2000 and 2012, according to International Monetary Fund statistics.

In contrast, since 2010, global output growth has weakened amid an investment spending slump.

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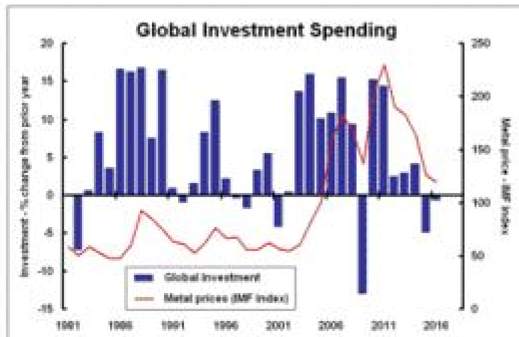
Excess production capacity has limited the need for private sector investment. At the same time, worryingly large fiscal imbalances have restrained the willingness of governments to drive infrastructure spending higher despite abnormally low funding costs.



Falling productivity growth, in the absence of supportive investment spending, has placed a lid on wages in many advanced economies which has, in turn, acted as a dampener on demand and output growth.

China's efforts come against the backdrop of historically weak global growth and contracting investment spending.

One Belt One Road is being promoted as a massive infrastructure building programme to connect China with Europe through central Asia. It will connect China's maritime routes to east Africa and the Middle East to the Mediterranean region.

Analysts have estimated that the Chinese government could kick start spending of up to $150 billon a year over the next 10 years to get its grand plans underway.

Without China, the economic landscape looks ominously bare for the mining industry.

Even where there is discussion about improved growth prospects, such as in the US after the election of Donald Trump as president, targets are quite modest with few expecting the US economy, in the best of circumstances, to grow sustainably faster than 3% after battling for years to reach 2%.

The G20, which had nominally committed two years ago to raise growth through productivity enhancing initiatives appears, to have made no meaningful progress toward better outcomes and, as a group, now shows no sign of offering alternative ways to engineer an acceleration.

Some have compared the potential impact of the Chinese moves to the Marshall plan that drove development in Europe after the Second World War.

Despite the obvious development benefits and potential to precipitate stronger growth in many developing countries, considerable scepticism about the motivation of Chinese economic leadership is reducing the potency of the effort.

From China's perspective, One Belt One Road will open up new markets for its goods and services as growth in domestic demand slows. However, the motivation clearly extends beyond economic considerations.

China's plans assert a pivotal political role on the global stage. One Belt One Road projects China's potential influence in an unprecedented fashion at a time when the USA, Russia and the EU are preoccupied elsewhere.

One Belt One Road also has a military dimension with China using its commercial and political connections to establish a naval presence within the Indian Ocean region despite its historical opposition to others bidding for regional military influence.

Among the major developing economies, India has been conspicuously hostile to Chinese overtures. The Italian prime minister attended a meeting of 28 world leaders in Beijing this month to promote China's plans but major European leaders were absent.

> ***"Priming the pump may not be enough"***

Wariness about China's motives is slowing the embrace of advanced economy governments, international funding organisations and private money on which China will depend for fulfillment of its ambitious plans.

Financial constraints among already highly indebted national governments and, among existing development agencies, fears about ceding too much influence to newly formed funding institutions backing China's plans are headwinds.

To demonstrate its determination to succeed, China could decide to speed up deployment of funds from its own reserves in selected countries willing to grasp the opportunity but rates of return will be important if private-sector money is to be recruited.

Priming the pump may not be enough.

In many of the 68 countries signed up to the Chinese development initiative, unsubsidised risk adjusted returns from infrastructure investments remain lower than those available in advanced economy markets.

The mining industry will be better off for having China's economic muscle behind developing country infrastructure spending but the impact of the spending could be easily exaggerated.

One Belt One Road funding will allow better use of Chinese savings. Economists have long documented China's inefficient use of savings in domestic investment projects designed to meet growth objectives. Stories of unoccupied apartment blocks, palatial official accommodation and uneconomic pet regional projects abound.

Diverting relatively inefficient domestic spending to One Belt One Road spending will improve the social and economic returns from Chinese investment and contribute to a more robust financial system but limit the extent to which the mining industry can count on a net increase in demand for its products.

Even without a diversion of investment from within China to other countries, a $150 billion annual commitment would be equivalent to only 3% of China's own average spend in 2015 and 2016.

No matter how enthusiastically welcomed in some countries, $150 billion today would be equivalent to just 0.2% of annual global GDP and 0.8% of current global investment spending.

The numbers being contemplated are dwarfed by the 13% average growth in global investment during the mining industry cyclical upswing in 2003-2007 and well short of compensating for a $1.1 trillion spending contraction over the past two years.

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