China's rare earth monopoly threatens global suppliers, rival producers claim

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The Chinese acquisition of stakes in Australian rare earth miners Lynas Corporation and Arafura Resources has "caught the rest of the world sleeping," said Rod McIllree, managing director at Australian-based Greenland Minerals & Energy (GME).

Following two acquisitions in the past six months for an aggregate USD 163m, Korean, Japanese and Western players may find themselves locked out of the sector, McIllree told mergermarket. Speculation is rife as to what this may mean for the high tech and green industries that rely on rare earth metal resources. With over 90% of the global rare earth resource held by Chinese companies, the country's monopoly looks unchallenged. The recent Australian acquisitions have brought China control of the majority of the rare earth deposits outside China.

Rare Earth metals are a collection of 17 different metals that occur within the same ore deposits. While China currently produces 95% of the worlds rare earth supply, the metals are also found in the US, Indonesia, Australia and South Africa. Rare earth metals are needed for the manufacturing of wind turbines, plasma televisions, mobile phones, hybrid car batteries meaning the Chinese monopoly could shift the high-tech manufacturing industry bases from Japan and Korea to China.

Acquisitions of Australian rare earth miners are strongly backed by the Chinese Government, a China-based industrial banker said. Since 2004, or even earlier, the Chinese government has treated rare earth resources as strategic. In order to protect the resources available to China, the government employs a three-pronged strategy; rare earth exports are restricted, imports encouraged, and outbound rare earth acquisitions actively encouraged.

GME's Rod McIllree, said the recent Chinese acquisitions highlighted the importance of the industry. With its multi-commodity ore body, GME is one of the last independent rare earth miners. Companies like GME that lack multi-commodity ore bodies including minerals such as iron ore alongside rare earths will find it hard to operate outside of China's influence because most of the technology needed for refinement is only produced in China, he said. Japanese, US and European players now face higher barriers to entry which may prevent them from regaining a foothold.

However, Australian-based Lynas, despite now being majority owned by China Nonferrous Metal Mining Co (CNMC), will not sell resources exclusively to China, Vice President Matthew James said. CNMC is on board as an investor, not a buyer of rare earth; it differs in operation to Chinalco, James noted.

Arafura, which recently sold a stake to East China Exploration (ECE), was unavailable for comment.

Japanese and Korean players voice fears

The Chinese Government's protective moves over rare earth are likely to impact Korean high-tech industries in the next couple of years, said Daehyun Kim, chief executive of Saebo Energy, the privately-held Korean rare earths material developer.

The technology gap between Korean high-tech companies and their Chinese peers is expected to close in four or five years. Moreover, China's export quota and pricing policies will place significant pressure on Korean companies who will find their competitive prices at stake when faced with rising competition from China in the global market, Kim added

Unlike large, Korean electronic products makers such as Samsung and LG, small to medium sized businesses in Korea would suffer from limited supply or higher prices of rare earth resources. Samsung and LG have been purchasing rare earth from Japanese suppliers which boast top-tier technology for rare earth extraction. These two industry giants, at least, can afford the high prices commanded by Japanese suppliers

The South Korean Government must secure rare earth resources and invest in the development of extraction technologies if it wants to ensure the competitiveness of Korea's hi-tech industries, Kim said.

The current economic downturn presents an attractive opportunity for Japanese firms to invest in rare metal mining rights, industry and government sources said. However, privately-owned Japanese companies are at a disadvantage when competing with state-owned Chinese companies. The Chinese have easy access to government capital while the risk assessment for a Japanese company can take much longer. Additionally, the Chinese government, in its determination to increase rare earth resources, is also less risk averse.

A source at Sojitz, a leader in rare metal imports, agreed that the Japanese companies are unable to compete. Unlike the worry-free Chinese, listed Japanese trading and mining companies have to consider the impact on their share price if they overpay for assets.

Rare earth prices have been on the increase again since this March, having fallen 50% year on year, making the assets attractive assuming the economy improves. While the government-owned Japan Bank for International Development will guarantee project financing, the difficulty lies in assessing the right price. Asset valuations for metals such as nickel have been driven up by Chinese acquisitions rather than demand, the Sojitz source noted.

Japanese Government-owned institutions are watching with concern as the Chinese Government-owned companies continue their shopping spree in countries like Australia, sources at Japan Oil, Gas and Metals National Corporation (JOGMEC) said. JOGMEC, which finances prospection and exploration projects, is actively seeking to support Japanese companies that want to invest in natural resources which will supply to Japanese industry. JOGMEC, whose budget increased to over JPY 30bn this year, prefers to invest in low risk countries like Australia but investments will have to be made where the deposits were found.

A source at Nippon Export and Investment Insurance (NEXI), which provides insurance on foreign investments made by Japanese companies, echoed JOGMEC's concerns. While the Japanese Government's financial aid is welcome, it will not be enough to help the Japanese compete effectively with their Chinese peers. NEXI does not have a fixed budget. It is willing take on a portion of the project financing risk by providing insurance not only on project financing but also for natural resource deposits and against country risk for up to 15 years.

However, those defending the Chinese position argue that one of the purposes of the Chinese acquirers of rare earth in Australian is to serve their Korean and Japanese clients because China has restrictions on rare earth and other resource exports. More generally, they note that while in the past Chinese companies had been out-bid by cash-rich Japanese bidders, the situation has now reversed because the Chinese government has now recognized its need to purchase overseas resources.

China relentless

Chinese outbound acquisitions or co-development of overseas rare earth mines is encouraged and guided by the Chinese Government, said a source at Inner Mongolia Baotou Steel Rare Earth Hi-tech [Bao Gang Xi Tu], one of China's largest rare earth mine developers. Acquisition financing can be raised through state-owned banks, guaranteed by the Government.

Rare earth mines in Australia are prime targets given their quality and the nation's low risk profile. The rare earth arm of Baotou signed an agreement with Arafura to co-develop an Australian rare earths mine at Nolans in late 2008.

Although China is home to the largest rare earth reserves in the world, it is still actively seeking chances to acquire overseas mines, a Chinese based analyst said. The purpose is to assure resources for the green energy, high-tech and defense industries. China is not the only country aggressively seeking to expand its rare earths resources; the US and Russia have similar policies, the analyst noted; the only difference is that China is leading the race.
