

CARNEGIE COUNCIL *for Ethics in International Affairs*

By All Means Necessary: How China's Resource Quest is Changing the World

Public Affairs, Global Ethics Forum TV Series

Elizabeth Economy, Michael Levi, Joanne J. Myers

Transcript

Introduction

JOANNE MYERS: Good afternoon. I'm Joanne Myers, director of Public Affairs programs, and on behalf of the Carnegie Council, I would like to thank you all for joining us.

Today our guests are Michael Levi and Liz Economy. They are both senior fellows at the Council on Foreign Relations. Liz is also the director of Asia studies and Michael is the director of the program on energy, security, and climate.

Together, they have written an interesting new book entitled *By All Means Necessary: How China's Resource Quest Is Changing the World*. In it, they talk about China's economic explosion and the need for China to pursue raw materials and just where this may take the country and what the consequences are for both China and for the world around us.

I will begin by asking them questions and then, after about 30 minutes or so, I will invite you to do the same.

It's said often that you can't judge a book by looking at its cover. But oftentimes the title does reveal what's inside the book. To state the obvious, *By All Means Necessary: How China's Resource Quest is Changing the World*. Let me ask you, do you think China is in fact changing the world?

Remarks

ELIZABETH ECONOMY: Let me first thank you, Joanne, for hosting us at this lovely event. It's a real pleasure for us to be here and have the opportunity to speak with all of you.

Let me start by taking the title, *By All Means Necessary*. What that really refers to is all the tools that the Chinese government has at its disposal for going out to secure resources outside its own borders—for example, a special kind of presidential diplomacy. When President **Xi Jinping** travels to Africa, he may travel with a number of government ministers, as well as heads of state-owned enterprises, and propose a vast array of trade, aid, and investment deals in a way that is really not like any other country.

China also has at its disposal low-cost financing and low-cost labor that it can export to undertake a lot of the infrastructure projects that surround a lot of the resource development that it also wants to pursue.

And, of course, there is the kind of backroom deal at which the Chinese often excel. We see that they do this on the home front and they do it when they travel abroad as well. The same kinds of laws and governance that may limit the ability of U.S. companies to do these sorts of things—the Chinese don't necessarily have the same kinds of restrictions on them.

So the first part of the title really refers to those kinds of tools that we see the Chinese utilizing when they go abroad.

MICHAEL LEVI: Why don't I pick up the subtitle, *How China's Resource Quest Is Changing the World*.

When you look at all these tools the Chinese can bring to bear, you're bound to see consequences across the board. We see consequences for the economies where China invests, for governance structures, for political relationships, and for even the military and security underpinnings of the global resource trade.

But for all the excitement you see on all those fronts and all the great stories you can find, when it comes down to it, one of the most surprising things we saw was that it's China simple demand and the impact that has through traditional trade that may be changing the world in bigger ways than anything else.

Chinese demand exploded over the last decade. The world was slow to catch up. That drove prices steadily higher for a host of different commodities. And regardless of whether China was trading with this or that producer—oil or iron ore or copper—the consequences for these countries' economies were enormous. The consequences for other consumers were huge, too, because they were paying higher prices as a result, and we have seen transformations everywhere from Africa to Canada to the Middle East as a result of that very basic piece, that surging demand that China has brought to the world.

JOANNE MYERS: Just to follow up, do you think in some way they are undermining markets or causing an increase in prices, then?

MICHAEL LEVI: They've certainly caused increases in prices. If you look at oil, we wouldn't have moved from \$20-a-barrel oil to \$100-a-barrel oil over the span of less than a decade without growing Chinese demand. You see similar patterns in places like iron ore and copper.

There are other commodities where the story isn't the same. Aluminum, for example, because there were a lot of other sources of demand and because people were expecting increased consumption, didn't respond as strongly on prices. You saw food prices go up a lot, but that was in part because of China and in part because of a host of other pieces, both on the supply and the demand sides.

There's a distinct question to do with whether they are undermining markets. There was a lot of talk, particularly about 10 years ago, about China locking up resources, moving to a more mercantilist system for trade rather than using markets. If we look at what has actually happened, there is very little evidence for that outcome. China certainly is buying equity stakes in oil production around the world, but it sells most of the oil that it gains on the open market rather than shipping it back to China. You have other cases where China has inadvertently promoted more market-based systems.

Ten years ago, the world used very rigid, closed-door systems for structuring trade in iron ore. A host of small Chinese steel mills came into the market, essentially fractured it, and brought forth a much more market-based system for iron ore trade.

Here's a case where you need to look at the mass of China, at China as a huge consumer, rather than at what the Chinese government says it wants. If you look at what they say they want, you will miss some of these transformations that come not from their intentions, but from their sheer size.

JOANNE MYERS: They also say that China, in this pursuit, sometimes acts very aggressively and far-reachingly. Have you found that in your research to be true, that they are more aggressive than, say, American companies or other multinationals?

ELIZABETH ECONOMY: I don't really know that they are more aggressive, necessarily. I think, frankly, what we have seen is this very fast rise over the past 10 years of Chinese outward expansion and search for resources as the Chinese economy has been growing at a rate of 9 to 10 percent per year, until very recently. Two years ago it dropped a little bit.

So I think there's this sense somehow that they are everywhere and doing everything in ways that are very different from what previous companies have done. But I think, with the exception of the different tools that I outlined at the outset, we find that Chinese companies, as Mike mentioned, behave in similar ways in terms of bringing resources online into the global market—sometimes not so much. For example, soybeans is different. What they bring online for soybeans, they take home. But I do think that this sense of China as this [Cookie Monster](#) of resources is somewhat overblown.

We also discovered, to our collective surprise, that when you look, for example, at China's investment in land overseas, it is the third-largest investor; it's not the first-largest investor. The largest is Canada, the second is the United States. If you look at its investment in Africa, it's the fourth-largest investor, after the EU and the United States, and I think Malaysia has now moved into third place.

So, again, the picture is much more nuanced, and we really need to look closely at what China is actually doing rather than simply accepting a lot of the hype that has surrounded its activities.

JOANNE MYERS: When you say you have to look at what they are actually doing, do you think they behave differently than other multinationals, like in Africa or in Latin America, in some ways? And how is that so?

ELIZABETH ECONOMY: I think in the governance areas, when we're talking about things like the environment or labor or corruption issues, transparency, certainly we see some differences. I think the easiest way to understand it is simply to look at the way that Chinese officials and Chinese businesses behave at home, because that's pretty much the way they behave when they go abroad. If they're not undertaking environmental impact assessments at home, which oftentimes they don't, they're not doing them in Zambia. Sometimes they are, but not as often as they might.

JOANNE MYERS: This leaves a trail of corruption and violations, which they—

ELIZABETH ECONOMY: Absolutely. And it's not just Africa. I think that's also important in our book. This is not all about China and Africa. That story has been exhaustively explored. But it's also China-Latin America, Southeast Asia. We even looked at the United States, Canada, and Australia to get a different set of comparisons to understand, does China behave differently in the advanced industrialized countries than the developing countries?

MICHAEL LEVI: I have to throw in a very short bit about Zambia and environmental impact assessments. I visited Zambia when we were working on this book. Someone told me about a Chinese company that had submitted an environmental impact assessment in Chinese, and it was

approved, despite the fact that no one in the environmental ministry in Zambia spoke Chinese.

One of the beliefs that's out there when it comes to how Chinese companies approach investment is that they are directed by the state, that they are called up and told, "You do this, that, and the other." No. Occasionally they are called up and told, "You do this, that, and the other." Sometimes they listen; sometimes they don't. But the more powerful direction that comes from the state comes through a set of incentives that is set up that encourages them more broadly.

A policy decision can be made to provide lower-cost financing—and Liz talked about that early on—if you are investing in priority areas. Once you do that, you don't need to tell a CEO to go after this particular resource. Their desire to turn a profit will direct them toward the places where they can do better because of that financing edge.

You don't need to tell a CEO who aspires to be promoted to a minister post in the government—remember, these are people who are part of a political system—that while they're out trying to make their profit, they should also be trying to rack up gains on the fronts that top Chinese political leaders are saying are priorities.

These are the more subtle ways that the Chinese state influences behaviors of these companies, but I think they are frequently the more powerful ones.

JOANNE MYERS: And do you think, then, that Chinese learn things from the countries they're investing in that they bring back home? How has that changed internally China's domestic policy?

MICHAEL LEVI: The first place I actually look for China taking lessons from abroad back home is not on the political front. We tend to look only for the politics and the governance, but the first place you see them taking lessons home is on the technical and managerial fronts.

Let's talk about oil for a moment. When China goes out to invest in oil, Chinese companies are trying to put reserves on their books, just like any Western company would, but they are also trying to partner with Western firms that have technical skills and management skills that the Chinese companies themselves don't have that they would like to apply, not only around the world, but within China itself. So you see, for example, Chinese companies taking minority stakes in joint ventures for tidal and shale gas acreage in the United States. They're not going to ship that gas back to China. They're not going to ship that oil back to China.

These are pretty minor stakes. They aren't going to transform the bottom line for these companies. But what they hope to learn through this is how you choose where to drill a shale gas well, how you manage the service company that brings the fracking expertise and the land and the water, and put all the pieces together, so they can go and try to apply those back in China.

To me, that's the first place where China is bringing back lessons from abroad—not political, not governance, but just how to do business more effectively and maximize their own domestic output.

ELIZABETH ECONOMY: I think on the political and governance side, they are beginning to learn the lessons from foreign multinationals, from pressure from host governments and host NGOs. But it's a much slower process than the one that Mike described on the technical and managerial side.

But we are seeing learning by Chinese companies, and sometimes they learn from each other. For example, in Peru there was a particularly egregious case of environmental and labor malfeasance by an early entrant into the mining area, by Shougang Hierro Perú, in the early, mid-1990s. But if you

look over the past two decades or so, you can see that the later entrants from the Chinese mining industry have really begun to learn from the negative example of that one company, and they are beginning to undertake environmental impact assessments. They are considering, when they are relocating the people to develop the infrastructure surrounding a mine, where these people want to live and how they want to live. They want single-family homes. They don't want to be put into multi-family dwellings with bunk beds.

Whatever it may be, they're beginning to understand how to practice better corporate social responsibility. They will hire a local CEO or a Western company to advise them on how to manage community relations.

So we are seeing some of that learning, but it is a slow process, a slow uptake.

JOANNE MYERS: Better to go forward, I guess, than to go backwards in some way.

ELIZABETH ECONOMY: Absolutely.

JOANNE MYERS: Just to change directions a little bit, you have a substantial section in your book devoted to security consequences, such as the need to secure shipping lines and trade routes and pipelines. Could you talk a little bit about that? Other than the [tensions](#) that we have seen in the East China Sea between China and Japan, what do you see as other flashpoints?

MICHAEL LEVI: There are a host of different places where the security world collides with China's resource quest. One of the ones that we talk about a lot is the impact that China's pursuit of resources has on its behavior in multilateral diplomacy around some big, global security challenges. Take, for example, efforts to put sanctions on Iran in order to get it to stand down or slow down its [nuclear program](#).

One of the big worries that the West had when putting sanctions, not on the Iranian oil sales, but on investment in Iranian oil and gas, was that the Chinese would just come in and take over where any Western firm had exited. The Chinese certainly had the desire to do that in several cases. But we have learned a few things from the experience.

First, even where China has wanted to step in, there have been a lot of cases where, because they didn't have the right access to Western technology or Western partners, they couldn't actually substitute effectively. The technical capacity often still lies in the West, which constrains China's ability, and even if they want to do something, they can't necessarily execute.

That drills home a broader point, which is that we should be looking at least as much at their capabilities as their intentions if we want to know what's going to happen in the world.

Another data point with Iran: During some of the discussions about China possibly stepping in and replacing Western companies in Iran, there were also Chinese companies that wanted to come and invest in the United States, in U.S. resource development. While we, in theory, have an open policy toward foreign investment, there's very little question that signals were sent to these Chinese companies and to the Chinese government that their attempts to invest in the United States might be looked upon less favorably if they were also stepping in and investing in Iran.

So they needed to ask themselves, not just a question about global strategy, but a question about their bottom line. What was more important to their futures as companies, investing in a cutting-edge technological opportunity in the United States or in these particular fields in Iran? Again, you can't

nail this down. This isn't conducted all in the open. But there are a lot of signs and a lot of stories that this influenced the Chinese companies to choose to invest in the United States rather than go into Iran and undermine the sanctions.

This is one place where we see that, yes, there's the potential for China to undermine some of the global security architecture, but in reality it turns out that the West has more leverage than we sometimes think.

JOANNE MYERS: But also when they were investing in the Sudanese oil fields and then the rebels started attacking, that had to bring China into Sudanese politics. Do you want to say something about that?

ELIZABETH ECONOMY: Right, that was part of what brought them into Sudanese politics. The pressure from the West certainly was a big part of that as well. And, frankly, the Chinese population, the public, has become much more concerned about the Chinese government's ability to protect its people abroad. This is, frankly, a new pressure that Beijing and the state-owned enterprises are facing, the demand from the Chinese people that the government keep the people overseas safe. This was an issue in Sudan. It became an issue in Libya, exactly.

So I think there are all sorts of pressures now being exerted on the Chinese government that say, "You have this traditional mantra that we don't mix business with politics"—even on the face of it, that, of course, is not true—but now we're seeing the Chinese people themselves say, "This is not acceptable to us."

JOANNE MYERS: And do you think that will in some way lessen their interest or their pursuit in going further abroad? Will they think twice about it before they go now?

ELIZABETH ECONOMY: I think it's at a transition phase. I don't know that we have hit the inflexion point. I think there is a lot of discussion and debate within Chinese society, certainly in academic circles and, I'm sure, policy circles as well. But I don't think a determination has been made that they are going to change their policy. In fact, the most recent statement from President Xi Jinping is very much along the lines of "we don't mix business with politics."

MICHAEL LEVI: I think we also need to remember that the opportunities for China to go in, particularly alone, are often in these places that are screwed up, for lack of a better term, precisely because they are screwed up.

We conflate two kinds of risk. When you look at Sudan, this seems like the Wild West; this is pioneering. It's actually not pioneering when it comes to oil exploration. This is a place that was extensively worked in by Western firms. They got out because this was an untenable situation. So China came in. They took a big political risk and a big security risk. They weren't taking big technical risks and, at some level, they weren't taking enormous business risks. So they were able to come in, despite their relatively low level of technical capacity, and put reserves on their books and produce oil and really deliver on their big goals.

Despite the fact that these companies are improving, they are learning, there is still a limited set of places where they are the most powerful bidder and where they can really come in by themselves, without anyone else, and win. Often those are going to be places that are pretty sketchy.

JOANNE MYERS: Before we open this up to you, the audience, I just want to know if you were surprised by anything in your research. You have been, I guess, to Asia, Africa, and Latin America.

What surprised you the most?

ELIZABETH ECONOMY: I think there were a number of things that surprised us. Maybe I'll say one or two and then Mike will offer his own as well.

One thing that surprised me was that, really, China's rise and its search for resources is not unprecedented. It's not unprecedented in history—because you can look all the way back to ancient Athens and see that it went out to secure resources from outside its own borders, and certainly up through the United States, and Japan is our most recent example. Even in the early 1970s, Japan commanded 10 percent of global, world oil consumption. That is just about what China commands today. China is about 11 to 12 percent. We really don't tend to think of these kinds of parallels.

And it's not unprecedented in terms of China's own history. Looking back at least as early as the [Ming](#), but even before that, you see that China had to look beyond its borders. Sometimes it pushed to acquire land from outside its borders because its own arable land was becoming degraded. It had a very strong central government-directed sense of investment abroad. It controlled who could participate in the resource trade. It controlled where they went for the resources. It controlled how much money people could earn from the resource trade. That same sense of state-directed investment continues today, although I think one of the things we found is that it's much more fragmented than we anticipated.

And that will be my second point, which is that Beijing is not quite the puppet master that we assume. I think Mike alluded to this. Yes, it certainly exerts a degree of control over its state-owned enterprises, through its ability, frankly, to remove the heads of state-owned enterprises. These are people that, if they don't do a good job in the eyes of Beijing, they can take them out. They can fire them, basically.

But there are also an enormous number of non-state actors, particularly in mining. Each one of these resources has a different makeup; the industry is made up differently. Two-thirds of the mining sector, smaller-scale industries—they are going out as well. In many instances, Beijing doesn't want them to be going out. Having to deal with, for example, 4,000 to 5,000 Chinese miners in Ghana that the Ghanaian government just [kicked out](#) last July—illegal Chinese miners—Beijing doesn't want to have to deal with this kind of political problem.

So I think, for me, two of the surprises are that first, that this is not the first time this has happened in history, that there are these strong lines of continuity in terms of China's own history, and that, again, Beijing doesn't really control, in many respects, as much as we think it does.

JOANNE MYERS: It's not as extensive as we would think it was. When you read in the newspapers that they are just all over the place, they are just leaving nothing in their wake for anyone else, they're grabbing everything—

ELIZABETH ECONOMY: They are all over the place. Don't misunderstand. You can look in pretty much any country and you will find that the Chinese are there. But again, you can look at the numbers and the relative levels of investment and find out that they are not the number-one investor in most of these areas.

MICHAEL LEVI: It shouldn't have been a surprise, in retrospect, but in a lot of places where you see very strong reactions to Chinese activity around natural resources, when you dig deep, it's actually other things that are driving the reaction. Because they are pursuing resources all over the place, it looks like one is driving the other.

You go to various places in Africa and you ask people about the resources. They will talk about that, but what they're really upset about is Chinese workers in the markets, Chinese workers on infrastructure projects, Chinese goods coming in—all of these. That coincides with resource investment, but when push really comes to shove, it's those other pieces that are really driving a lot of the concern.

A second piece that struck me as interesting was when we looked at Australia. In the United States we have this sort of assumption that advanced economies have open regimes for trade and investment. Sometimes we'll block things for national security reasons, but otherwise we let it in. In Australia there is occasionally a calculation that involves reciprocal market access, which is very different—you see in the political debates over allowing investment, let's say, in iron ore, some people say, "Well, if we allow investment in iron ore in this country, we'll get more access for steel into China."

So there's a different kind of calculation that happens in some of the advanced economies.

Let me throw in a third thing that I found surprising. One of the great things about co-authoring a book is that you don't only learn from your own reading and from going out around the world; you learn from your co-author. One of the things I learned was about how much is happening from civil society within China to actually influence what some of these companies are doing. Pressure from Chinese NGOs that go and look at what's happening around the world and then try to put social and political pressure on the companies back in China to perform better—not the kind of thing you instinctively think about, if you're not deeply immersed in China, when you imagine how Chinese political and social change happens, but a real reality in this space.

Questions

QUESTION: Don Simmons.

Your colloquy is very interesting. One of the things that has been happening in China in recent years is the significant increase in labor costs. In the shipbuilding industry, with which I'm familiar, the average cost per hour of labor, including white-collar, was about \$2.50 in the year 2000. In 2012, it had grown to around \$13.

Are these trends prevalent throughout the Chinese economy? Do you think they will continue? And what do they portend?

ELIZABETH ECONOMY: I think this is the beginning of a potential trend. There are still, of course, hundreds of millions of Chinese living in poverty and migrant workers who are not making anything close to \$13 an hour. What you're talking about is a phenomenon of much of the coastal part of the country, but not really of the inland, and certainly not of the far west or southwest.

From the work that we're doing, it still pays for tens of thousands, hundreds of thousands of Chinese to go to Ghana, to be an illegal miner in Ghana, as opposed to trying to get work in Guangdong province, even. For the uneducated, unskilled Chinese, the opportunities are greater, in many respects, going abroad into this kind of work than staying at home.

So I think there is a phenomenon, absolutely. In manufacturing you see it. In shipbuilding and several industries, wages are going up. But there still is a vast reserve of unskilled and largely unemployed labor that's seeking to go out.

QUESTION: Carol Spomer.

Can you enunciate what you consider to be the five most critical resources China is questing after today? As a corollary, how about water? I haven't heard you mention that.

MICHAEL LEVI: Water is one of those five—I don't know that we have a ranking. I'll give a handful off the top of my head.

You can rank them in two different ways: critical to China and critical to the rest of the world. Certainly oil overlaps both. Oil is critical to economies around the world and is critical to the Chinese economy as well.

Water is absolutely critical to the Chinese economy. It's critical to others as well, but because water isn't traded in the same way that a commodity like oil is, the spillover effects from what China is doing are more localized—still international, but more localized.

Iron ore is a place where that's going to affect particularly developing economies. That's where you need a ton of steel production, where you are building out new infrastructure. But for a country like the United States that is actually a net iron ore exporter, China driving up the prices is not really a dangerous thing.

Food is a fourth big place where you have large global consequences. But to come back to an earlier point, it's one where it's an extraordinarily important resource that China is focused intently on producing and is consuming ravenously, but it's also one where so many other countries are big players in grown consumption and where so many other factors are influencing prices that maybe China isn't so decisive there as in other places.

QUESTION: Matthew Olson.

I think you alluded tangentially to the tendency of the Chinese to bring in their own labor force in exploiting some of these natural resources, which reminded me of the fairly extensive coverage of the labor problems in Zambia, in the copper mines, where people were [shot](#).

All of that sort of died away, but I continue to see little paragraphs once in a while that say that this labor problem with the Chinese and the indigenous population, especially in Africa, is difficult. Please comment on that.

ELIZABETH ECONOMY: I think, as Mike suggested, one of the things that stokes the most nationalism and negative sense of the Chinese resource quest is the export of the Chinese labor. But as he also mentioned, oftentimes it's not actually focused on the resource itself, but rather on the infrastructure or on Chinese selling goods in the markets. It could be small-scale Chinese farmers that are developing their plots to feed the newly growing Chinese economy.

But in some cases it is, in fact, the Chinese labor in the Chinese mines. Absolutely, in Zambia there have been several cases, in fact, of violence, in different mines. There have been problems in Peru with violence, ongoing [strikes](#) related to Chinese workers, Chinese managers, workplace frictions, the failure of Chinese managers to be able to communicate, simply. Frankly, they don't speak the native language. They don't speak English. And their way of dealing with local labor is problematic.

Some states with slightly stronger capacity, like Mongolia, for example, have developed regulations that say, if you want to bring in a Chinese miner, you have to hire nine Mongolian miners to make up

for that. I spoke with a quite senior Mongolian official who said, "The Chinese are going to come whether we want them to or not. It's my job to figure out how to protect the Mongolian people." So Mongolia has instituted a range of different policies to try to limit the number of Chinese that come into Mongolia.

I think the labor issue is a very significant one, particularly just in terms of that nationalistic response and the sense that these are valuable jobs in a lot of these communities, and people don't anticipate that when the Chinese announce a major new investment, the jobs are then going to go to the Chinese themselves.

So I think that's part of the problem.

The last point I'll make is that, especially early on, the Chinese used to build into their contracts—for example, in Angola, for the infrastructure part, they would say 70 percent of the labor needs to be Chinese. "So we're loaning you the money, but, by the way, the machinery and the people and everything else are going to be Chinese."

I think that's going to change as the capacity of the host of the resource-rich countries increases.

QUESTION: Robert Shaw.

I want to ask you about Chinese government official policy on self-sufficiency in certain commodities as an aspiration. There was an article yesterday in the *Financial Times* about agriculture, saying that they are shedding even an official stance about self-sufficiency. One of the arguments that's going on at the moment in iron ore is that even though there may be less fixed-asset investment, and therefore less iron ore needed for new construction, the amount of iron ore being imported will still increase because of the relative inefficiency of the Chinese mines compared to those in Brazil and Australia.

To what extent do you see now a much more declared policy that we will no longer allocate resources to preserving inefficient production locally on commodities?

ELIZABETH ECONOMY: On the agricultural front, it's very interesting. What they are doing is actually not declaring that they are not pursuing self-sufficiency, that this is not still an objective of the Chinese government. They have not changed their policy. What they are doing is lowering the bar for the self-sufficiency.

So it's a little bit of a shell game. They're saying, "It used to be that we needed 600 million tons of grain, but now it's going to be 550 million tons that will mean self-sufficiency."

It still is quite deeply ingrained in the Chinese psyche and core, the need for "resource security." Again, this dates back thousands of years, quite frankly, especially on the grain front. But I think that there is, particularly with this new leadership, a realization that they are going to have to become more dependent on international markets, and indeed it's not that scary.

But they're not ready to completely, at least on the grain sort of self-sufficiency, shed that deeply ingrained kind of philosophy.

MICHAEL LEVI: I think what you see is a pattern where the Chinese pursue self-sufficiency, but when it becomes clear that it's not possible, they quite quickly give up. You see it in oil. Not possible. Iron ore, not possible. And when you look at the domestic production side in response to that, I think

it's almost more useful to think of it simply as another piece of domestic economic promotion, rather than to see it as about some sort of pursuit of self-sufficiency, because they're not going to get close.

There are two places where I think you do have interesting distinctions. The first is, not even food broadly, but grain. They are willing to shed self-sufficiency in other kinds of foodstuffs, like soybeans, just to preserve this focus on grain, in part because of what Liz said—it goes back so far.

The other is actually natural gas. They are not self-sufficient, but they don't import a lot of natural gas. That's a case where, if they wanted to boost gas consumption enormously, they probably would have to become a lot more import-dependent. But they have substitutes that are available, particularly for gas and power generation in a lot of industries. They have coal as a substitute. It may be dirty and cause them a lot of other problems, but they have an option. So because they have an option of not being heavily import-dependent, they choose to take that. But there aren't a lot of places where you get to that point.

QUESTION: Bill Holstein.

I've been following these stories since 1979 as a young guy in Shenzhen.

You haven't talked about urbanization. The Chinese are going to move 200 million or 300 million people into cities in the coming years. That's going to have a huge impact on their consumption of materials from around the world. That is question one.

Question two is, if we're looking at this, where is the flashpoint going to come? As American policy people, where will be the testing point at which we say, "Ah, this has gone too far. This is threatening our interests"?

ELIZABETH ECONOMY: On the urbanization question, it's a really interesting one because I think there's this natural assumption, as we talk about China's rebalancing of its economy, moving away from an investment-led to a consumption-based economy, of which urbanization is an important part—the development of this much larger middle class, urban-based—there's this sort of assumption that, in fact, that's going to be a much less resource-intensive kind of world in China. But, in fact, it's going to be just a different kind of resource-intensive world.

First off, moving another 300 million to 400 million people will require continued investment in infrastructure, because they have not built up all the cities that they need or the highways or the railroads that they need to service all of these new cities. So I think that's one thing we have to bear in mind, that we're basically talking about urbanizing the entire population of China that has already been urbanized. We're doubling the urban population of China at this point. I think that's pretty significant.

I think the second part is that urban residents in China use three to four times more energy than rural residents do. Now, maybe they can use it differently; the energy mix will be different. But when we're looking at cars, China sold more cars last year than the United States did. That's going to be a lot more oil demand, unless they actually make a breakthrough with electric or hybrid, which they have yet to do.

So I think it's going to be important for us, as we think about China's resource quest, to look almost commodity by commodity at what that impact is going to be. Of course, everybody talks about the impact on food as incomes rise and China becomes more meat-consumption based, etc.

I think it will have a profound impact. I'm not sure we have fully laid out exactly what that impact is likely to be, and a lot of it is going to have to do with the other choices that China makes with regard to its economy. Does it begin to conserve its resources? Does it begin to use energy more efficiently? It has made some strides. Is it really going to move forward aggressively? Is it going to have more renewables?

I think a lot of other choices that China makes in terms of its future economic development path are also going to influence that resource use.

MICHAEL LEVI: I would only add that what drove up prices so quickly over the last decade wasn't a fundamental shortage of resources around the world, it was the sudden rapid rise that wasn't particularly anticipated, or at least not anticipated enough, on the supply side.

Now we are anticipating further growth in Chinese commodities demand, and supply is responding elsewhere. So it will take more than just the continued trend to drive prices up even further.

You asked about the flashpoints. I think we're actually hitting on one of them in this discussion. We tend to look for the place and the time and the particular thing that will happen. But the biggest security spillovers, in a way, from what's happening in China are also through the price of resources. We are much more worried about disruptions in the Middle East because the price of oil could double from \$100 to \$200 a barrel. It would be a lot less troubling if we were worried about it doubling from \$20 to \$40 a barrel, which is what the world looked like 15 years ago.

We are more concerned about the Iranian nuclear program, to go back to something we talked about earlier, because Iran has had strength derived from high resource prices.

That doesn't mean that we get to have a showdown with China and take out half their cars so that they have less oil demand. The response, in some ways, has to both be at home, in curbing our own consumption, both to take pressure off prices and to make ourselves more resilient, and also to work with China and others to curb their own demand so that we take some of that pressure off the financial system.

If you want to look for a place where there's a potential for genuinely hot conflict, it is probably in the sea lanes near China. But here, the critical thing is again to disentangle the resource piece from everything else. An enormous amount of the talk about conflicts in the [South](#) and East China seas is about the oil and gas resources there and the fishing resources. That's probably not the primary driver of a lot of the conflict there. Particularly the oil and gas resources are just not likely to be all that large.

But you do have one other piece that is resource-related, and that is security of the paths through which resources of all kinds travel. It doesn't matter how much oil is produced in Africa if you can't get it through these sea lanes and back to the demand centers. So there's competition to control those lanes through which resources pass, and there's just an enormous overlay of nationalism and sovereignty issues that go along with all of this that aren't driven by any particular underlying material concern about this resource or that one, but are driven by much more fundamental issues that aren't going away.

QUESTION: Thank you for an excellent conference. I'm Jean Ergas. I'm an adjunct faculty member at NYU, and I often comment on the Chinese situation in my global economics class at the graduate level.

There's a huge amount of talk right now about major trade agreements that are being discussed with the [Trans-Pacific Partnership](#). We have the trans-Atlantic agreement with the European Union. Hopefully in our lifetimes, we will see these actually concluded. Somebody said to me that what it's really about, the Trans-Pacific Partnership, is ABC: Anybody but China. That was a quite cute way of putting it.

Do you think that this resource aggressiveness, to a certain extent, is a China that is saying, "They are trying to, so to speak, push us in a corner. We are going to get those resources. We're going to become direct investors so that when these pacts are concluded, they cannot throw us out," and that this is basically a defensive maneuver and a self-sufficiency argument as well? This is something you keep hearing. I'm wondering, is there any basis to this?

ELIZABETH ECONOMY: I don't really think that China's outward quest for resources and the TPP, the Trans-Pacific Partnership, are that closely linked. I think if you look at the timeline of China's quest for resources, it traces back, as I mentioned, hundreds and hundreds of years, but I think, more recently, at least since 1999 or so, when Premier [Zhu Rongji](#) sort of formally announced a go-out strategy and recognized that China could not be self-sufficient in oil. That was what actually drove it to begin with.

So I don't think that those are linked. The TPP really didn't gain momentum until the past two to three years, with the beginning also of the whole U.S. rebound and pivot. I think there are two different types of phenomena occurring.

I also don't think the TPP is an anything-but-China trade pact. I understand why it is perceived that way by some, but I think it is supposed to be a higher-end trade agreement and one that China is more than welcome to join when its intellectual property rights and environment and labor practices, transparency, and corporate governance merit it. It should be, hopefully, aspirational.

An interesting thing that I think has come out in maybe the past year or so is that there are pretty significant pockets of people inside China—for example, the Ministry of Finance—that actively want to join the TPP and see it in many ways as the Chinese, back in the late 1990s, saw the World Trade Organization [WTO]: as an opportunity to bring external pressure to bear on domestic actors to force change.

So I think there is an element there where the TPP speaks to reform elements within China who understand that this is not, as you put it, ABC.

QUESTION: Michael Schmerin.

You commented that Chinese oil companies were taking minority positions in American exploration corporations. Is that in order to gain our technology? Are they able to bring their engineers and geologists, even though they have a minority position, to the American oilfields to learn fracking, etc.?

Two, we have had Chinese companies buying American corporations, such as our pork producer, [Smithfield Foods](#). When IBM shrank into just being a consulting company, Lenovo [took over](#) what, in essence, was their PC manufacturing. Was that an economic decision or was that to gain technology?

Also, what role does corporate espionage play in Chinese corporations making investments in Western companies?

MICHAEL LEVI: The Chinese learned in the 2000s that trying to take a majority or a full ownership stake in an American oil company was going to engender a lot of political resistance. This is another one of the many ways that China is learning and that the world's governance systems, particularly in a country like the United States, are pretty resilient. So they have gone and focused on these minority stakes. I'll come back to that in one moment.

More recently, they had one acquisition, this [acquisition](#) of Nexen, a Canadian-controlled company, but with assets all over the world, including in the Gulf of Mexico. That's a place where the U.S. review, as I understand it, focused on a small number of things, but among them, not just proximity to sensitive military installations, but a broader ability to use that as a platform for cyber-espionage.

So this is a continuing issue, not specific to the oil and gas space, but, because it's a technologically sophisticated space, it's one that people do worry about.

Are they getting access to technology? Yes. This is part of the deal. They are learning about the technology. It doesn't mean they're going to replicate it. It may mean they learn how to work with the service companies. It's important to remember that even the U.S. companies doing this development are typically hiring service companies to work for them. So when Sinochem goes and [does a deal](#) with Pioneer, it's not like Pioneer is an expert on fracking. They're hiring Halliburton or Schlumberger to do the fracking for them.

So there are a variety of different pieces.

What they are really getting out of the partnership is that management component, figuring out how to bring the different pieces together, which is very important in this space and, if you talk to people in the industry, far more scarce than any other piece of capacity that is brought to bear.

Are they successful in absorbing that? I think it's too early to tell, in part because there are a lot of other variables that intervene before these activities can be replicated in China. You talked specifically about shale gas and tidal oil development. Look, in China they have limitations on their resource. It's not as high-quality a resource as in the United States. They have resources that are very distant from population centers, so it's much expensive and requires new infrastructure to bring them to the centers.

To link it up to another question earlier, these activities, at least right now, the way they are done, are also very water-intensive, and the resources are in regions where there is domestic competition for water for various purposes, and the more water they use, the more water they extract from some of these places, the bigger international spillovers they are going to have to deal with. China is upstream of a lot of other countries in the region. It can make the decision to extract more water from these various shared resources, but, at a minimum, it has to cope with the political fallout downstream when others become intensely concerned with the consequences of what China is doing.

ELIZABETH ECONOMY: I think I would only add the non-resource side, because you made the point about the stealing of technology or the espionage and whether they are just getting our technology.

I think we have a pretty robust [CFIUS](#) [Committee on Foreign Investment in the United States] review process. That's what Mike was mentioning when he said that in the early 2000s, CNOOC learned you're not going to take an entire U.S. oil company and just buy it wholesale. So I feel reasonably comfortable that when the Chinese companies are coming in—you know, Wanda's [taking](#)

over AMC theaters—or when you have an injection of capital from a Chinese company into an American one, the U.S. government is very highly sensitive to the issue of technology transfer and to the issue of what's considered to be something like rare earths investment, things that we don't want to sell to the Chinese.

So while I think it is an issue, and it's an issue that's going to come up more and more frequently, and it's probably an area where the U.S. government is going to need to become a little bit more transparent in terms of what the considerations are in a CFIUS review, because we're going to have, I think, many more Chinese companies coming to the United States looking to buy the full range of assets—we have them coming now in agriculture. There was just an article in the Chinese media talking about the enormous attraction of U.S. land, not only because it's fertile, but because of U.S. technology, agricultural technology. The Chinese Academy of Sciences did a study that said they are 108 years—I don't know how they came up exactly with that number—108 years behind the United States in agricultural technology.

So there's a lot of incentive for them to come in, as Mike was talking about in the energy field, and buy into the agricultural arena as well.

I think we have in place a system that is pretty good at ferreting out what should be open for sale and what shouldn't be.

QUESTION: Philip Wolfson. Thank you for the informative talk.

Ms. Economy, your point just now about our natural advantages that we might have, say, in agriculture vis-à-vis the Chinese—I was thinking before, where we seem to be at a disadvantage in negotiations with them and, across the board, seem to be on the defensive and back on our heels so much of the time. They own a lot of our debt. They engage in unfair trade practices, manipulating exchange rates and so forth—all of this stuff. Whereas the Australians maybe are playing hardball, insisting on reciprocation a little bit more than we have, I'm wondering whether you would think that we're not playing to our advantages enough against the Chinese.

The other thing that you said early on about the fragmentation, which, frankly, I was surprised to hear had advanced that much—it used to be monolithic, state-driven, everything with the full force of the government behind Chinese. Now it's becoming more capitalistic, more fragmented—whether that, in a sense, good news/bad news might play to our advantage ultimately, too.

ELIZABETH ECONOMY: In terms of the second point about whether the fragmentation plays to our advantage or not, it remains to be seen. It is easier to negotiate, at some level, with a central government. For example, to tie together the two questions, right now we're in the midst of negotiating a bilateral investment treaty. This has been ongoing for a number of years, but it's something that has recently received new impetus. It's something that our secretary of state is actually going to push on the trip that he's making right now.

I think that's an important way of leveling the playing field. We're dealing with Beijing, with that central government, and putting in place a set of regulations that the Chinese government is agreeing to, that its firms are supposed to adhere to.

I think we found in the World Trade Organization that the Chinese government can adhere to things and the Chinese companies may not abide by them. But there is an adjudication process. I think that's the strength of the bilateral investment treaty, that you have an agreement that both sides are supposed to adhere to and mechanisms for adjudicating or taking each other to court in some form.

So I put my hope, quite frankly, in moving forward with these kinds of agreements, because I think that is the best way of leveling the playing field.

As far as the Chinese buying our debt, that serves our purpose as well. Frankly, the Japanese are just a little bit behind them in terms of purchase of our debt. So that doesn't tend to get me as agitated as it does many people. I tend to see it as kind of a mutually assured destruction system, too. They're not going to go and sell it all off at once, because that's going to hurt them. So I'm not so worried about that.

Other issues—IP theft and things, I am worried about, and I do think it puts us at a disadvantage. It's something that our companies have to pay an enormous amount of attention to. While the Chinese say they are getting better, I think it's still a huge problem.

QUESTION: Linda Richards.

If we take the title of your book and some of the things that have happened recently with the [nine-dotted line](#) claim, the Japanese, etc., if the economic plays that you have been talking about cease to work, and given our relationship with Japan and the Philippines, do we have a military component that's going to start to move into this area?

ELIZABETH ECONOMY: I think the rebalance to Asia was, first and foremost, just that. It sort of expanded to encompass the Trans-Pacific Partnership and other issues of good governance, and the United States is going to help with the Mekong River and other kinds of issues. But it really was, frankly, primarily a response to the concerns of the region about rising Chinese assertiveness on the military front and the security front.

So the U.S. response was, to begin with, a military one. It was the rotation of more troops through in Australia. There has been a pretty dramatic ramping-up, not only in terms of U.S. multilateral exercises and talk of the importance of the security alliance and treaty with Japan, but also security relationships among the countries in the region. I think that's one of the most important, and potentially under-examined, aspects of what has happened in terms of China's rise in the region, that the other nations in the region—Vietnam, India, and Japan—undertake their own military cooperation, training, and exercises. Australia gets involved with them. There's a whole new dimension that's emerging that, in some ways, is not completely dependent on the United States, although we clearly are the most dominant force.

But I think certainly that's ever-present in this discussion.

MICHAEL LEVI: The only thing I would add is that, to the extent that people think of this rebalancing or pivot, or whatever it is, as a move from the Middle East to Asia, the resource lens suggests that that is an unwise tack to take. If one of the big concerns of American allies and friends in the region is access to stable resources, and particularly to stable energy supplies, leaving something of an American vacuum in the Middle East to be eventually filled by China as it gains capability certainly would not accomplish that end.

So even though the focus is on security in Asia, the security needs of Asia extend well beyond the immediate region.

JOANNE MYERS: Well, as we all pivot out of the auditorium, I want to tell you that *By All Means Necessary* is not only for policymakers and business leaders, but it's for anyone interested in China.

I thank you both for really giving us a wonderful discussion on these issues.

Audio

As China's urban middle class expands, China's government--and private companies--are traveling the globe in pursuit of fuel, ores, water, and farmland. And the government has all kinds of tools to bring to bear, from public diplomacy and backroom deals, to low-cost financing and low-cost labor. How is this quest changing the world, including China itself?

Video Clip

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