

Free trade deal opens possibilities for greater Chinese investment in Australian rare earths sector

✘ China and Australia, after years of negotiations, have reached a free trade agreement (FTA) after the G20 meeting in Brisbane on the occasion of the visit to Australia by Chinese President Xi Jinping. The FTA further strengthens already deep economic relations between the two countries. The agreement allows for pricing changes that will benefit farmers, growers and other service companies in Australia while allowing Beijing greater investment access in Australian companies and its workers easier access to the labor market. Australian agricultural products such as rice, milk and dairy products, wool, cotton, and 40 services including health, social security and legal services will be the first to benefit. Meanwhile, Chinese enterprises will be able to invest one billion Australian dollars up from the previous ceiling of AUD\$ 248 million – agricultural land remains the exception with a threshold of AUD\$ 515 million. The Australian Trade Minister, Andrew Robb, on the sidelines of the press said that once fully operational the agreement will include 99.9% of Australian exports.

China is already the most important trading partner for many economies in the Asia-Pacific and swallows up their raw materials. In the case of Australia, there are immense quantities of iron ore and coal and even rare earths of course. Last year, China took on nearly 40 percent of all Australian exports, particularly natural resources. This makes China the largest trading partner of the resource-rich nation. The volume of Australian exports of goods and services toward China has surpassed the AUD\$ 100 billion mark in 2013

according to the Australian Bureau of Statistics. Therefore, China now accounts for nearly a third of the volume of Australian exports of goods and services and accounts for a much larger slice of that trade than the next highest countries including runner-up Japan (AUD\$ 50 billion), South Korea (AUD\$ 21 billion), the United States (AUD\$ 16 billion) and India (AUD\$ 11 billion). Moreover, also in 2013, the volume of trade in both directions between the two countries reached AUD\$ 151 billion or 20 percent more than 2012.

Australia and India are targeting a similar agreement, designed to spur trade between the two countries, which in both cases will be helping Australian exporters of mining products, thanks to the immediate reduction of tariffs on copper, zinc, and the majority of aluminum based products. Ironically, the Australian Government's hope is for the free trade deal to open up new economic sectors, as a means to reduce its dependence on the mining sector, and 'green tech' in particular. In this respect Australian and Chinese companies have already secured important partnerships. Arafura Resources ('Arafura', ASX: ARU) is one of Australia's fastest-growing rare earths developers and it has secured Chinese technological and financial backing for its Nolans Rare Earths Project. The Nolans Rare Earths Project, a world-class rare earths resource grading 2.6% rare earth oxides ("REO") according to Arafura's 'Nolans Development Report (NDR)'.

Chinese magnet producers are very interested in Arafura's Nolan Project, which is not surprising given its (20%) neodymium and praseodymium content – two of the main materials used to make magnets. Given China's dominant position in the rare earths sector, is a very welcome and surprising prospect. Arafura's uniqueness stems from the composition of its resource, which as stated above, features 25-26% magnet feed materials, accounting by themselves to some 70-77% of its potential revenues. The growth in demand growth for NdPr Oxide is expected to lead to supply shortages in the next decade,

prompting a faster price appreciation than other rare earths. Arafura has worked closely with Chinese experts to accelerate the path to production and de-risk the Project. The East China Mineral Exploration and Development Bureau (ECE) has helped Arafura achieve project optimization thanks to a careful and review of capital and operating costs, which will maximize the savings achieved thanks to an ambitious cost cutting plan. ECE holds a strategic equity holding of 24.86% in Arafura, enabling Arafura to avoid having to dilute the share price while continuing to work on its own innovative rare earth extraction process. The much higher investment threshold for Chinese Companies also open up possibilities for Chinese investment in Lynas Corp (ASX: LYC). Chinese rare earth producers would gain from Lynas's highly advanced and environmentally superior processing facility. In the past, Australian politics have interfered in a deal involving China, Lynas and/or the Mt. Weld rare earth mines.

There had been some concerns over the status of Australian-Chinese relations and their potential deterioration. While, military and international diplomatic cooperation has suffered over Prime Minister Tony Abbott's stance against China's ally Russia, economic cooperation is actually flourishing. Beijing is currently doing its best to challenge the influence of the United States in the Asia-Pacific region and aims to establish itself as Asia's dominant economic and military power. The Free-Trade deal with Australia (that reached an impasse lasting almost a decade because of some contentious issues) will accelerate this strategic objective. Australia remains a close political and military ally of the US, but the growing wealth of the Chinese people, makes China an increasingly important engine for economic growth in Australia. China's demand for raw materials actually managed to prevent Australia from experiencing a recession in the wake of the 2008 global financial crisis.

Hong Kong's student protests scare Beijing

✘ Some have described it a “Little Tiananmen” but the leaders of ‘Occupy Central’ have a clearer notion of what they want to achieve than their Chinese cousins in 1989. This is because, unlike the citizens of the People’s Republic of China, the inhabitants of Honk Kong know what freedom, democracy, and rule of Law mean. This means that they are prepared to endure any sacrifice to convince Beijing to listen to their demands. Predictably, nobody in Beijing is going to listen, much less go along with them. The protests intensified over the past weekend and they have waned somewhat on Monday; however, the movement will not be dissolved by mere the police’s tear gas. Furthermore, should the protests continue, intensify and lead to the police being forced to using arms, there is no telling what ripple effects it could have in the heart of the Chinese mainland, where social conditions and, paradoxically, the emergence of middle class in the urban areas, might well respond in tune with Hong Kong’s students. Beijing is facing a significant challenge and it will have to address it with finesse.

In 1997, Hong Kong changed status from being a British colony to a Special Administrative Region; the architects of the transformation were UK Prime Minister Margaret Thatcher and Chinese Premier Deng Xiaoping. The former colony has always lived with the idea of being special, free and independent. Hong Kong and China have always had a special relationship but the city’s streets have always feared the possibility of a sudden invasion from the mainland. Many Hong Kong residents actually fled in 1997 because they were convinced that Beijing would impose its own political customs to the island, crushing

freedom and independence, including through violence if necessary. Well, looking at what's going on in the streets of Hong Kong today, with police charging the barricades constructed by the students and their professors, one might call it a delayed reaction. The city-state cannot help but fear the worst, because the situation has the potential for exacerbating out of hand.

Hong Kong will become to all intents and purposes Chinese in 2047; however, the students have taken to the streets now because they fear that China is fully ready to take over now. They have read the signs, which include Beijing's lifting of freedom of the press to the imposition of higher education curricula and the appointment of the gubernatorial candidates, who would be allowed to campaign to run the Island. In other words, the Communist Party will choose who can and cannot run for power in Hong Kong. The 'democratic candidates' will be chosen by the Executive Committee of China, effectively rendering the entire electoral process, pointless. Surely, Beijing has imposed too much too soon even if Hong Kong has lived under the illusion that it could remain "special".

Universal history has taught that when the dialogue degenerates into struggle, it is difficult to keep the situation under control and under reason. The fear is that, with neither side willing to give in, this very difficult confrontation could escalate and do so suddenly. China, however, is acting rationally because it worries that the democratic wind from Hong Kong could easily reach the island of Macao – just a few dozen kilometers away – and then hit the Mainland, threatening the power of the Communist Party itself. The students, for their part, have excellent timing. President Obama and western nations have spoken about democracy and freedom at length throughout the duration of the UN General Assembly over the past week and throughout the Ukrainian crisis that has intensified since last January. Beijing clearly fears the inevitable moral support for the protesters

in Hong Kong from the British, the former colonial rulers, and from Washington. The Chinese government has, in fact warned the United States and other foreign nations, not to interfere in Hong Kong's internal affairs of Hong Kong, stressing that it is a Chinese internal matter. Ignoring the appeals of the Hong Kong and Chinese Government, thousands of people have stayed in the streets to protest. Braving the risk of bursts of tear gas and batons, thousands of protesters continued their protests over the weekend.

The protesters have chosen the umbrella as their symbol, given its ability to protect from the scorching sun and from tear gas such that in social media, the Hong Kong protest has already earned the title of the umbrella revolution". The student protesters also remind observers of 'Occupy Wall Street', the protest movement that began in the United States on September 17, 2011 in an effort to block New York's financial centre. In fact, the students have blocked the financial center of Hong Kong. 'Occupy Central', the name of the Hong Kong protest, has a founder, Benny Tai Yiu-ting, Associate Professor of Law at the University of Hong Kong, who started the civil disobedience movement in January of 2013. Tai Yiu-ting has been careful to keep the protest focused on Hong Kong rather than try to appeal to the West and its regional allies; however, Taiwan has already expressed its support to the people of Hong Kong. Some Taiwanese students have exhibited signs that read "Today, Hong Kong, Taiwan tomorrow", expressing the hope, therefore, that the island of Formosa can finally get rid of Beijing.

The protests in Hong Kong come at a time of tension in the East China Sea with Japan and the South China Sea with Vietnam and other regional powers. However, the repercussions will be more economic than geopolitical at first. Hong Kong serves as the financial link between China and the world. Should the protests turn into a sustained political movement the resulting turmoil will have deep economic repercussions. While

the students have expressed concern over freedom, democracy and human rights, Hong Kong's business leaders, care more about stability and their wealth. They have accused the students of damaging Hong Kong, threatening its wealth. The financial markets have reacted in tune with the business leaders' concerns, as shares took a bearish turn. Ironically, Beijing, which has celebrated China's 'conquest' of Wall Street as Alibaba (NYSE: BABA), amid concerns of lower economic growth, scored the largest ever IPO, will side with the business elite rather than the idealistic students. Karl Marx is surely rolling in the grave. The students can leverage the economic concerns on both sides because a compromise may be the only solution that would ensure business stability and China's long term full absorption of Hong Kong, averting a wider national and international crisis – and its inevitable economic effects.