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Opinion

Australia's critical minerals strategy needs more economic reality and less geopolitical wishful thinking

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Canberra is copping heat over its critical minerals strategy.

This is the sector that Treasurer Jim Chalmers, has described as the 'generational, defining opportunity for our country ... one we cannot afford to miss'.

But a new report by the Australian Strategic Policy Institute (ASPI) says that the Albanese government's critical minerals strategy sells 'Australia and its allies short'.

This is because it puts too much emphasis on 'domestic production' and 'outbound supply chains' (that is, Australian exports), and not enough on 'how it contributes to building supply chains from other nations'. The ASPI report exhorts the government to work more closely with its seven 'strategic supply chain partners': the US, the EU, Britain, Japan, South Korea, Canada and India.

In the government's critical minerals strategy, these are termed 'like-minded partners'. China is notably absent from the list.

There are good reasons to be sceptical of the government's recent embrace of a Made in Australia mantra, particularly when taxpayer funds are used to stand up projects, critical minerals-related or otherwise, without a clear explanation of how they might become internationally competitive and self-sustaining.

But the criticism that Australia is not delivering as an ally and a strategic partner is misplaced. In fact, the evidence points in precisely the opposite direction: it's Australia that's being sold short.

With a population of just 25 million, no investors, domestic or foreign, will set up shop with a motivation of supplying the local market. Australia's limited manufacturing ecosystem also means that being a competitive producer in any commodified space is delusional. The US manufacturing sector is 27 times larger than Australia's. And China's is double that of the US.

These economic realities rule out Australia emerging as a production hub of, for example, electric vehicles (EVs). Even batteries for EVs are a dubious proposition.

Australia's contribution to resilient critical minerals supply chains will inevitably be concentrated upstream at the mine site where it has a clear comparative advantage, or perhaps one or two steps downstream, such as minerals processing.

Niche manufacturing that leverages R&D to build competitive advantage and feeds into global supply chains is also in the realm of economic reality.

And upstream, Australia is delivering in spades. As the ASPI report acknowledges, ‘Australia’s domestic critical minerals sector, measured by exploration investment, reserves and capital expenditure, is the largest of any nation outside China.’

The real problem is that Australia’s strategic partners aren’t delivering on their end of the supply chain further downstream.

Any viable Australian critical minerals project must first and foremost have a market to sell to.

The irony is that the market most responsible for driving the development of Australia’s critical minerals sector is China’s.

Consider lightly processed lithium spodumene, Australia’s most valuable critical mineral export in 2023, worth $US13.3bn ($20.5bn). Nearly all of it goes to China. This doesn’t reflect strategic laziness, much less duplicity. While China’s total purchases of lithium spodumene last year stood at $US15.8bn, Australia’s strategic partners imported just $US1.1bn collectively.

It has been rocketing Chinese demand that has allowed Australia to nearly triple the volume of lithium spodumene it supplies to global markets compared with just four years ago.

In 2023, US imports were 36 percent less than in 2019. In part this reflects a spluttering energy transition, despite the Inflation Reduction Act (IRA).

Last year, sales of EVs in the US were just one-fifth the volume in China.

And despite coming off a much larger base, in the first quarter of this year EV sales in China rose by another 15 percent, year on year, compared with just 2.6 percent in the US.

Australia’s strategic partners are also not shy about wanting to ‘onshore’ rather than ‘friend-shore’ their critical minerals supply chains. Rather than relying on Australia to meet its future lithium demand, last month the US Department of Energy announced a $US2.3bn loan to develop lithium reserves in Nevada with the intent to ‘secure reliable, sustainable domestic supply chains for critical minerals’.

Apart from lithium, Australia is now also the world’s fourth-largest producer of rare earths. Off-take agreements with Chinese importers have been vital in getting projects off the ground that don’t rely on taxpayer support.

But as investment analyst Kingsley Jones has noted, the hope that the American market might become a major customer for Australia-based rare earths mines is likely to be misplaced. US production is already 2.5 times that of Australia, and owing to a lack of domestic demand nearly all of it is exported.

Even Australia’s Lynas, which proudly touts its ‘ex-China’ supplier credentials, relies on China for around one-third of the sales from its Malaysian rare earths processing facility.

Lured by US government funding, Lynas is also setting up a downstream rare earths’ separation facility in Texas.

So, it turns out the Albanese government’s critical mineral strategy does have a significant flaw: it assumes Australia’s strategic partners will deliver on their part of the bargain. But they aren’t.

Fortunately, China has stepped up.

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