# THE RIO TINTO AFFAIR

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## Executive Summary

1. Stern Hu, a China-based executive of Rio Tinto, one of the world's biggest mining companies and a major player in the Chinese market, is being held by Chinese officials for alleged stealing of state secrets.

2. The arrest has rocked the country's steel industry, as well as foreign firms in China, and has strained Sino-Australian diplomatic relations.

3. The West has been largely critical about the arrest of Hu and three other employees of Rio Tinto. The enforcement of laws and selective law enforcements in China, together with the coincidental timing of the incident just days after the failure of the Chinalco-Rio Tinto deal, have been regarded as a tit-for-tat move by the Chinese government.

4. China has been acquiring overseas energy and mining assets since the 1980s. The recent global economic downturn has driven asset prices to unprecedented lows. This has sparked a shopping spree by China for strategic assets which are key to its future economic growth.

5. At the local level, the Chinese steel industry is plagued by widespread corruption. The industry's structure and industrial regulations have not been effective in illegal trade practices leading to rampant "rent seeking", or bribery at many levels.

6. Chinese sources view the arrests as stealing of state commercial secrets and harming the nation's economic interest and security as it involved Chinalco, a state-owned enterprise, and the Chinese steel industry. China's use of its sweeping laws has strengthened this claim.

7. China has been criticised for the way it handled the issue. China's definition of state secrets versus commercial secrets is unclear.

8. China has been too quiet on the investigation process and updates of the case that led to speculations within the western media and anti-Chinese sentiments of certain sections of the west. Thus, relations with Australia have been negatively affected.

9. There are misconceptions of Chinese SOEs as businesses under the control of the central/local government, and their acquisition of strategic commodity assets overseas as an expansion of China's strategic interest.

10. Chinese iron and steel firms obtain their iron ore supplies largely by collective bargaining with international firms via the China Iron and Steel Association. However, a significant number of firms then resell the ore at a profit to smaller domestic firms, creating opportunities for corruption within the industry.

11. The steel industry's structure and its trade practices also open a door to rampant corruption and bribery within the whole industry. China has however taken serious steps to curb this rampant corruption. Latest developments suggest that China was using this case as an attempt to reduce industrial bribery.

12. China has a key interest in ensuring these industries remain relatively corruption-free. Classifying this case as espionage reflects the level of concern that China has over a strategic industry rather than as a tit-for-tat move for the collapse of the Rio Tinto-Chinalco tie-up.

13. Despite the frictions generated over the failed business deal and the arrests, both sides are still caught in a relationship of mutual dependence. Australia has benefited greatly from exporting iron ore to China while China is also dependent on Australia's iron ore exports.

14. After the Rio Tinto case, China has turned towards Brazil for iron ore to fulfil its demand for raw materials.