Dragoman Digest.

4.06.2021

Implications of the IEA's net-zero 2050 pathway for oil exporters

Net-zero will favour those with a technological edge and developable renewable energy inputs

In its recent energy sector roadmap, the International Energy Agency (IEA) sets out a pathway to net-zero by 2050 that would see an end to the exploration and development of oil fields beyond those already approved. If it transpires, this scenario will alter the incomes and significance of several major economies and consequentially the global political order.

The most important shift will be in the relationship between energy exporters and importers. The abundance and broad distribution of renewable energy – like wind and sun resources – suggests a democratisation of energy replacing producer dominance. Low-cost producers like **Saudi Arabia** and **Russia** will be at an advantage compared with marginal producers as demand for oil gradually diminishes. Countries that control materials critical to electrification – particularly in renewables and storage – and those with a competitive advantage in renewable technologies stand to gain.

The range of inputs demanded by new energy technologies means that supply chains will necessarily be complex and decentralised – with some notable exceptions. **China** is a leader in all areas. It produces over 70 percent of solar PV panels, half of the world's electric vehicles and has raw materials and critical minerals processing capability. China's leading position across the value chain – from inputs to manufacturing – means it will be relatively advantaged. The **US** will be well placed to assure energy independence.

China firms up control over processed manganese

China's tactics are making Western carmakers nervous

Since October last year, dozens of **Chinese** manganese producers have joined a Beijing-backed "manganese innovation alliance". Manganese is used in a variety of applications ranging from steelmaking to glass manufacturing. The Chinese 'alliance' looks very much like a cartel. Its aims include stockpiling resources, centralising control over the supply of key products, coordinating prices and creating networks for mutual financial assistance. China already produces 90 percent of the world's manganese products. In a situation analogous to China's control over rare earths, manganese is relatively abundant globally but almost exclusively refined in China. So far, the alliance's measures have contributed to soaring prices in global metal markets. The price of steel strengthening manganese additives has increased 50 percent over the last four months.

Manganese is becoming an increasingly important ingredient in batteries. Higher manganese prices are of particular concern for global carmakers including Tesla and Volkswagen. Carmakers including Nissan and Volkswagen are pursuing diversification strategies to avoid overreliance on China. This is proving to be a fillip to non-Chinese suppliers of refined manganese products, some of which may eventually be located in **Australia**. Industry experts caution that such projects take time to develop and are quite capital intensive. Global industry will be hoping that China's manganese cartel is not replicated across other sectors.

Indonesia’s Corruption Eradication Commission (KPK) further weakened

A more politically pliant KPK is not what many expected from President Jokowi

Late last week, **Indonesia**’s KPK fired 51 of its employees. This was despite a relatively muted appeal for restraint from President **Jokowi**. The 51 employees in question failed the civil service qualifying test (TWK), which reportedly included dubious questions pertaining to religion, ethnicity and sexuality. That TWK test was introduced for KPK employees as a result of 2019 legal changes requiring that all KPK staff become members of the civil service. Indonesia’s civil service has traditionally been controlled by political patronage networks. The 2019 laws also reduced the KPK’s independence and freedom of action by creating a politically appointed Supervisory Board.

The 2019 laws and firing of the 51 commissioners augurs poorly for the future probity of Indonesian politics. Since its inception in the early 2000s, the KPK has arrested no fewer than 13 government ministers and many more lawmakers. The KPK has served as a symbol of the more successful elements of Indonesia’s post-*Reformasi* transformation, and has strong social support. Because of its fearless approach, the KPK has always been in the crosshairs of less scrupulous members of the political elite.

Elected in 2014 on a reformist platform, it was hoped that Jokowi would be a consolidating force for Indonesia’s democracy. Jokowi’s main priority though (and not necessarily unreasonably so) has been to focus on infrastructure and economic development. The view from more liberal circles in Indonesia is that Jokowi has been willing to tolerate democratic backsliding in exchange for political stability and compliance. Whether this Faustian bargain will be worthwhile for Indonesia in the long-term remains to be seen.

Japan legislates net-zero 2050 target

Japan will be reliant on fossil fuels until new technologies can be scaled

The codification of Prime Minister **Yoshihide Suga**’s net-zero 2050 target in **Japan**’s parliament last Wednesday provides investor certainty and sets in motion its transition away from fossil fuels. Renewable energy, hydrogen and nuclear energy are slated to play key roles in Japan’s future energy system. To be successful however, Japan’s energy transition will likely rely on a range of energy sources, each with their own technical and social challenges.

By 2030, renewables are set to constitute the largest share of the power mix at 30 percent. However, the deployment of wind power and PV has been slow due to high installation costs, limited land availability and grid connectivity constraints. Recent solar PV auctions awarded only 574 megawatts (MW) out of a total 1,663 MW auctioned. Coal and gas are set to constitute 24 percent of Japan’s power mix by 2030. This assumes large-scale deployment of carbon capture utilisation and storage (CCUS), co-fired ammonia-coal plants and carbon-neutral LNG. Whilst co-fired coal plants are due to be tested in Japan this year, there has been limited uptake of CCUS and carbon-neutral LNG. Japan has bet on the use of fuel-cell vehicles to decarbonise its road transport sector. Toyota Motor has invested heavily in the technology. However, there are doubts about whether fuel cells for light vehicles will prove economic compared to battery electric vehicles. Nuclear power generation – set to contribute 21 percent to Japan’s 2030 mix – will be slow to restart due to public opposition. Only nine of 60 nuclear reactors have been restarted since the Fukushima disaster in 2011. When it comes to net-zero, targets are only the first – and the lowest – hurdle.

EU shifts gear on China trade

December 2020 feels like a long time ago

It has not been a good month for the **China**-**EU** trade and investment relationship. In early June, the EU unveiled draft rules which, if implemented, would substantially curtail Chinese firms' market access to Europe. The rules propose empowering EU anti-trust regulators to block overly subsidised (mostly Chinese) foreign companies from making acquisitions in Europe and prohibit such firms from tendering for public contracts. Then, on May 17, the EU postponed plans to raise tariffs on a series of **US** goods, instead issuing a joint statement with Washington promising to hold to account "countries like China that support trade-distorting policies". The final blow came when the EU Parliament overwhelmingly voted to shelve consideration of the Comprehensive Agreement on Investment (CAI) until Beijing lifts sanctions on EU parliamentarians. These sanctions were imposed in response to limited EU sanctions on China over abuses in Xinjiang.

The CAI Agreement, concluded in principle in December last year, was meant to forestall then president-elect **Joe Biden**'s pledge to build a China-focused alliance with the EU. Whilst it would be premature to talk of a US-EU alliance on China just yet, the trends are clearly going in this direction. China seems to have either underestimated the EU's resolve on human rights or felt compelled to take an extra strong line against perceived foreign interference regardless of the consequences. The issue of human rights may actually only amplify in importance. The **German** Greens, who have been vocal on Xinjiang and are overall quite hawkish on China, are polling neck and neck with the Christian Democratic Union (CDU) in the lead up to September's elections. How far the discourse has denigrated was illustrated by Chinese Foreign Minister Wang Yi's comments that Germans "know what genocide looks like". With China also being unlikely to deviate from its current path under paramount leader **Xi Jinping**, it is difficult to see EU-China ties improving anytime soon.