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Massive capital raisings set to cement China's dominance over EV supply chains

The combined fundraising far eclipses the policy support announced by other economies

China's EV industry is set for a US$10 billion expansion. Three EV battery and material companies – CATL, Tianqi Lithium and Huayou Cobalt – are to raise over US$10 billion in separate share placements. CATL has taken the lion's share – raising US$6.7 billion last week, China's biggest equity capital market transaction this year and the second-largest worldwide. CATL will use the proceeds for the production and upgrade of lithium-ion battery manufacturing in four Chinese cities, as well as research and development. Tianqi, a lithium chemical producer, plans to raise up to US$1.7 billion in a secondary listing in Hong Kong whilst Huayou aims to raise up to US$2.6 billion through a private share placement. Huayou will use the proceeds to expand its nickel cobalt processing joint venture in **Indonesia**.

These raisings and China's entrenched position highlight the scale of the challenge for economies like the **US**, **Japan** and **South Korea**, which have recently upped investment to displace Beijing's stranglehold over EV supply chains. China is responsible for 50 percent of rare earths mining globally and has over a 60 percent market share for chemicals processing and refining of battery minerals. CATL alone controls nearly a third of the global EV battery market. China's cost advantages are set to improve, aided by government subsidies, growing scale and robust demand. Chinese gigafactories have a per unit cost of US$60 million/GWh, compared with the **EU**, where the cost is over US$120 million/GWh. Over the next 10 years, that cost is expected to fall to around US$50 million/GWh – well below the global average of around US$78 million/GWh. Rivals, including Japan, are investing in areas where they have solid market share, such as high-performance cathodes and battery-related recycling technology. Nonetheless, massive investment will be required to defend their position.

EU presses ahead with carbon market reform

A slower timeline for phasing out free pollution permits could cost the EU's decarbonisation fund over €400 million

After months of debate, on 29 June, the **EU** adopted a package of legislation that will pave the way for the widening of its emissions trading system (ETS) and the introduction of its Carbon Border Adjustment Mechanism (CBAM). The EU agreed that from 2024, the ETS will expand to include intra-EU maritime shipping. It currently covers the electricity sector, aviation and heavy industry. From 2025, a separate ETS will also be created for the building sector and road transport. The most contentious point of reform was the timeline for the phase-out of 'free allocations' (which have been handed to energy intensive industries for free and grant the holder the right to emit one tonne of CO2 equivalent) for sectors covered by the CBAM. Free allocations will be phased down over 10-years starting from 2026, with an accelerated rate of reduction at the end of the period. The previous draft proposal, which was rejected in early June, nominated 2028 as the final phase out.

The slower timeline has been deemed by some as a missed opportunity. Permits are auctioned to fund the Innovation Fund, the EU's flagship financing instrument aimed at supporting industry transition. Delaying the phase-out date to 2036 instead of 2028 means that the EU will miss out on over €400 million across eight years that would otherwise have been raised from auctioning around 620 million permits. The rule may also fall foul of World Trade Organisation Rules when the CBAM is introduced in 2026. Until 2035, EU industries will be protected by both the CBAM – which requires European importers to pay a levy on non-EU goods that mirrors the price of carbon in the ETS – as well as free allocations. Several economies have already raised concerns, including **China** and **Brazil**. A multilateral 'Carbon Club' – the formation of which is now underway after the G7's announcement – could reduce the risk of retaliation.

G7 officially launches global infrastructure partnership

Initiative is intended to serve as a counter to China's Belt and Road

Approximately one year after the G7 first flagged its intent to launch a global infrastructure partnership, leaders gathered in **Germany** unveiled the Partnership for Global Infrastructure Investment (PGII). The PGII will replace the G7's earlier 'Build Back Better World Initiative' (B3W), a necessity given President **Biden**'s failure to pass his eponymous Build Back Better domestic package. Through PGII, the G7 economies plan to mobilise US$600 billion worth of public and private funding by 2027 across four priority areas – climate, digital, gender equality and health. Existing projects now retrospectively christened as GIIP initiatives include a solar project in **Angola**, vaccine manufacturing facility in **Senegal**, small modular reactor in **Romania** and a US$40 million USAID investment in Southeast Asia's Smart Power Program.

The intervening year has enabled the G7 to flesh out in far more detail how PGII will actually work. Most of the aforementioned projects involved **US** or European development agencies providing grant financing to support commercial activities, often involving US and European companies. There is notably a greater security emphasis in PGII's four priority areas. Projects under the ambit of the digital pillar will include "deploying secure information and communications technology" and working with "trusted vendors to provide 5G and 6G". The climate pillar will involve investments in "clean energy supply chains" including critical minerals and "new global refining, processing and battery manufacturing sites".

Theoretically, the PGII is very well placed to compete with the Belt and Road. Outbound investment from G7 countries (and in the case of the US, individually) far outweighs **Chinese** investment. The trick will be in communicating a clear message. **Japan**, the EU and **UK** have all announced infrastructure initiatives under the broader aegis of PGII. How these initiatives function together to create a distinctive GIIP brand will be key in determining the PGII's success.

Issuances of 'panda bonds' slow amid policy uncertainty

China's rigid adherence to its zero-covid strategy is the principal source of uncertainty

In a sign of investor wariness, foreign issuances of yuan-denominated bonds (colloquially coined panda bonds) from January to June fell 50 percent from a year earlier, to a six year low of 7.9 billion yuan (US$1.18 billion). Panda bonds are typically used by European companies to raise capital for new factories and other investments in **China**. BMW and Mercedes-Benz were the only two companies to issue panda bonds in the first half of 2022, compared to five companies in 2021. This downfall happened despite issuances climbing to a record of 32.4 billion yuan (US$4.8 billion) in the second half of last year.

There are multiple factors driving growing investor caution. Though lockdowns have eased in Shanghai for now, omicron's virulence means that it is likely only a matter of time until a major metropolis is locked down. Paramount leader **Xi Jinping's** 'common prosperity' campaign and crackdown on the tech sector, whilst showing signs of becoming potentially more predictable, remains very much in play.

The growing risk aversion is further reflected in rather gloomy American Chamber of Commerce in Shanghai survey results. 48 percent of 133 member companies said they were planning to reduce or postpone investment plans in China. The **European Union** Chamber of Commerce in China survey suggested that 23 percent of respondents are considering relocating their Chinese investments towards other markets. Whilst a mass exodus of multinationals is unlikely, these figures suggest that in the absence of a circuit breaker, foreign investment in China may well stagnate over the coming years.

Russia defaults on sovereign debt despite being able to pay

The default is more symbolic than anything else

On Monday, **Russia** defaulted on external sovereign bonds for the first time since 1998. Payments for the two eurobonds were due on May 27, with a 30-day grace period having now passed. Over US$100 million worth of interest was due on Sunday night. Russia's situation is highly unusual, as the country has the means to pay, but is unable to access the global financial system because of **EU** sanctions. Russia's bond payments were sent to its National Settlement Depository (NSD). These funds would normally in turn be sent to international securities depositories such as **Luxembourg**'s ClearStream, or **Belgium**'s Euroclear. However, sanctions have impeded these institutions' ability to receive payment.

What is effectively a forced default has predictably caused chagrin amongst Russian officials. Minister Anton Siluanov claimed that western governments pushed Russia into an "artificial default". The default could potentially trigger legal recourse from investors, however it is more likely they will take a 'wait-and-see' approach, with claims only becoming void three years on from the payment date. Defaulting on bonds would usually result in further difficulties accessing capital markets. Of course, Russia has already been all but cut off from western capital. The default, even if forced, highlights Russia's growing isolation from the global financial system.