

## Dragoman Digest

### Indonesia targets globally competitive green manufacturing hub in Borneo

*Ambitious project has struggled to attract foreign capital thus far*

**Indonesia** is [building](#) a clean manufacturing hub in Tanah Kuning, North Kalimantan. In keeping with President **Widodo**'s aspiration to move up the value chain, the Indonesia Green Industrial Park (KIHI) aims to produce lithium-ion EV batteries, semiconductors, solar panels, green aluminium and industrial silicon. Indonesian energy giant Adaro Energy's Mentarang Induk Hydropower (MIH) project is slated to serve as the park's primary source of electricity. Adaro also proposes to develop 10GW of solar.

So far, only **Chinese** and local companies have committed to developing KIHI. Adaro has outlined plans for a US\$728 aluminium smelter and is constructing a petrochemical plant with Chinese-backed Taikun Petro Chemicals. Fortescue Future Industries', the green-energy subsidiary of **Australia**'s Fortescue Metal Group, plans for an ammonia and hydrogen plant are yet to [materialise](#).

The highly ambitious project faces numerous obstacles. MIH is scheduled for completion in 2028 – four years after production is expected to begin at KIHI. Local opposition, as well as engineering and financing challenges, may further extend these timelines. In the meantime, Adaro will power KIH using coal. The project is also entangled with the interests of Indonesian elites. Garibaldi Thohir, the CEO of Adaro and brother of SOE Minister Erick Thohir, is the majority landowner of the KIHI – Erik Thohir has pushed for a planned smelter to be built at Tanah Kuning over alternative sites. Close Jokowi ally Luhut Pandjaitan is also believed to be invested in the project. This elite backing may prove advantageous for foreign investors in the short term. However, as Indonesia gears up for elections in 2024, there is no guarantee that this support will endure.

### Taiwan lays out plan to achieve 2050 net zero target

*Ambitions place Taiwan's carbon-intensive chip industries between a rock and a hard place*

Earlier this month, **Taiwan** [passed](#) legislation introducing a legally binding net zero 2050 target, accompanied by a so-called 'carbon fee' for carbon-intensive companies. Under the *Climate Change Response Act*, Taiwan will initially charge a yet-to-be-announced fee to companies that emit over 25,000 tonnes of carbon per year. The fee will gradually increase over time. To mitigate carbon leakage, Taiwan will also introduce a carbon border adjustment mechanism (CBAM). Under the CBAM, Taiwanese importers will pay a levy on goods that mirrors the price of carbon in Taiwan. Revenues collected from the CBAM will be put towards a *Greenhouse Gas Management Fund*, which will finance emissions reduction projects.

Taiwan finds itself in a particularly difficult position. It currently imports 98 percent of its energy, with coal comprising about 45 percent of its energy mix. It also lacks a suitable landmass for renewables, with almost the entire island being used for either urban development or agricultural use. At the same time, Taipei has realised it cannot afford to be out of step with international partners. The threat of the **EU**'s CBAM and a potentially similar policy in the **US** makes this challenge all the more tangible.

Taiwan's leading chipmakers are similarly torn between the need to retain international competitiveness and the practical difficulties of procuring renewables in Taiwan. Electricity constitutes up to 30 percent of a chip plant's operational costs. Taiwan's TSMC, the world's most advanced contract chipmaker, has attempted to get ahead of the issue. It has allocated two percent of its revenue to "green initiatives" and, in 2020, signed what was then the world's

largest corporate green energy supply deal with **Denmark's** Orsted. Still, the practical difficulty of decarbonisation and pressure from major Western customers may ultimately force TSMC and other Taiwanese chipmakers to consider building additional foundries overseas where green power is available.

### **Japan's Sumitomo to build a non-Chinese supply chain for rare earths**

*Challenging China's control of downstream processing will be no easy task*

**Japanese** trading house Sumitomo plans to [establish](#) a rare earths supply chain that excludes **China**. Expected to start operations in July, Sumitomo's neodymium-praseodymium (NdPr) supply chain will be sourced from the **US** and further metalised in **Vietnam** and the **Philippines**. NdPr produces rare earth magnets, critical inputs to clean technologies, including EVs and wind turbines. Under the new arrangement, US company MP Materials will [supply](#) Sumitomo with refined NdPr from its Mountain Pass facility in Las Vegas – the US' only rare-earth mining and refining facility. Sumitomo is expected to distribute over 3,000 tonnes of refined NdPr to Japanese magnet makers.

Sumitomo's alternative rare earths supply chain is an early, tangible sign of Japanese and US efforts to bolster critical minerals and rare earths supplies. Tokyo has set a target for 50 percent of rare earths to be sourced outside of China by 2025 and will disburse subsidies through its economic security promotion act. The new supply chain aims to leverage the US *Inflation Reduction Act's* (IRA) US\$2.8 billion in grants and tax credits for onshore production and processing of over 50 critical rare earth and critical minerals. Eligibility requirements for the IRA's EV purchasing tax credits will increasingly become contingent on battery minerals being mined and processed outside of China. Sumitomo's move is the first in a long series of steps needed to break China's monopoly on downstream processes for rare earths.

### **US businessman Ajay Banga set to take on World Bank presidency**

*Banga will face pressure to prioritise green investment*

The **US** has [nominated](#) former Mastercard CEO Ajay Banga as the next President of the World Bank. His appointment follows pressure from Western economies to place climate action at the forefront of the World Bank's agenda. The World Bank has drawn criticism for [spending](#) almost US\$15 billion on fossil fuel projects since 2015. The outgoing president, David Malpass, a Trump administration appointee, had appeared to downplay the need to counteract anthropogenic global warming.

Banga will face an uphill battle in increasing the World Bank's climate financing beyond current levels. Currently, the World Bank aims to direct 35 percent, or around US\$175 billion, of its total financing between 2021 and 2025 towards climate-related projects. Although some member states have argued that further access to funding for climate action could be achieved by growing the World Bank's balance sheet – a measure which would require majority approval by shareholders – some countries are opposed. Earlier this year, around 35 countries, including **India**, **Brazil** and **Russia**, published a note opposing the potential change, claiming it would negatively impact the World Bank's triple-A rating. Importantly, many of these countries are among the largest emitters and [largest recipients](#) of World Bank loans. Banga will have to strike a fine balance between pushing for increased climate funding and assuaging their demands.

## Western clothing brands slowly depart China

*Closer-to-home manufacturing and alternative Asian locations are increasingly viable*

In another example of supply chain realignment, Western fashion brands are beginning to [shift](#) their textile production away from **China**. One example of this phenomenon is **Britain's** Dr Martens. The share of its Chinese production has fallen from 55 percent in 2018 to 5 percent this year. **German** brands Marc O'Polo, Hugo Boss and Adidas, as well as the **US'** Nike and **Spain's** Zara have all moved some of their Chinese operations to **Turkey**. China has for decades dominated textile supply chains, accounting for 36 percent of global textile exports in 2020.

Numerous trends are driving the industry shift. One major factor is China's increasing wages, which have doubled from around US\$6,600 to US\$13,200 between 2013 and 2021. Supply chain bottlenecks amid Covid lockdowns have highlighted the advantages of placing manufacturing sites close to primary markets. Increased supply chain scrutiny is an additional factor. Forced labour laws such as the US' *Uyghur Forced Labor Prevention Act* and Germany's *Supply Chain Due Diligence Act* have forced Western companies to abandon Xinjiang's cotton industry. Companies throughout the EU may soon have to follow suit, with [similar legislation](#) currently making its way through the European Parliament.

The extent to which companies have truly diversified away from China may be less than it seems. **Vietnam** and **Bangladesh**, for example – two favoured alternative textile manufacturers – continue to import [most](#) of the relevant raw materials from China.