China's big move in the energy transition and what it means for commodities

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Key Takeaways

- China's energy transition efforts are accelerating, with major implications for global commodities
- Weak market sentiment overlooks the long-term growth potential in the metals and energy sectors
- Investors can capitalise on China's strategic shift for future gains in commodity markets

Market sentiment towards China has been notably weak, with policy stimulus efforts failing to lift investor confidence. Despite the government's attempts to invigorate the economy, recent data, such as the persistent softness in manufacturing Purchasing Managers' Indices, has only deepened the pessimism. Yet, while the headlines focus on these short-term struggles, a significant shift is occurring beneath the surface.

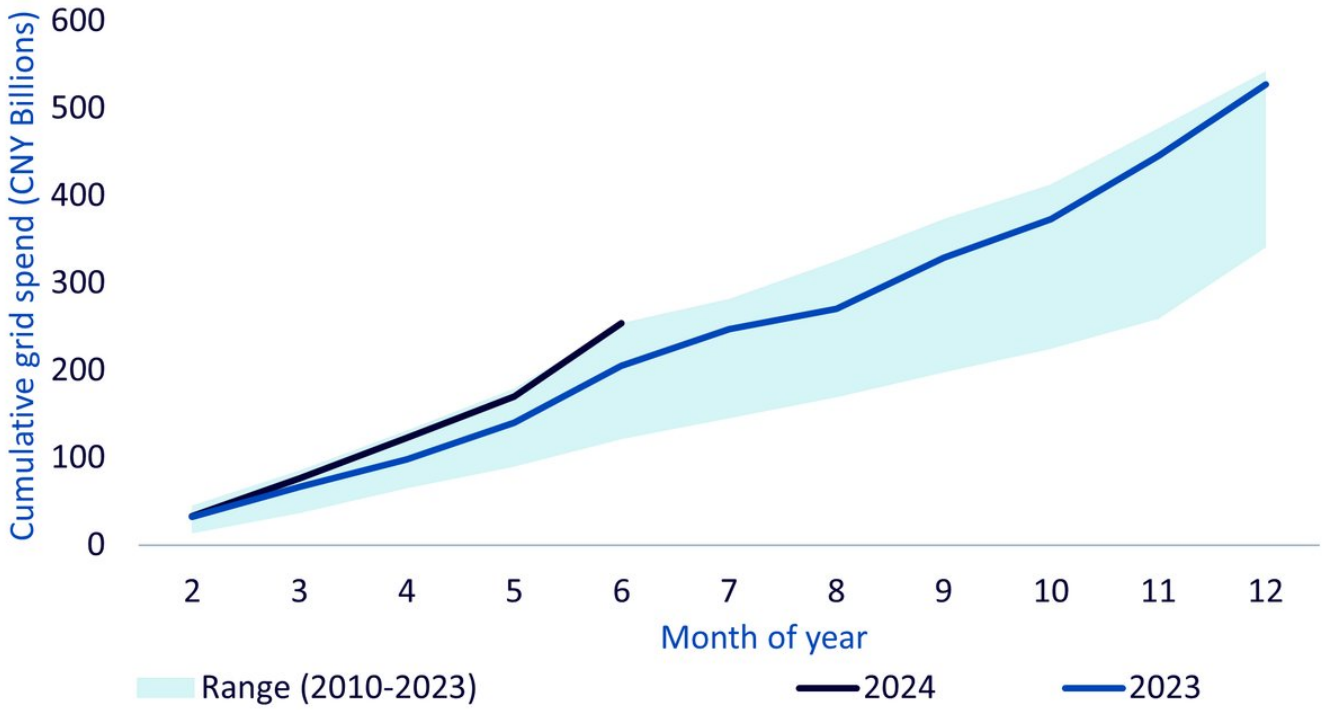
China is quietly advancing its energy transition at an unprecedented pace – an effort that has far-reaching implications for global commodity markets. Although these transformative measures are currently being overlooked, their long-term impact is something that markets will eventually have to reckon with. For savvy investors, this presents a unique opportunity. By looking beyond the current weak sentiment and focusing on the underlying fundamentals, investors can position themselves for substantial growth in commodity markets driven by China’s energy revolution.

Policy matters

China is likely to be a target of additional tariffs and will have close to a year to formulate a plan for policy easing to counteract trade disruption. China’s economy is already faltering under the pressure of a real estate implosion, and we expect the Chinese government to announce plans to stimulate its economy. In China’s Third Plenum, which is usually very long-term focused, the government noted in its communiqué some near-term issues, potentially pointing to the urgency in dealing with its economic soft patch. The mid-year Politburo meeting, however, failed to articulate a meaningful plan, with some subtle tilts to stimulating consumer demand.

We believe that in order to meet growth targets, China will follow up with more meaningful stimulus that will lean heavily on energy transition, i.e. a metal-intensive sector. China is already ramping up domestic electric grid expenditure, spending more money on transmission and distribution cabling, a copper and aluminium heavy sector. Figure 1 shows that spending on the grid is at record highs in China in 2024 (i.e. above the 2010-2023 range for June, the last available data point) and far above 2023 spending at this time of the year.

Figure 1: China grid spending



Source: WisdomTree, Bloomberg. 2010-June 2024. **Historical performance is not an indication of future performance and any investments may go down in value**

In May, China eased limits on “curtailments”, indicating its willingness to allow renewable infrastructure to grow further. “Curtailments” refer to the reduction of output from renewable energy projects owing to grid constraints or lack of demand. The challenge is particularly common in the north, which has ideal wind and solar resources but limited local power demand. Excess power produced in these regions requires more grid infrastructure to move the electricity to higher-demand regions. According to Bloomberg New Energy Finance, lifting the curtailment cap could trigger another 100 gigawatts of wind and solar installations.

Sanctioning this extra capacity indicates a strategic choice to move decisively with an energy transition strategy, with likely grid spending to match the production ambitions.

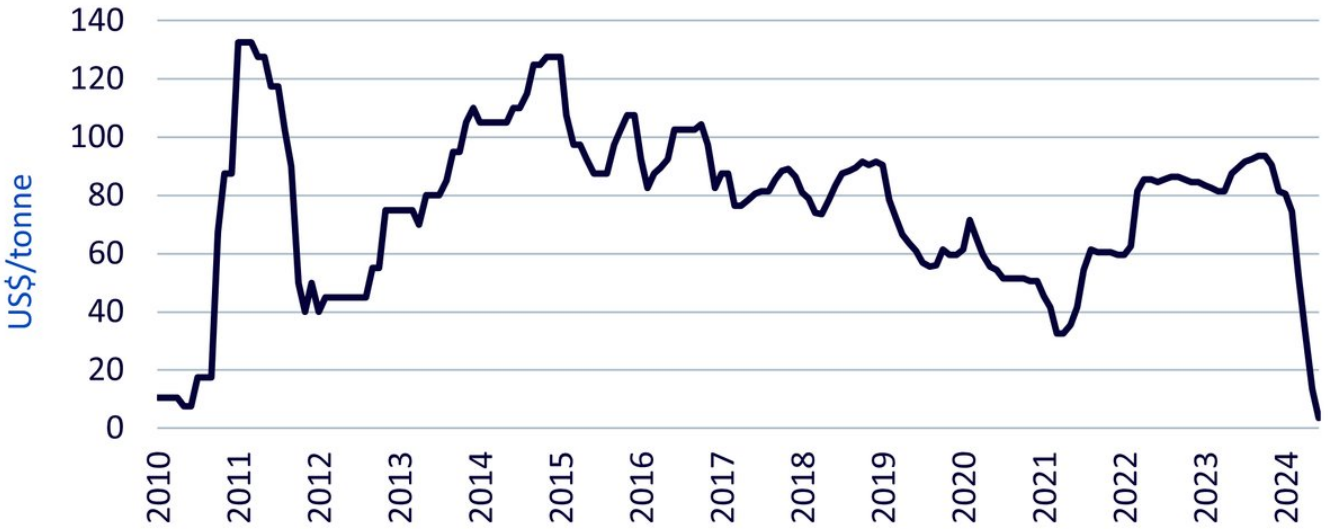
We believe China will continue expanding manufacturing and deployment of electric vehicles, solar panels, and batteries. Electric vehicle sales already represent 40% of passenger vehicle sales in China, and we could see that becoming close to 50% by the end of the year, with the costs of the EVs now lower than their internal combustion vehicle equivalents in China.

There may even be a small opportunity for China to expand exports to the US and Europe just before higher tariffs kick in. We have certainly observed this phenomenon in the run-up to Biden’s tariffs being implemented.

Impact on metals

The metal markets that are to benefit from the energy transition pivot are giving mixed signals. For example, the exchange inventor of copper has risen, indicating that the finished metal is in plentiful supply. Conversely, treatment and refining charges have fallen close to zero in China (Figure 2), indicating a lack of copper ore available to Chinese refiners to process Mining sector difficulties, including closures (e.g., Cobre Mine in Panama), declining ore grades, and delays in the opening of new mines, have contributed to this problem. Also, China's willingness to produce more finished copper than needed immediately (because it is preparing for future demand) may also be driving the treatment costs lower. If China is indeed preparing for a higher consumption level in the future, this should be a strong signal for the market 1.

Figure 2: China copper concentrate treatment charges



Source: WisdomTree, Bloomberg. 2010-2024. **Historical performance is not an indication of future performance and any investments may go down in value**

1. The greater the competition for the ore, the lower the amount refiners will charge for treatment and refining.

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