



News

China's Energy Crisis: The Effects on Apple, Tesla, and the Chinese Economy

Oct 06, 2021 — 8 min read



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China has been experiencing an energy crisis since last year. The country's power grid was hit by a series of natural disasters, including floods, landslides, and earthquakes. As a result, the country experienced a shortage of electricity supply.

Experts fear that with the global market's attention focused on the Evergrande crisis, another major supply shock to China's economy, may be underestimated or missed. The debt crisis of China's Evergrande has been in the global spotlight for the past weeks, but there's been another crisis brewing that has already affected major suppliers: the ability to produce electricity and renewable energy.

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How Bad is the China Energy Crisis?

China is heavily reliant on coal for domestic energy use and is the world's largest greenhouse gas emitter.

However, their push towards a greener initiative has set strict targets to cut emissions. Many of the country's massive factories — aluminum smelters, textiles producers, soybean processing plants — are being forced to curb activity or shut down altogether.

Unfortunately, efforts to slow down emissions and consumption have not been easy. The regions of Jiangsu, Zhejiang, and Guangdong have been among the most affected and missed their energy consumption targets set by the Chinese government.

The Chinese economy is also at risk of major coal shortages and natural gas along with rising demands and prices. In the past, China has curbed these problems with power rationing measures that aimed to ration energy reserves in the cold winter months.

The Demand for Renewable Energy in China

However, with energy prices skyrocketing for the region, the demand for an energy mix will have to be slated for a later time with high global prices like now.

The ability to produce electricity and other power sources, such as nuclear power, will also have to be scheduled for a later time as energy firms in Northern China are struggling to keep up with the total energy consumption coming from the region.

This power crisis is affecting homes, local businesses, and power factories that are dependent on these energy resources during this energy crunch. Nevertheless, the first subjects to feel this strain comes from those on stock markets around the world.



Photo by Lalit Kumar on Unsplash

Suppliers for Apple and Tesla Halt Production

As the Chinese government tightens its grip on stricter energy consumption policies, several Chinese companies, of whom provide essential resources to enterprises such as Apple Inc. and Tesla, have suspended production at some of their factories — putting supply chains at risk and halting economic development.

How Does This Affect Apple?

Apple Inc. is another major player in China and one of the largest exporters to the world. In 2018, Apple generated nearly half of its revenue outside of North America and Europe. Its products were sold in almost every single country around the globe except Japan.

Apple supplier Unimicron Technology Corp — a printed circuit board manufacturer — reported that three of its subsidiaries stopped production from September 26th to the 30th in order to comply with the new electricity limiting policies enforced by the Chinese government.

In 2019, Apple had revenues of \$234.5 billion worldwide, up 11% year-over-year. Of those revenues, \$17.6 billion came from Greater China, representing 26% of total revenues. That number increased to 28% in 2020.

Analysts believe that Apple's recent struggles in China can be attributed to several factors including lower smartphone shipments, weaker consumer spending, and weak retail sales. For example, according to research firm Canalys, Apple shipped only 7 million iPhones during Q1 compared to 10.7 million units in the same period last year.

This drop-in unit volume was largely driven by consumers switching away from older models towards newer ones such as the XR series. As a result, Apple lost ground against Samsung Electronics Comp., Ltd. and Huawei Technologies Co., Ltd. who saw strong double-digit gains.

Foxconn affiliate Eson Precision also reported that it suspended production for nearly a week at its facilities in Kunshan, a strategy aggravated by China's economy and its total energy mix consumption levels. Concraft Holding Co Ltd — an iPhone speaker component supplier — notified that it would suspend production for five days while relying on its current inventory to meet demands.

How Does This Affect Tesla?

As for Tesla, they generate roughly 20% of their sales in the Chinese region but BofA analysts have identified that Tesla is already losing shares in the Chinese electric vehicle market — down 1.2% in August from 13% in June. However, Elon Musk reassured at the World Internet Conference that Tesla will stay committed to China and will continue to expand its investments and R&D efforts in the country.

Tesla's Model 3 was recently launched in Shanghai and Beijing, where it sold out within hours. In addition, Tesla announced that it had received approval to build two Gigafactories in China, one each in Chengdu and Chongqing. These factories will produce batteries and powertrains for both domestic and international markets. They plan to invest \$4 billion into these projects and create more than 6,000 jobs.

However, if Tesla does experience difficulties or delays in building these factories, then it might affect demand for Model 3 cars and cause problems for the company. In terms of demand, Tesla expects to sell more than 100,000 vehicles annually in China by 2020. With these new factories, Tesla hopes to boost local manufacturing capacity and reduce costs.

How Will Coronavirus Impact Global Markets?

However, if the coronavirus outbreak continues or spreads further into Europe and North America, then we can see how much longer the company can sustain itself without significant support from foreign governments.

Coronaviruses are highly contagious viruses that cause respiratory illnesses such as colds and flu. They spread through droplets when people cough or sneeze. There are four types of coronaviruses known to infect humans; 229E, OC43, NL63, and HKU1. Of those, only 229E causes mild symptoms.

This development can affect key industry players that have been unaffected by the current Chinese energy crisis, such as semiconductor producers. Ahead of current estimations regarding total energy consumption, chipmaker suppliers such as United Microelectronics and Taiwan Semiconductor Manufacturing expect zero bottom-line impact on their industrial plants and production.

These economic changes have affected multiple industries but can be a resolved problem for a select few. The current situation rivals the past decade of hockey-stick growth and predictability for each industry but shows how even the most energy-averse businesses can be affected as Chinese companies.



Photo by Frédéric Paulussen on Unsplash

China's Economic Growth, Its Troubles, and How It Affects S&P 500 Companies

With Apple and Tesla suppliers experiencing bumps in their production schedules, S&P 500 companies, and U.S. investors are also not invulnerable.

According to Bank of America strategist Savita Subramanian, S&P 500 companies have approximately 5% direct sales exposure in China but the correlation between China's GDP and their earnings has seen a 90% increase since 2010. Companies have increasingly capitalized on cheaper labor abroad and supply chain efficiency over the last 30 years, which accounts for about 80% of margin expansion for the S&P 500.

The fact that economic troubles have been brewing in China means that S&P 500 companies may be in trouble. Analysts have reported that sales, profit, transactions, hiring, and so on have weakened this quarter, and construction sub-sectors have plummeted.

The economy has already been slowing due to Covid-related restrictions and now that China has cut production to meet their strict emission targets, there could be greater impacts on consumption and investment.

China also accounts for about 30% of global sales and production and has been a source of growth for U.S. automotive companies. This growth has been slowing and the auto industry could be challenged. BofA analysts note that suppliers with the biggest Chinese exposure are most at risk and include companies like Adient (ADNT), Aptiv (APTV), BorgWarner (BWA), and Lear (LEA), and Visteon (VC).

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The Power Crunch and Growth Outlook of the Chinese Economy

Analysts say the power crunch has hurt production in industries across several Chinese regions and is dragging their economic growth outlook. Home and non-industrial users have also felt the brunt of it as China's northernmost cities reach near-freezing temperatures.

While the National Energy Administration (NEA) is making sure coal and natural gas firms monitor a sufficient energy supply to homes this winter, residents in cities have been discouraged from using high energy-consuming electronics during peak periods. This is due to power generation declining significantly since July and the supply gap reportedly widening to a "severe level".

Power shortages have been driven by tight coal supplies and toughening emission standards. The Chinese government has vowed to cut energy intensity by 3% in 2021 in order to meet its climate goals. They are also aiming to bring carbon emissions to a peak by 2023 and to neutrality by 2060.

With only 10 of its 30 mainland regions managing to achieve their energy goals for the first half of the year, authorities have increased enforcement of emissions curbs.

Could China's Power Crisis Help (or Harm) Its Green Energy Push?

China's energy crisis may just be getting started, and no less than its economic growth and its green, renewable energy future hang in the balance.

The power shortage fallout has prompted analysts to change their 2021 growth outlook. According to Nomura Holdings Inc, they have cut their third and fourth quarter China GDP

growth forecasts to 4.7% and 3.0% from 5.1% and 4.4% previously. Their full-year forecast has also decreased from 8.2% to 7.7%.

"The power-supply shock in the world's second-biggest economy and the biggest manufacturer will ripple through and impact global markets," state Nomura analysts. There is little immediate relief in sight for China's power woes, given the global surge in coal and natural gas prices and rising energy demand, not to mention potentially extreme weather.

China is the world's biggest producer and consumer of coal, and right now its inventories are at record lows. To ensure adequate energy supplies as winter sets in, China has loosened restrictions on coal mining operators in its coal belt region stretching from Shaanxi to Inner Mongolia and prioritized shipments to regions in need.

Though coal currently accounts for nearly 57 percent of China's energy mix – and its reliance on fossil fuel is likely to increase in the coming months, the problems being worked out in China's power markets and energy supplies may end up accelerating the country's pivot to greener more sustainable energy.

Coupled with the concerns of Evergrande's fate, this power crunch is unsettling Chinese stock markets with the world's second-largest economy showing signs of slowing.

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