Monthly Energy Transition Materials Market Report

June 2023

HANetf & Sprott Asset Management
Sprott Energy Transition Materials UCITS ETF
SETM
75 bps
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This report was written by, and is the opinion of, the Sprott Asset Management.

Energy Transition Materials ETF: Key Takeaways

In May, lithium and lithium miners staged a sharp rebound rally, but copper and copper miners were weighed down by disappointing data from China, ongoing global growth concerns and the U.S. debt ceiling drama. China's economy was expected to rebound following the end of its zero-COVID policy in December and the completion of its regulatory reform this year, but signs of economic recovery are now limited, particularly within China's industrial sector. Metals traders that had built inventory in anticipation of a China rebound have been destocking aggressively, putting downward pressure on the prices of most metals commodities.

The lithium commodity market experienced a significant rebound in May, with prices rising more than 60% after a massive sell-off from the November 2022 peak. Market sentiment improved given that high demand has depleted lithium inventories, restocking has started to heat up and global EV sales recovered in May.

In China, lithium carbonate imports surged by 84% in April compared to March, reaching a volume of 17,500 metric tons of lithium carbonate equivalent. This is an important indicator of demand growth. It represents the second-highest import volume ever recorded and suggests that domestic demand in China is rising. Market sentiment had been weak for months, but it has improved, increasing consumption of existing lithium stockpiles.

In May, there was another significant realignment in the lithium mining space. Livent and Allkem, two prominent players and the only two lithium producers in Argentina agreed to merge in a deal valued at $10.6 billion. The combination will form the world's third-largest lithium company.

Argentina, a fast-growing emerging lithium supplier, is making progress in gaining access to the U.S. market. Argentina is actively lobbying to secure an exemption to current regulations as it lacks a free trade agreement with the U.S. This move to secure end-market access comes during intense global competition between the U.S. and China for critical EV minerals.

The Livent-Allkem merger followed Liontown Resources' rejection of a $3.7 billion proposal from Albemarle Corporation in March. Liontown's market capitalization rose significantly the day after it rejected the proposal, to $3.8 billion from $2.2 billion, indicating potential tailwinds from further mergers and acquisitions. Similar large gains in lithium miners have occurred recently due to EV carmakers making direct equity investments into miners to secure lithium supplies.

Copper prices fell in May after China's economic data was weaker than expected and failed to meet expectations that demand would increase with the post-COVID reopening. Renewed concerns about further U.S. rate hikes also dampened sentiment in the metals market at large. These appear to be typical shorter-term cyclical pricing effects within a longer secular commodity supercycle. Chinese economic data released in May included two items that indicated the depth of the country's economic weakness and negatively affected metals prices. One was industrial output for April, which was a very disappointing 5.6% year-over-year vs. an expected 10.9%. The other was April's credit data, which showed new loans were the lowest in six months and total social finance growth was well below expectations. Mid- and long-term household loans (a proxy for mortgages) recorded the sharpest drop in 15 years after a strong March. China's consumers remain reluctant to enter the property market. These two data points hurt sentiment and drove a sharp sell-off across most industrial metals. However, China's economic policy committee may announce stimulus initiatives to boost economic growth as it has done repeatedly over two decades.

Copper inventories, meanwhile, remain very low across all three major exchanges and the inventory coverage ratio continues to decline. Long-term and short-term copper markets are expected to remain in deficit. Mine supply growth continues to miss expectations while demand, particularly in China, surpasses previous forecasts. The global copper concentrate market remains on track for a steep deficit during 2025–2027 as significant new smelting capacity comes online in Asia while mine supply growth lags.

Nickel prices fell 15.6% in May—the fourth steepest monthly drop in a decade. Nickel is a minor commodity compared to other metals, making its prices more volatile. The nickel market was affected by the same macro news out of China as the other metals markets in addition to reports that Chinese nickel producers are seeking to have their nickel cathodes "certified LME deliverable." This news follows efforts by the LME to bolster the liquidity of its nickel contract, including shortening contract terms for new brands from one year to three months and waiving fees. Anecdotal reports suggest market participants are concerned this could quickly inundate LME warehouses with currently non-deliverable material, putting considerable downward pressure on LME nickel prices. (We believe this would likely have a very short-term trading effect on nickel prices.)

Source of all performance data: Bloomberg / HANetf as of 31.05.2023. **All performance figures are showing net data.** Past performance is not indicative of future performance and when you invest in ETFs your capital is at risk.

Macro Outlook

We believe the post-pandemic era marks the beginning of a new supercycle for commodities, especially for the critical minerals covered in this report. The clean energy transition is just one trend driving demand higher. Geopolitical tensions and conflict are prompting global powers to reshore their supply chains and production to ensure industrial security—an about-face after many decades of offshoring.

These trends are commodity- and capital-intensive, creating a demand shock for commodities. They are also inflationary in nature. We expect a steady increase in demand to drive commodities in the medium term. Meanwhile, the commodity demand shock is colliding with a supply situation that is woefully inadequate. Miners and production facilities have faced a decade of underinvestment caused by the low commodity prices that prevailed during an era of record-low interest rates and the long lead times required—often a decade or longer— to bring new production online. Sanctions on Russia, the world's largest producers of many commodities, only aggravate the situation—while also fanning the flames of rising "resource nationalism."

The commodity supercycles of the past arose from varied conditions. In the 1970s, an energy supply shock drove the distress, rooted in OPEC embargoes. In the early 2000s, it was demand shock from an aggressively growing China that underpinned commodity inflation. The emerging supercycle has both supply and demand shocks, prompting heated global competition to secure commodities.

Please remember that when you invest in ETFs, your capital is at risk.

Product Details

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Sprott Energy Transition Materials UCITS ETF (SETM) provides exposure to the companies that are providing the critical materials needed for the global clean energy transition.

The fund tracks the Nasdaq Sprott Energy Transition Materials Ex Uranium Index (NSETMU Index).

Visit the SETM fund page for more information.

Exchange	Ticker	RIC	SEDOL	ISIN	Valoren	WKN	CCY	Listing Date
LSE	SETM LN	SETM.L	BMD1W41	IE000K6PPGX7	-	-	USD	14/03/2023
LSE	SETP LN	SETP.L	BMD1WF2	IE000K6PPGX7	-	-	GBP	14/03/2023
Borsa Italiana	SETM IM	SETM.MI	BMX5LF7	IE000K6PPGX7	-	-	EUR	30/03/2023
Xetra	M7ES GY	M7ES.DE	BMX5LD5	IE000K6PPGX7	-	A3DCVJ	EUR	16/03/2023

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