Volume 11, Issue 6, June – 2026 International Journal of Innovative Science and Research Technology
ISSN No:-2456-2165 https://doi.org/10.38124/ijisrt/26jun075

The Macroeconomic Impact of Decarbonizing Industrial Heat vs. Electrical Grids: A Comparative Analysis of Capital Investment, GDP Growth, and Long-Term Economic Returns

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Publication Date: 2026/06/15

Abstract: The global transition toward net-zero emissions has historically prioritized the decarbonization of the electrical grid through renewable energy deployment. However, the abatement of emissions from heavy industrial thermal processes presents distinct thermodynamic and macroeconomic challenges. This paper provides a comparative macroeconomic analysis of decarbonizing industrial heat versus electrical grids. Utilizing a conceptual framework grounded in structural macroeconomic modeling, we compare capital investment requirements, implications for Gross Domestic Product (GDP) growth, and long-term economic returns. Drawing upon foundational frameworks of energy-growth nexuses (Shahbaz et al., 2020), systematic sustainability transitions (Bhuiyan et al., 2022), and multi-sector national climate solutions (Attanayake et al., 2024), this study demonstrates distinct structural divergences. Our findings indicate that while electrical grid decarbonization requires immense up-front capital for transmission and storage assets, it yields highly predictable long-term economic returns due to falling levelized costs of electricity (LCOE). Conversely, industrial thermal decarbonization requires deep structural capital investments into low-carbon technologies like green hydrogen (H_2) and carbon capture, utilization, and storage (CCUS). Due to high operating expenses (OPEX) and technology premiums, industrial thermal abatement introduces higher near-term risks to industrial competitiveness and GDP growth, but offers profound systemic resilience and raw material stability over long horizons. Ultimately, integrated multi-sector planning is required to mitigate macroeconomic shocks during the structural transition.

Keywords: *Macroeconomic Modeling; Industrial Heat Decarbonization; Grid Decarbonization; Capital Investment; GDP Growth; Long-Term Economic Returns.*

How to Cite: Aanu Loveday Solomon; Ekpu Matthias; William, Merie A. I.; Sunday Luton Uebari; Seyi Sunday Olugbeja; Osondu Chukwuebuka (2026) The Macroeconomic Impact of Decarbonizing Industrial Heat vs. Electrical Grids: A Comparative Analysis of Capital Investment, GDP Growth, and Long-Term Economic Returns. *International Journal of Innovative Science and Research Technology*, 11(6), 242-245. https://doi.org/10.38124/ijisrt/26jun075

I. INTRODUCTION

The imperative to mitigate global climate change has forced an unprecedented restructuring of macroeconomic systems. To achieve mid-century carbon neutrality, structural shifts must occur across all sectors of production. For the past two decades, both public policy and private capital have disproportionately targeted the power sector. The electrification of the economy via solar photovoltaics (PV), onshore and offshore wind, and battery energy storage systems (BESS) represents a mature tech-economic paradigm with established financial models (Bhuiyan et al., 2022). However, a critical blind spot in the sustainable economy discourse remains the industrial heat sector. Heavy industrial activities—predominantly iron and steel production, cement manufacturing, chemical synthesis, and petroleum refining—account for approximately one-third of global energy-related greenhouse gas (GHG) emissions. More than 70% of this industrial energy footprint is consumed not as electricity, but as thermal energy (heat), often at high temperatures exceeding 400°C to 1000°C (Alcayde et al., 2018). While grid decarbonization relies on scaling existing, modular technologies, decarbonizing high-temperature industrial heat requires deep, disruptive process innovations (Attanayake et al., 2024). This paper investigates the comparative macroeconomic impacts of these twin transitions. Specifically, we address three core pillars:

- Capital Investment Infrastructure Requirements: The scale, intensity, and duration of asset configuration.
- Gross Domestic Product (GDP) Trajectories: The transitional impacts of energy price adjustments, technology premiums, and supply chain re-shoring on aggregate output (Shahbaz et al., 2020).
- Long-Term Economic Returns: The structural productivity gains, asset depreciation metrics, and systemic value generated post-abatement.

II. METHODOLOGY & ANALYTICAL FRAMEWORK

To systematically contrast the macroeconomic profiles of industrial heat and electrical grid transitions, this study employs an analytical framework anchored in endogenous growth theory and structural macroeconomics. We evaluate the economic impacts by modeling the energy transition as a structural shock to the capital stock (K) and total factor productivity (A) within a standard production function:

$$Y = A f(K, L, Ee, Et)$$

Where:

- Y represents total macroeconomic output (GDP).
- L represents labor.
- Ee represents electrical energy inputs.
- Et represents thermal energy inputs. We distinguish the transitions along three structural vectors:

Table 1 Structural Attributes of Decarbonization Pathways

Parameter	Electrical Grid Transition	Industrial Thermal Transition
Primary Technology Suite	Solar PV, Wind, BESS, Hydro, Nuclear	Green Hydrogen (H_2), Biomass, CCUS, Electric Arc Furnaces
Capital Profile	Modular, highly standardized, distributed	Bespoke, highly integrated, centralized facility assets
Fuel Dependence	Zero marginal fuel cost (for wind/solar)	Continuous high-cost feedstock dependency (e.g., green H_2)
Abatement Frontier	High technical maturity; low green premium	Low-to-moderate maturity; high green premium
3. Capital Investment Requirements		
3.1 Electrical Grid Decarbonization		
The capital expenditure (CAPEX) required to transition power grids to 100% renewable configurations is monumental but front-loaded (Bhuiyan et al., 2022). Investment is split into three main components:		

- Generation Assets: Expanding wind and solar capacities.
- Transmission & Distribution (T&D): Upgrading lines to connect remote renewable resources to urban load centers.
- Flexibility Assets: Deploying grid-scale battery systems and pumped hydro storage to handle renewable intermittency. Because these assets are modular, capital can be deployed iteratively. Private capital markets absorb this debt efficiently because renewable generation projects feature highly predictable cash flows backed by Power Purchase Agreements (PPAs).

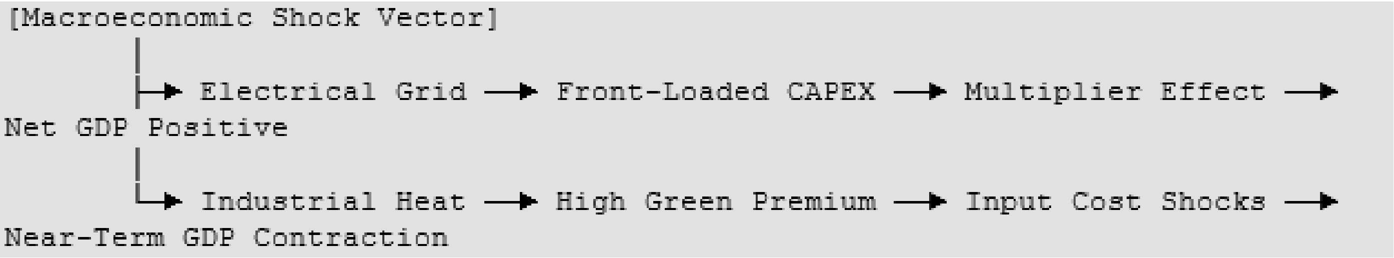
➢ *Industrial Thermal Decarbonization*

Decarbonizing high-temperature industrial heat requires deep process re-engineering (Alcayde et al., 2018). Low-temperature heat ($<150^\circ\text{C}$) can be effectively electrified via industrial heat pumps. However, high-temperature processes require fundamentally new chemical and thermodynamic mechanisms:

- Steelmaking: Replacing traditional coal-fired Blast Furnaces (BF/BOF) with Green Hydrogen-based Direct Reduced Iron (DRI) coupled with Electric Arc Furnaces (EAF).
- Cement Production: Deploying Carbon Capture, Utilization, and Storage (CCUS) facilities to capture process emissions from limestone calcination, along with oxy-fuel combustion systems. These investments are deeply lumpy, highly capital-intensive, and site-specific. Unlike a modular solar farm, an iron plant cannot be incrementally decarbonized; it requires a wholesale capital replacement of the core facility. Furthermore, the infrastructure required to supply the inputs—such as regional hydrogen pipelines or carbon transport networks—requires large-scale public-private co-investment before individual industrial sites can transition.

III. IMPACTS ON GDP GROWTH DYNAMICS

The transitional effects on GDP vary significantly between the two pathways, presenting distinct short-term costs and long-term structural changes (Shahbaz et al., 2020).



```
[Macroeconomic Shock Vector]
        |
        ├─► Electrical Grid ──► Front-Loaded CAPEX ──► Multiplier Effect ──►
Net GDP Positive
        |
        └─► Industrial Heat ──► High Green Premium ──► Input Cost Shocks ──►
Near-Term GDP Contraction
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- *Demand-Side Multiplier Effects*

In the short to medium term, both pathways act as classic Keynesian demand-side stimulants. The massive deployment of capital creates robust domestic supply chains, stimulates engineering and construction sectors, and creates high-skilled employment (Jha et al., 2017). For the electrical grid, this structural stimulus is widespread and directly boosts GDP. For industrial heat, the near-term domestic GDP multiplier can be even stronger per dollar invested because it triggers major retrofits of localized manufacturing plants. This drives demand for heavy engineering, metallurgy, and specialized machinery.

- *Supply-Side Pricing Shocks and Competitiveness*

The divergence in supply-side impacts is sharp:

- The Grid: As wind and solar assets scale, the marginal cost of producing electricity drops to near zero. While grid integration and balancing costs rise, the long-term Levelized Cost of Electricity (LCOE) stabilizes (Bhuiyan et al., 2022). This provides a predictable inflationary anchor for the wider economy, supporting sustained GDP growth.
- Industrial Thermal: Conversely, switching to low-carbon thermal options introduces a substantial "green premium." Green hydrogen and clean biomass remain significantly more expensive per gigajoule (GJ) than unabated natural gas or coal. If heavy industries absorb these elevated operating costs (OPEX), their profit margins squeeze, reducing their contribution to national GDP. If they pass these costs down the supply chain, it can create structural inflation in intermediate goods like steel, cement, and basic chemicals (Shahbaz et al., 2020). This can weaken a nation's international trade position and slow overall economic growth during the transition period.

IV. LONG-TERM ECONOMIC RETURNS AND PRODUCTIVITY

- *Asset Lifespans and Depreciation Risk*

Electrical grid assets typically face structured, predictable depreciation cycles (20\text{–}30 years for wind/solar; over 50 years for transmission lines). The primary macroeconomic risk here is the premature retirement of legacy fossil-fuel infrastructure, which can result in stranded assets on utility balance sheets. In contrast, industrial thermal assets are exceptionally long-lived; a blast furnace or chemical cracker can operate for 40\text{–}60 years through regular maintenance cycles. Forcing a rapid transition can lead to severe capital write-downs of high-value industrial assets. However, once clean systems like hydrogen-based DRI-EAF are fully established and integrated into local supply chains, they offer remarkable long-term economic stability (Attanayake et al., 2024). They insulate domestic manufacturing from the volatile global oil and gas markets, ensuring more stable, predictable production cycles.

- *Macro-Prudential Resilience and the Avoided Cost of Carbon*

A complete evaluation of long-term economic returns must include the avoided systemic costs of carbon emissions, such as carbon taxes, border adjustment mechanisms (like the EU's CBAM), and climate damages (Shahbaz et al., 2020). While grid decarbonization protects the economy from broad fuel shocks, industrial thermal decarbonization protects the foundational building blocks of the physical economy. Ensuring a clean supply of domestic steel, cement, and chemicals ensures that downstream sectors—such as construction, automotive manufacturing, and infrastructure development—can remain globally competitive in a low-carbon world economy.

V. POLICY FRAMEWORKS FOR MECHANICAL & INDUSTRIAL ENGINEERING SYSTEMS

To balance these macroeconomic trade-offs, industrial and mechanical engineering policy must move away from isolated, siloed solutions. Instead, it should adopt an integrated approach focused on Sector Coupling:

- Strategic Co-Location (Industrial Symbiosis): Policymakers should incentivize the co-location of renewable energy generation with industrial clusters. Using excess, curtailed renewable electricity during peak generation times to run industrial electrolyzers for hydrogen storage directly bridges the gap between grid flexibility and thermal fuel needs.
- Waste Heat Recovery Mandates: Mechanical systems must maximize efficiency prior to switching fuels (Alcayde et al., 2018). Implementing industrial waste heat recovery technologies—such as capturing low-grade heat for district heating systems or organic Rankine cycles—reduces the overall thermal load that needs to be decarbonized, lowering the total capital required.
- Targeted Public De-risking: Because industrial thermal transitions carry a high green premium, governments should deploy targeted fiscal tools. Contracts for Difference (CfDs) for carbon and green hydrogen can help stabilize operating costs, protecting industrial margins and preserving GDP growth during the early stages of adoption (Shahbaz et al., 2020).

VI. CONCLUSION

Decarbonizing the electrical grid and transforming industrial heat represent two deeply interconnected yet structurally distinct macroeconomic challenges. Grid decarbonization is a capital-intensive but technically mature pathway. It provides predictable, front-loaded economic growth, low marginal operating costs, and manageable risks to GDP. On the other hand, decarbonizing heavy industrial heat requires deep, complex capital overhauls. It carries higher near-term operating costs and poses real risks to industrial competitiveness, but it provides vital long-term systemic resilience by securing the core supply chains of the modern physical economy. For macroeconomic stability and long-term sustainable growth, these two transitions cannot be pursued in isolation. The falling costs of renewable electricity must be strategically leveraged to produce affordable green hydrogen and power industrial electrification. This integrated approach can minimize transitional shocks to GDP while building a resilient, fully decoupled industrial economy.

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