Industrial metals prices still down from their 1 January 2015 level

Dollar strength will limit strong gains for base metal prices, despite good fundamental support

Global steel and iron ore prices will remain soft this year on global overcapacity

China manages slowdown; India to be the new growth engine

While most economies in Emerging Europe are expected to show decent growth in the coming years, Russia and Ukraine are sinking into a depression, dragging the regional forecast down. The US economy is expected to perform solidly, despite the relatively slow start in early 2015. While the dollar’s appreciation will negatively affect US exports, we think US household consumption will receive an impulse from lower import prices. Meanwhile, we expect economic growth in Emerging Asia to remain strong. India will be the new growth engine, surpassing China this year and next. Metal demand in India will be buoyed by government infrastructure spending. Due to the ambitious economic reform plans in China, growth is expected to slow. We expect that the slowdown will be gradual during 2015/16, and think the authorities will remain prepared to add support to prevent a hard landing. But the gradual slowdown of the Chinese economy will have a downward effect on overall metal demand.

China industrial metals consumption growth set to slow

China is still the world’s biggest producer and consumer of metals. On average, China accounts for 43% of global production of base metals and 48% of consumption. Needless to say, economic data coming from China and other developments have left their mark on international metal markets, particularly as regards consumption. Alongside the deterioration of GDP growth per capita in China, demand growth for base metals per capita is decreasing. This is also the case for per capita steel production growth. In fact, China’s Iron and Steel Association has forecast a 1% decrease in the country’s crude steel output in 2015. This indicates that steel production per capita will also decrease this year for the first time in decades. Although the slowdown in China will also have negative implications for demand in base metals markets, growth in demand for base metals remains likely. We are projecting that per capita demand for Chinese base metals will grow by 7% and 8%, respectively, in 2015 and 2016. This is low in historic terms, but still provides a solid base.

Industrial metals prices still down from 1 January levels

Industrial metals prices have been struggling this year. While base metals prices have lost from 1-17% since the start of 2015, prices in the ferrous industry dropped more sharply. Iron ore fell by 33%, global steel prices decreased by16% and coking coal declined 7%. Prices in the base metals industry came under fire from the dollar’s strength, the drop in the oil price and weak sentiment (especially with respect to China). The main concern for stakeholders is China’s relatively weak economic performance and the resulting slower demand for industrial metals. Good macro numbers from the global economy (particularly the US and Europe) were not able to shift general sentiment in base metal markets. However, since 1 April prices for copper and zinc have been showing some cautious signs of recovery.
Focus is on Chinese trade data for aluminium and copper
The drop in Chinese export and import volumes in February was expected. Due to the Chinese New Year holiday during the last two weeks of February, trade activity was relatively slow. Although aluminium exports were down, they were still at historical high levels. A further increase in aluminium exports in March is expected. China has abundant aluminium resources and the excess material will be pushed onto international markets against highly competitive prices. This will depress global market conditions even more. Chinese copper imports were also down in February. In fact, copper demand has disappointed globally so far and, despite favourable conditions, a revival in demand has not yet materialised. We think that the second quarter will witness an upturn in base metals demand in most regions. This fundamental support will lift base metals prices, but real strong gains will be limited this year due to further strengthening of the US dollar.

Iron ore and steel head downhill, coking coal remains flat
While coking coal prices managed to stay flat, prices for steel and iron ore have dropped significantly during 2014-2015. Overcapacity of steel and iron ore is the underlying cause. This has become a protracted problem and things are especially worrisome in China, which produces 50% of global crude steel output and is therefore the key to future market balance. The good news is that recently, the Chinese government announced ambitious plans to resolve the matter. China wants to accelerate the domestic merger & acquisitions process and create 10 big steel-producing companies, which together account for 60% of the country’s total output. Alongside this target, polluting emissions and total energy use is to be cut significantly. But interestingly, the Chinese government launched a similar plan in Q3 2013, with the aim of reaching that same goal by 2015. We wrote about this plan in August 2013 and signalled in publications thereafter that not much had changed. Let’s hope this time we will see some results. To ensure a sustained future for the global steel industry, this initiative to reach market balance is certainly welcome.

China iron ore inventory remains high
In any case, the steel sector is still in relatively poor health in most regions and, as a result, the appetite for steelmaking raw materials among steel mills is generally weak. Data coming from China are especially interesting to monitor. The latest figures show that Chinese port stocks are still fairly high. Iron ore imports into China decreased by 1% in the first two months of 2015 yoy and domestic production dropped by almost 6% yoy in the same period. In the meantime, more iron ore output from existing mines around the world is being added to the heavily saturated market and iron ore prices are weakening further. At current price levels, it will come as no surprise that the number of loss-making operations is set to increase. Although we expect prices to revive slowly in Q2 and Q3 from current (very) low levels, the price gains will not make up for the losses.

Chinese steel exports increase pressure
Low iron ore prices are good for steel mills’ margins but, given the relatively weak demand for steel, there is little incentive to source much material. In addition, steel exports from China are putting pressure on international prices. Chinese steel exports accelerated during 2014 and in the first two months of 2015 yoy and domestic production dropped by almost 6% yoy in the same period. In the meantime, more iron ore output from existing mines around the world is being added to the heavily saturated market and iron ore prices are weakening further. At current price levels, it will come as no surprise that the number of loss-making operations is set to increase. Although we expect prices to revive slowly in Q2 and Q3 from current (very) low levels, the price gains will not make up for the losses.
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