Metals Newsletter

September 2018

Economic Indicators and Comment:

The U.S. and Canada have reached a new trade deal, along with Mexico, to replace the current North American Free Trade Agreement (NAFTA) which has been in place since 1994.The United States-Mexico-Canada Agreement (USMCA) gives the U.S. greater access to Canada's dairy market and allows extra imports of Canadian cars. The agreement was announced at month end when it previously looked as if Canada could be excluded from the final agreement. The deal which has 34 chapters and governs more than US$1trillion (£767billion) in trade, is intended to last 16 years and be reviewed every six years. The agreement contains updated arrangements for U.S. access to Canada's dairy industry, quotas on Canadian and Mexican car exports to the U.S., the requirement that 40% of vehicle car parts produced in the USMCA area must be made in areas of North America and protection for the Canadian lumber industry from US anti-dumping tariffs.

According to the U.S. Federal Reserve, industrial production rose 0.4% in August for its third consecutive monthly increase. Manufacturing output moved up 0.2% on the strength of a 4% rise for motor vehicles and parts. Excluding the gain in motor vehicles and parts, factory output was unchanged. The output of utilities advanced 1.2% and mining production increased 0.7%. Total industrial production was 4.9% higher than in August last year.

Industrial production in the Euro Area edged down 0.1% from a year earlier in July 2018, following a revised 2.3% growth in the previous month and missing the market consensus of a 1% increase. It was the first output contraction since January 2017 mainly due to declines in production of durable consumer goods and energy.

According to estimates from Eurostat, seasonally adjusted industrial production fell by 0.8% in July 2018 compared with June 2018 in the euro area (EA19) and by 0.7% in the EU28. In June 2018, industrial production fell by 0.8% in the euro area and by 0.5% in the EU28. Industrial production in the euro area in July 2018, decreased by 0.1% compared with July 2017, due to production of durable consumer goods falling by 2.3%, energy by 2.1%, non-durable consumer goods by 0.5% and intermediate goods by 0.1%, while production of capital goods rose by 1.4%.

The Office for National Statistics (ONS) said UK GDP increased by 0.4% in the second quarter, up from 0.2% in the previous quarter, helped by stronger retail sales and good weather which enabled the construction industry to make up lost ground. Service industries experienced growth of 0.5% in the second quarter, with the retail and wholesale sectors providing the strongest contribution. The figures however, show the economy increasingly reliant on the services sector amid a downturn for factory output. There were also indications of slowing growth in June, with the ONS figures showing May was the strongest month of the second quarter. The manufacturing industry recorded its second consecutive quarter of negative growth since the first quarter of 2016, meeting the official conditions for an economic recession, amid weaker international demand for British goods. While manufacturing output fell by 0.9%, its drag on overall economic growth was only about 0.1%. The biggest falls in output were in factories producing metal products and electrical equipment, where exports are important. Growth in the production industries – which include mining and energy alongside the manufacturing sector – fell by 0.8% as the warm weather reduced demand for heating.

Companies:

Prysmian Group published its first half 2018 results. Group sales amounted to €4,364 million, including €381 million sales generated by General Cable in June 2018. Excluding the General Cable's contribution and net of metal price variation and exchange rate effects, organic growth was +2% compared to H1 2017. Adjusted EBITDA was €339M of which €25M was attributable to General Cable. A solid uptrend of the Telecom sector was confirmed while there was growth in the High Voltage Underground and Trade & Installers businesses. Telecom grew sharply with rising margins thanks to higher volumes and industrial efficiencies. For the remainder of this year, the Group confirmed its forecasts for a full-combined adjusted EBITDA in the range of €860 and €920 million.

Market Commentary and News:

At the end of the month, Aurubis, Europe's biggest copper producer announced that it will offer its European customers a cathode premium of US$96/t over the LME cash basis for 2019 contract deliveries. This compares to US$86/t in both 2018 and 2017. Earlier in the month, traders reported that Codelco had signed 2019 copper cathode supply contracts with European consumers at a delivery premium of US$98/t basis CIF European Port delivery. That would be the highest level since 2015 and compares with its premium of US$88/t for 2018. Codelco is also reported to have signed copper supply contracts with Chinese clients at a delivery premium of US$88/t over LME basis. This compares with a premium of US$75/t for 2018 contracts. In recent history, both Codelco and Aurubis have set the benchmark cathode premiums for other producers to follow.

The global world refined copper market showed a 45,000t deficit in June, compared with a 50,000t deficit in May, the International Copper Study Group (ICSG) said in its latest monthly bulletin. For the first 6 months of the year, the market was in a 51,000t deficit compared with a 148,000t deficit in the same period a year earlier, the ICSG said.

According to metals consultancy CRU, outstanding and unresolved copper mine labour negotiations this year could affect nearly 1.9 million tonnes of annual production capacity. This follows completed negotiations year to date covering nearly 2.2 million tonnes of production. The details are;

Completed		**Outstanding**	
Mine	2018 Output Forecast (kt)	Mine	2018 Output Forecast (kt)
Escondida	945	El Teniente	456
Los Pelambres	354	MMH	187
Esperanza	149	Cerro Verde	470
Chuquicamata	275	Antamina	433
Andina	215	Cuajone	158
Radomiro Tomic	101	Toquepala	1522
Caserones	114		
	2153		1856

Chile produced 3.31Mt of copper in the first seven months of the year, an increase of 10.8% from the same period a year earlier, Chilean copper commission Cochilco said. Chile produced 481,700t of copper in July, an increase of 2.9% compared to July 2017, boosted by higher output at large, privately held mines. Copper production at Codelco, Chile's state-owned copper mining company, rose 2% in the first half of 2018 to 813,000t.

A company owned by Russian billionaire Alisher Usmanov's holding company said it had started construction of a massive mining and metallurgical plant at the Udokan copper deposit in a remote region in eastern Siberia. With total reserves of around 26.7 million tonnes of copper, this is the largest undeveloped copper deposit in Russia and one of the biggest in the world. Copper at the deposit is hard to extract due to the characteristics of the ore and because it is located in a remote area with poor infrastructure, high seismic activity and permafrost ground conditions.

Traders report that copper demand in China remains strong regardless of the threat to growth posed by the worsening trade war with the U.S. This optimism is based on expectations that China will step up investments in infrastructure to shore up its economy and that the barrage of tariffs on goods won't derail global growth. Cathode premiums at the Chinese port of Yangshan have risen to the highest level in almost three years and have soared some 50% since the end of July as importers lock in supplies. Inventories in SHFE warehouses have more than halved in about six months, signalling tightening supplies. At the same time, production has been rising as smelters expand capacity - refined copper output in August was 749Kt, giving a YTD production of 9.054Mt - up 3.4% on 2017. Imports of refined copper and concentrates are up strongly on a year earlier. Traders suggest that this is feeding sustained demand from copper fabricators of pipes and wires for air conditioning and power supplies.

Global mining giants Freeport McMoRan Inc and Rio Tinto have struck a binding accord to sell a majority stake in the world's second-biggest copper mine, Grasberg, to Indonesia's state mining company, Inalum for US$3.85 billion. The sale brings Freeport close to ending more than nine years of often fractious negotiations with Indonesia over ownership rights to Grasberg.

Participants in the aluminium industry met at the annual Metal Bulletin Aluminium Conference in Berlin in September where the main talking point was the sanctions imposed against Russian producer Rusal. Uncertainty about the situation divided opinion as more than half the delegates polled thought that the sanctions would be lifted some time in 2019. But traders admitted that the lack of liquidity in the market was due to the uncertainty about whether the sanctions would be lifted by October 23 - the deadline date for US companies to end their dealings with the Russian company. Traders had previously reported that European customers who to date had been sanguine about the fallout from Rusal sanctions on expectations they would be lifted in October, are now avoiding deals with Rusal on the basis that they could remain in place. One unnamed source said; “Anyone that has a relationship with Rusal will be preparing for the sanctions to remain in place for now. People do not want to lose out and do the wrong trade. If the sanctions are lifted, or remain in place, the market could be a very different place.” The position remains just as unclear even as the U.S. Treasury subsequently tweaked its sanctions to allow Rusal to enter into new contracts with existing U.S. customers.

The start of aluminium production at Rusal’s Taishet aluminium smelter in Russia has been postponed until after 2020, Russia's economy ministry said. Rusal had previously planned to build the first line of the Siberian smelter, with an annual capacity of 430,000t by 2020.

According to U.S. analysts and aluminium makers, aluminium tariffs aimed at boosting U.S. producers’ profits appear to be having the opposite effect. Together with sanctions against Russian producer Rusal, they have pushed up prices for alumina, aluminium’s key ingredient, eating into the profits of U.S. producers. Companies that had previously purchased alumina from Rusal have been scrambling to get supplies from other producers, squeezing limited supplies. Production curbs at the world’s largest alumina refinery in Brazil and a strike by workers at aluminium giant Alcoa have also put pressure on alumina prices. Through mid-September, alumina prices had surged about 60% from a year ago to US$625/t, according to commodities analysts at CRU.

Market reports at month-end suggest that Chinese authorities had decided not to impose blanket cuts on industrial output in 28 northern cities this winter. The production cuts are instead to be determined by local authorities. On this basis, market analysts are expecting less restrictions on aluminium production.

On September 28, unionised workers at aluminium producer Alcoa's Western Australian operations agreed to end a strike that lasted more than six weeks after securing better job security provisions in a new wage agreement. Workers at two alumina refineries and three bauxite mines walked out on August 8 because of concerns about a new workplace agreement.

Norwegian aluminium maker Norsk Hydro said that it had signed two deals with Brazilian authorities involving social and environmental obligations, in a move that could pave the way for a resumption of full output at the company's Alunorte alumina refinery that was accused of polluting the environment. The deals include payments for food cards for nearby families and investments for the social development of local communities, as well as technical improvements, the company said in a statement.

China's aluminium producers cut output by 3% in August from the month before, government data showed mid-month, as high raw material costs squeeze their profit margins. China, the world's biggest aluminium producer, produced out 2.84 million tonnes in August, according to the National Bureau of Statistics. That was down from 2.93 million tonnes in July, which matched the all-time monthly high, but was up 7.8% from a year earlier, the NBS said. On a daily basis, China produced around 91,600t of primary aluminium in August, the lowest since May, according to Reuters calculations.

Some Japanese aluminium buyers have agreed to pay a global producer a premium of $103/t for shipments in the October to December quarter, reflecting lower spot premiums, sources reported. The premium is 22% lower than the $132/t premium in the current quarter and follows three quarters of rising premiums.

The LME will maintain its discounted fees for carry trades indefinitely as it believes the discounts have had a positive impact on trading volumes, the mainstay of the exchange's revenue. The exchange cut fees for short and medium-dated carry trades for its members and clients on October 1 last year for a trial period that was due to expire at the end of October this year.

The LME's clearing house may not be immediately allowed to provide services for members in European Economic Area (EEA) countries after Britain leaves the EU, the exchange said on its website. European Securities and Markets Authority recently advised that the exchange may not be able to apply to become a recognised third country clearing house until after Brexit, the LME said.

Major Chinese broker Nanhua Futures is planning to start trading on the LME in the first half of next year. Nanhua's move comes as Chinese conglomerate Fosun International holds talks to buy Marex Spectron, one of the biggest brokers on the LME. Chinese banks and brokers have sought to capitalize on their country's growing role as a major metal producer and consumer, but they have yet to become major players on the LME. Many have seen their ambitious plans for trading metals hit by institutional red tape, cultural clashes and lack of clear strategy, according to sources. Five Chinese institutions are already running trading operations on the LME as clearing members and industry sources said at least four others - besides Nanhua and Fosun - are considering doing so. Chinese groups were attracted to the LME after the US$2.2 billion takeover by Hong Kong Exchanges Ltd in 2012.

The Shanghai Futures Exchange (ShFE) has launched copper options trading, aiming to take a slice of a $270 billion global market in one of its biggest challenges yet to London and New York rivals. The product comes as the exchange also considers opening its flagship copper futures to foreign investors and is a major step in China's prolonged effort to develop its derivatives industry. Over the past decade, the Shanghai bourse which was set up in 1999 has carved out a bigger share of the global copper futures market, challenging the LME’s dominance.

LME Commentary:

LME participants continue to fixate on the trade dispute between China and the U.S. which has chilled factory activity in August, tempered appetite for metals and confused investor sentiment.

Copper prices came under selling pressure during the first half of the month, largely mirroring the downward trend in the commodities sector. Battered by concerns about the worsening trade war and Trump’s threat to further ratchet up trade tariffs, the LME GBP copper cash price fell to a 15-month low at £4465.44/t on 17 September – some £956.36/t or 17.6% below the year’s high of £5421.80/t on June 6. The USD cash price had hit a similar multi-month low earlier in the month at $5823/t. Consistent with the unpredictable nature of the market and based on speculation that demand will continue to grow - that the escalating trade war won’t derail the global expansion - within 7 days the price had recovered to its September high of £4804.99/t - the highest since early July this year.

LME copper stocks continue to fall and closed the month at 199,125t, down 63,350t in the month and below 200,000t for the first time since December last year. Stockpiles tracked by the Shanghai Futures Exchange have almost halved this year and are at their lowest levels in 11 months having closed the month at 111,995t.

Primary aluminium prices on the LME were not immune from trade/tariff tensions, followed the general weakness in the metals sector and failed to maintain the positive tone witnessed at the end of August. The GBP cash price which hit a low of £1507.38/t on September 19 was the lowest since April and some £320.73/t or 17.5% below the year’s high of £1828.11/t also achieved in April. News that China would not re-impose its blanket restrictions on industrial output in 28 northern cities thereby anticipating less restrictions on aluminium production meant aluminium prices closed the month on a quiet note.

This weakness continues despite reports of tightness in the physical aluminium market and declining exchange stocks. LME stocks closed the month at 987,800t, falling below 1 million tonnes for the first time since March 2008 and compare with the year’s high of 1,412,500t, the 2017 year- end stock of 1,101,375t and some way below the 5 million tonne levels last seen in April 2014.

LME Statistics and Charts: September 2018:

	Copper			Aluminium			
	Cash £/t	3M £/t	Stocks	Cash $/t	Cash £/t	Stocks	USD:GBP
Opening	4623.57	4616.52	262,475	2083.50	1,618.76	1,068,675	1.2871
Average	4611.58	4604.94		2023.00	1550.02		1.3053
High	4804.99	4785.72		2083.50	1618.76		1.3280
Low	4465.44	4463.76		1981.00	1507.38		1.2820
Range	339.55	321.96		102.50	111.38		0.0460
Closing	4738.17	4716.12	199,125	2011.50	1542.21	987,800	1.2820
Opening:Closing Δ	-114.6	-99.6	-+63,350	-72.00	-76.55	-80,875	
YTD Average	4912.02	4913.75		2157.23	1596.74		
YTD High	5421.80	5402.51		2602.50	1828.11		
YTD Low	4465.44	4463.76		1967.00	1403.52		

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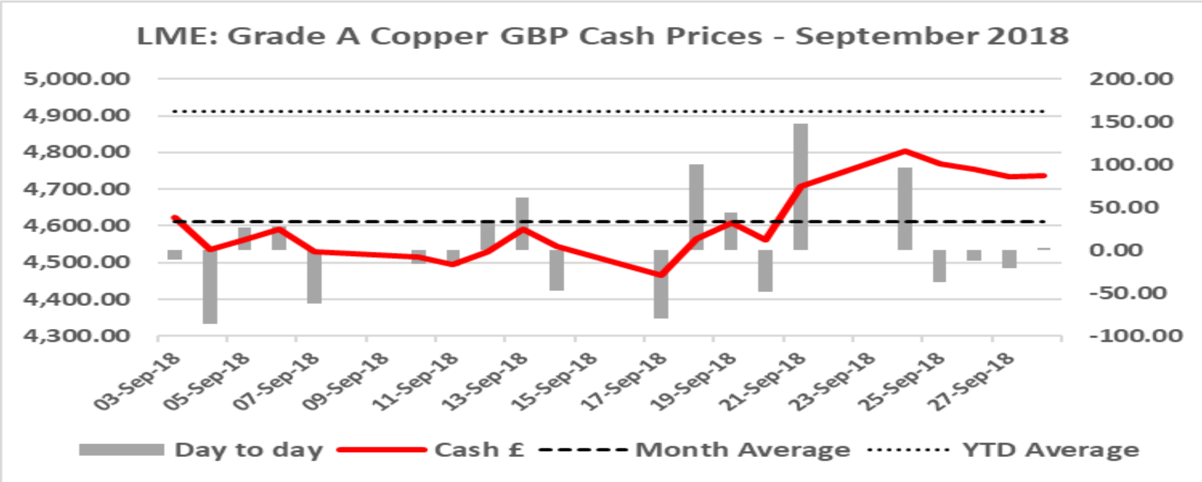

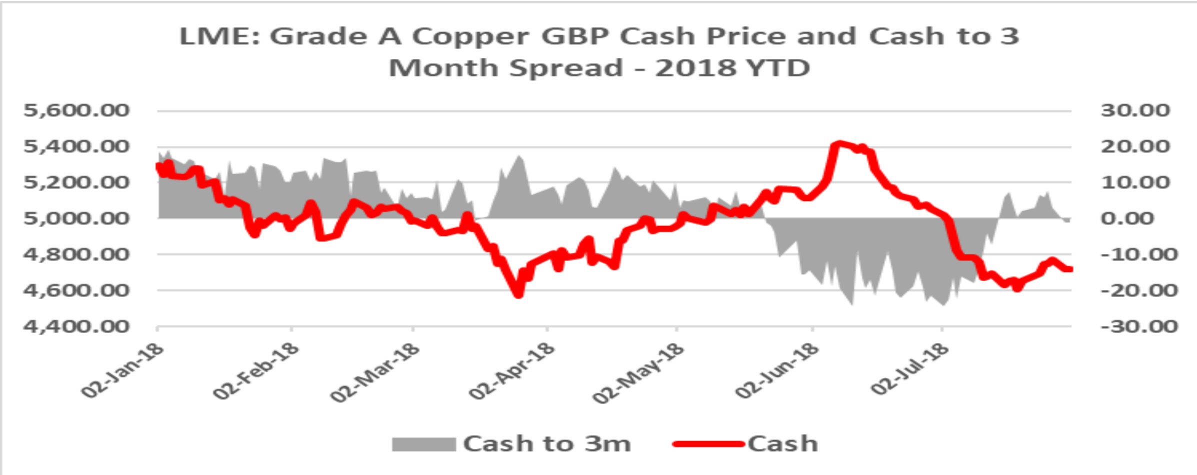

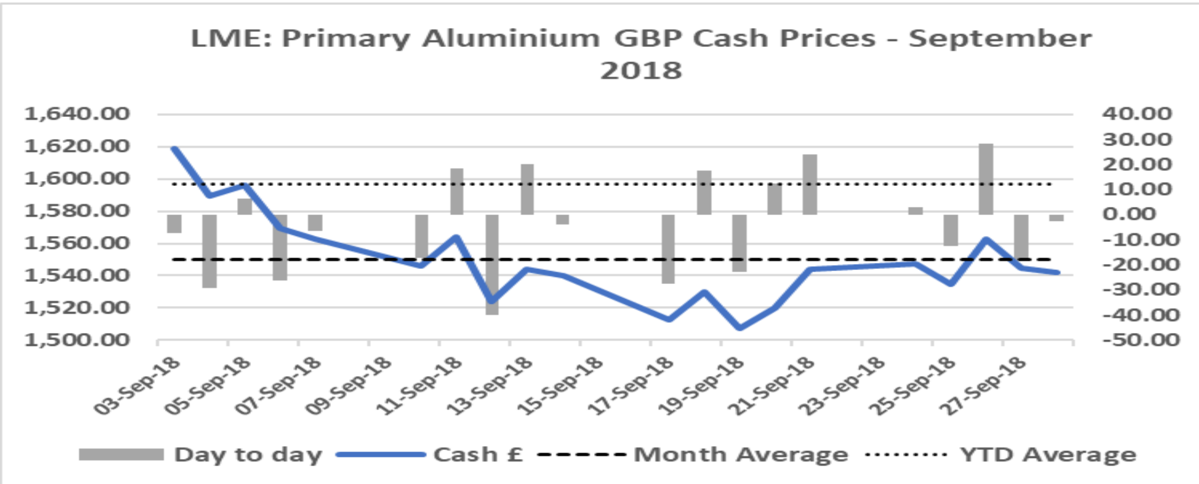

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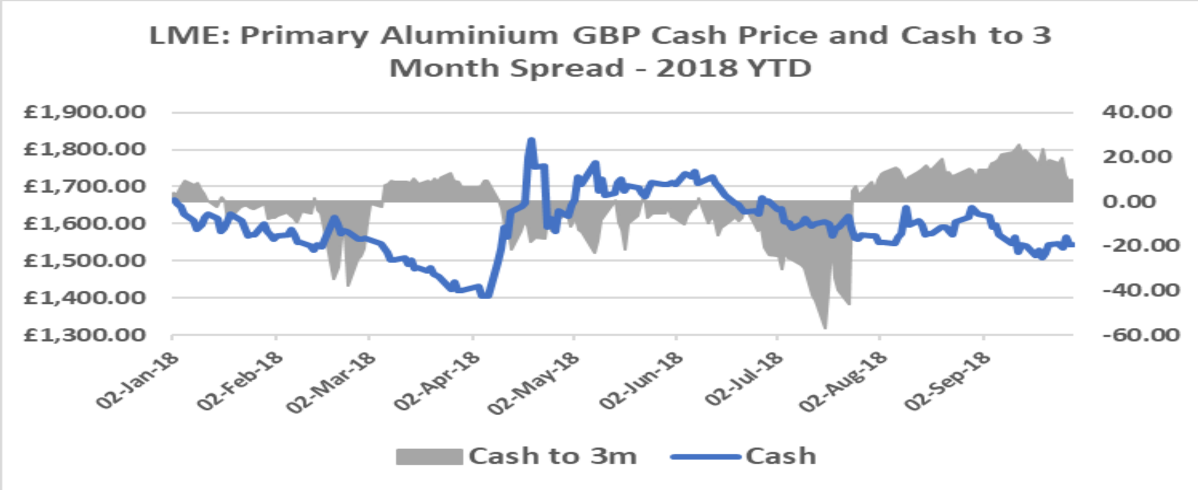

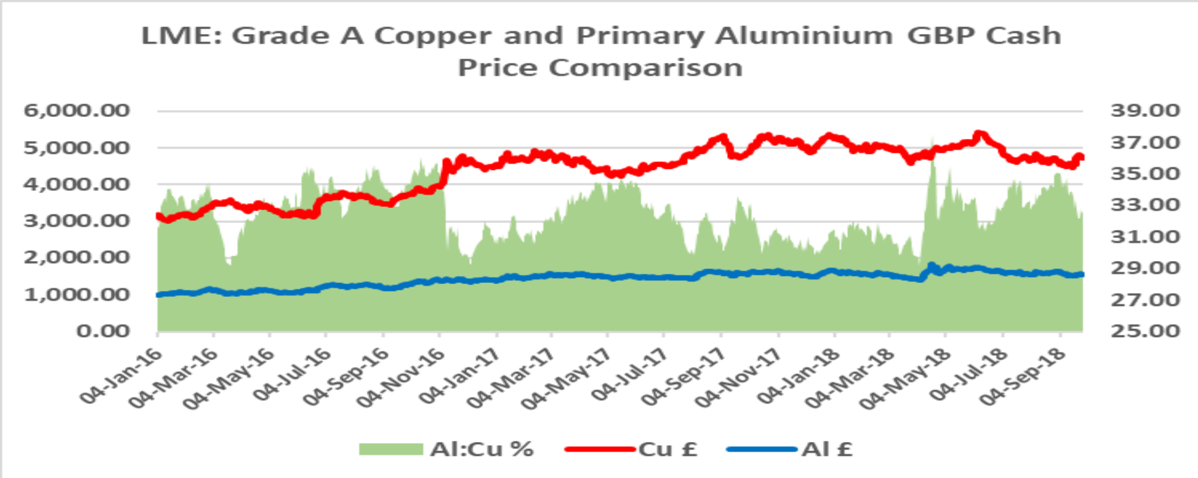

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