



China Sourcing Update

February 27, 2019

Energy Costs

1. Crude prices rebound strongly in January

In line with the movement of global crude prices, China's crude prices continued to rebound in early January, and then showed fluctuations in mid- to late January.¹ For instance, the Daqing² crude price rose markedly from its recent low of US\$ 41.8 per barrel on 26 December to US\$ 53.57 per barrel on 11 January, before fluctuating within a range of US\$ 50.98 per barrel to US\$ 54.02 per barrel during the rest of the month (see *exhibit 1*).

The global crude prices have rebounded since late December due mainly to the following two reasons. First, there have been signs that the OPEC and some other major oil producing countries are determined to reduce their crude oil output after making an agreement of production cuts on 7 December.³ For example, Russian Energy Minister Alexander Novak said on 25 December that the global crude prices would become more stable in 1H19 due to the production cuts. Moreover, Saudi Arabia's Energy Minister Khalid al-Fali said on 10 January that his country would further reduce its crude output in February.⁴ Second, in response to the intensifying political crisis in Venezuela, the US government announced on 28 January that it would impose sanctions against Petroleos de Venezuela, S.A., a Venezuelan state-owned oil

¹ From the year 2000 onwards, China's crude prices were determined with reference to global crude prices.

² Daqing Field is the largest oil field in China.

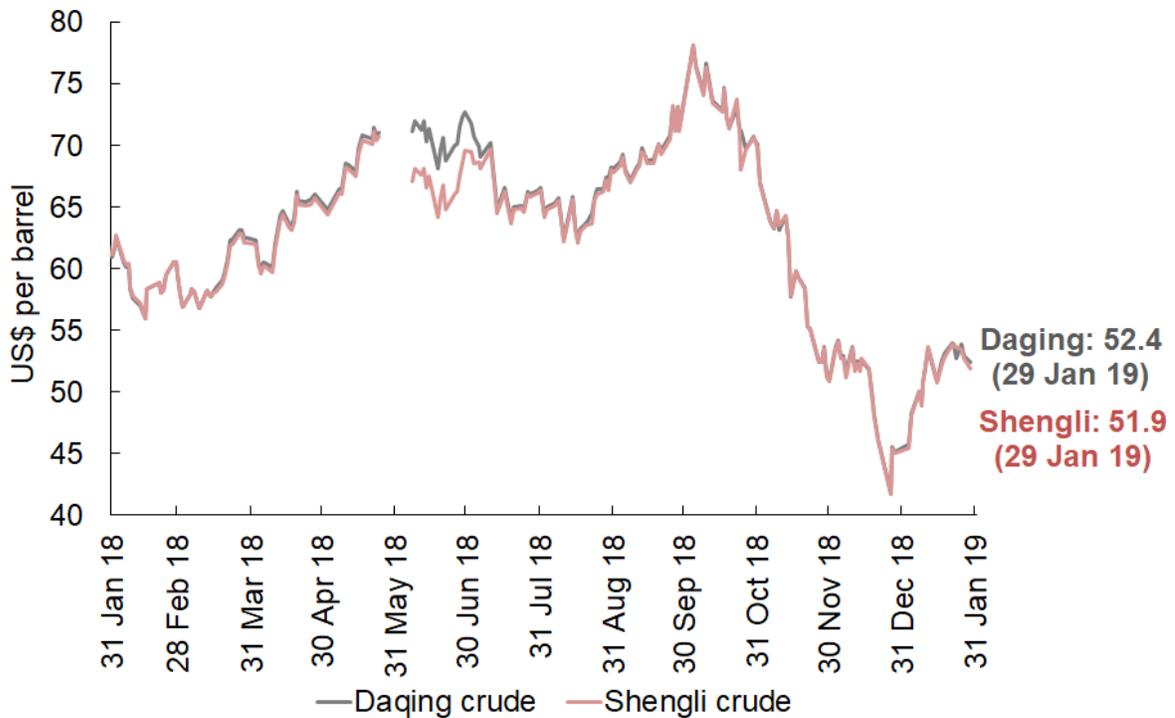
³ On 7 December, OPEC members and some non-OPEC oil producing countries agreed to cut their crude output by 1.2 million barrels per day in the first six months of 2019.

⁴ <https://www.reuters.com/article/us-saudi-oil-cuts-idUSKBN14W1Y5?il=0>

company, in order to put more pressure on Venezuela’s leader Maduro to transfer his power to the self-proclaimed Interim President Juan Guaidó.⁵ As Venezuela is one of the major source countries of the US oil imports, the sanction is set to have an impact on the oil supply and thus the crude prices in the US.

Looking ahead, we do not expect the global crude prices to rise much in the near future as the global demand for the crude is likely to moderate amid weaker growth of the global economy this year. According to the latest forecasts by the International Monetary Fund (IMF) on 21 January, the world’s economic growth is projected to decelerate to 3.5% in 2019 from 3.7% in 2018.⁶

Exhibit 1: China’s crude prices, January 2018 to January 2019



Source: ifeng.com, gcec.com.cn

⁵ <https://home.treasury.gov/news/press-releases/sm594>

⁶ IMF, *World Economic Outlook Update*, January 2019

2. Wholesale price index of refined oil products drops in January

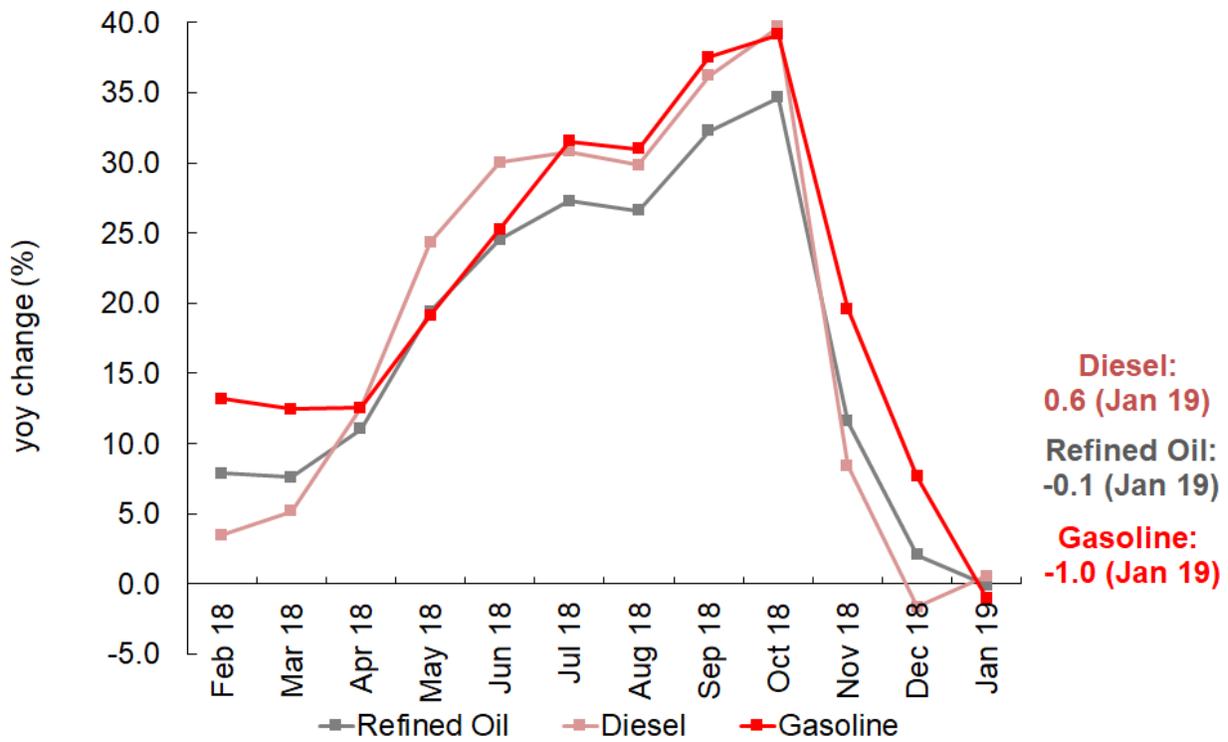
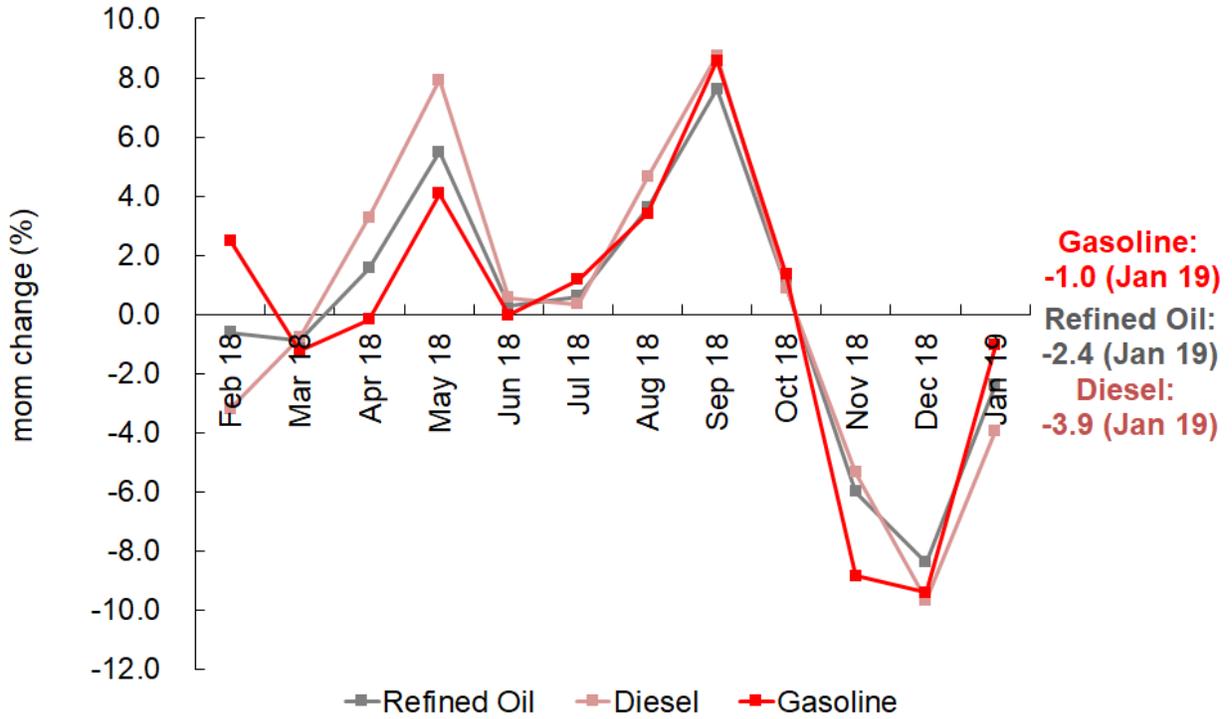
The wholesale price index of refined oil products fell by 2.4% mom in January (see *exhibit 2*).⁷ Specifically, the wholesale price index of diesel dropped by 3.9% mom, while that of gasoline decreased by 1.0% mom.

According to the pricing mechanism for refined oil products, the maximum prices of diesel and gasoline are adjusted every 10 working days, based on the change in a basket of global crude prices. In response to a fall in global crude prices during mid- to late December, the National Development and Reform Commission (NDRC) reduced the maximum wholesale prices of gasoline and diesel by 370 yuan and 355 yuan respectively on 29 December. Afterwards, as global crude prices rebounded in the following weeks, the NDRC raised the maximum wholesale prices of gasoline and diesel by 105 yuan on 15 January. Then, on 29 January, the prices of gasoline and diesel were further increased by 245 yuan and 230 yuan respectively.

Looking ahead, we expect the wholesale price index of refined oil products to rebound in February, as the NDRC raised the maximum wholesale prices of diesel and gasoline again on 15 February due to a rise in global crude prices during mid-February.

⁷ The index is compiled by the China Logistics Information Center (CLIC).

Exhibit 2: China's wholesale price indices of refined oil products, February 2018 to January 2019



Source: China Logistics Information Center

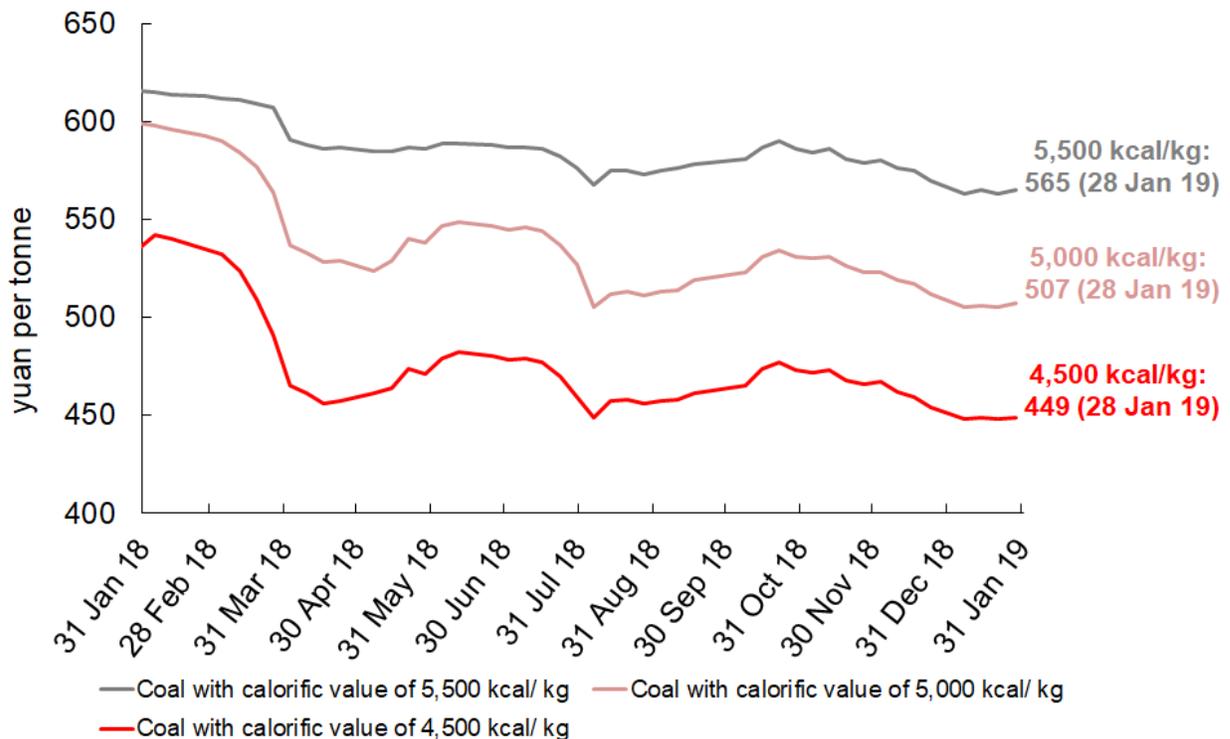
3. Benchmark Qinhuangdao coal prices stabilise in January

After trending downward throughout late October to December, the benchmark Qinhuangdao coal prices stabilised in January (see exhibit 3). For example, the price of coal with calorific value of 5,000 kcal/ kg was 507 yuan per tonne on 28 January, compared to 512 yuan per tonne on 24 December.

The stabilisation in the domestic coal prices in January was attributable to a tightening supply of coal. On 12 January, a coal mine in Shenmu county in Shaanxi province collapsed and thus 21 people were killed. Afterwards, the Chinese government ordered a number of coal mines in several provinces to shut down their operations for safety checks, according to media reports.⁸

According to media reports, the market sentiments on coal have improved after the collapse of the coal mine. Therefore, we expect that the coal prices will trend upward in February.

Exhibit 3: Qinhuangdao coal prices, January 2018 to January 2019



Source: ifeng.com, cctd.com.cn

⁸ <https://www.hellenicshippingnews.com/chinas-domestic-thermal-coal-prices-under-close-watch-ahead-of-key-political-meetings-sources/>

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