



# China Sourcing Update

December 20, 2018

## Energy Costs

### 1. Crude prices plunge in November

In line with the movement of global crude prices, China's crude prices plunged in November.<sup>1</sup> For instance, the Daqing<sup>2</sup> crude price dropped markedly from US\$70.1 per barrel on 31 October to US\$51.02 per barrel on 30 November (see exhibit 1).

In our view, the plunge in the global oil prices was highly associated with the announcement made by the US government on 5 November that it allows eight countries to continue to import crude oil from Iran, despite the introduction of the US sanctions on the country's oil exports on the same day. The announcement triggered market concerns about an oversupply of the global crude in the coming future as several major oil producers had already increased their crude output in order to offset the potential loss of Iran's crude supply.

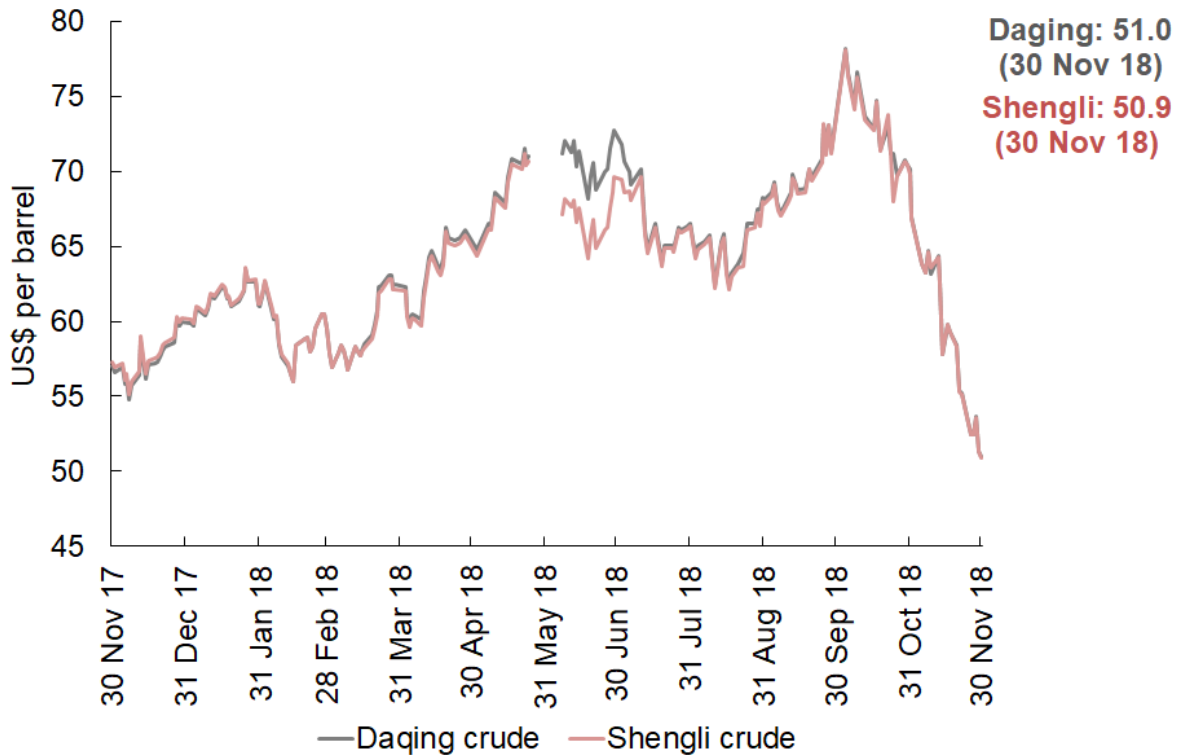
Afterwards, on 7 December, OPEC members and some non-OPEC oil producing countries agreed to cut their crude output by 1.2 million barrels per day in the first six months of 2019. In spite of such an action, we still expect the global crude prices to drop further in the near future, as the demand for global crude is likely to weaken given the recent signs of a slowdown of the global economy. For example, China's manufacturing PMI, a leading indicator of the Chinese economy, fell to a 28-month low

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

<sup>2</sup> Daqing Field is the largest oil field in China.

of 50.0 in November while the Eurozone's PMI dropped to 51.8 in November, the lowest level since August 2016.

**Exhibit 1: China's crude prices, November 2017 to November 2018**



Source: ifeng.com, gcec.com.cn

## 2. Wholesale price index of refined oil products drops in November

The wholesale price index of refined oil products fell by 6.0% mom in November (see exhibit 2).<sup>3</sup> Specifically, the wholesale price index of diesel dropped by 5.3% mom, while that of gasoline decreased by 8.8% mom.

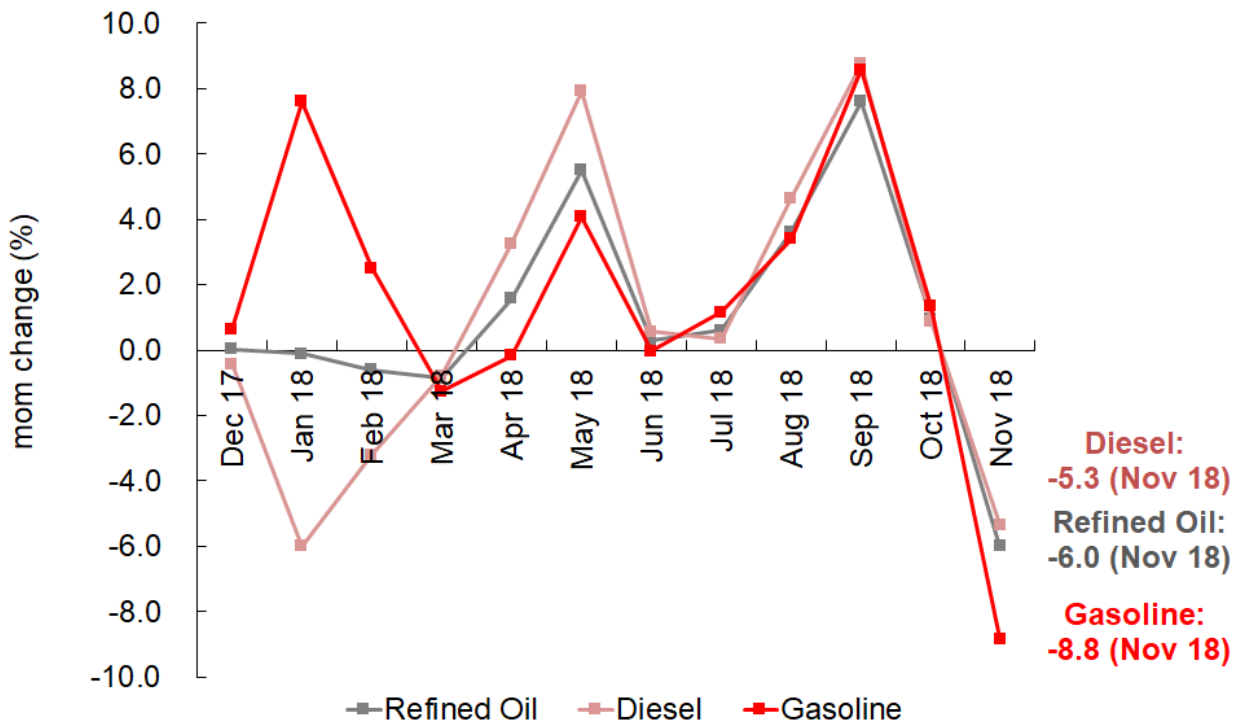
In response to a fall in global crude prices during late October to mid-November, the National Development and Reform Commission (NDRC) made downward adjustments to the maximum wholesale prices of refined oil products on 3 November and 17 November. According to the pricing mechanism for refined oil products, the maximum

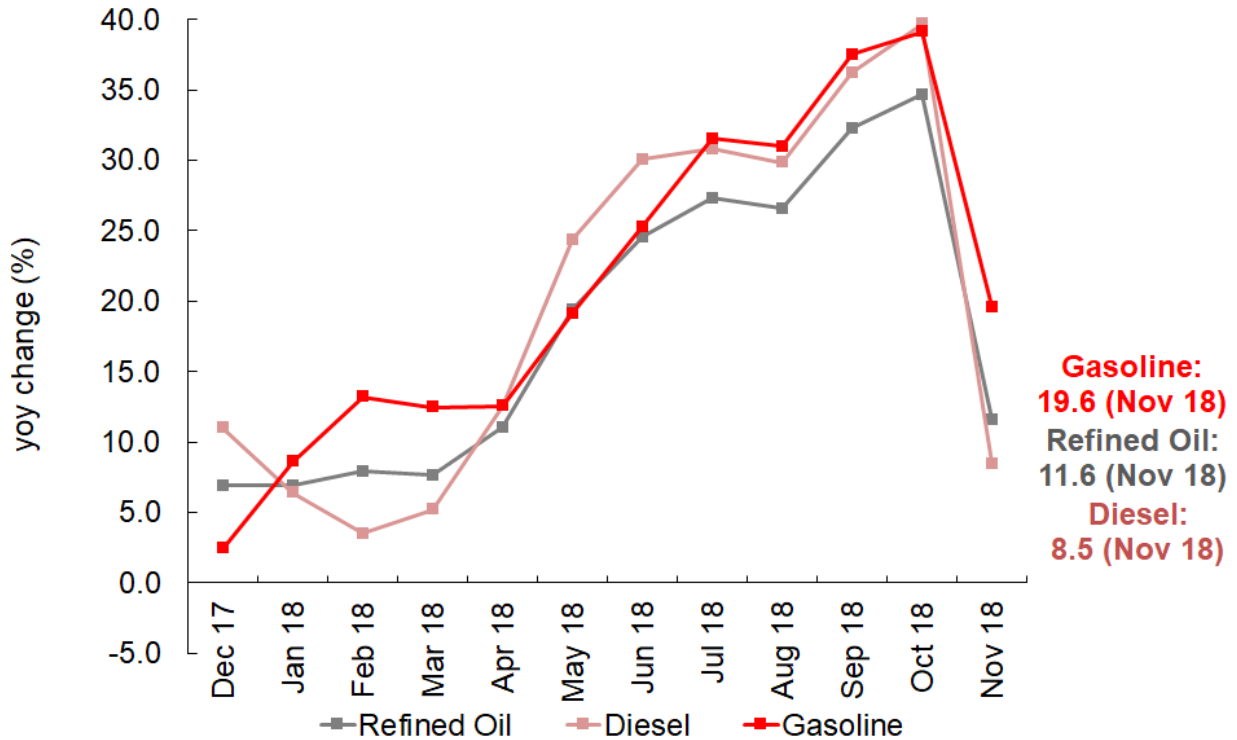
<sup>3</sup> The index is compiled by the China Logistics Information Center (CLIC).

prices of diesel and gasoline are adjusted every 10 working days, based on the change in a basket of global crude prices.

Looking ahead, we expect the wholesale price index of refined oil products to go down further in December, as the NDRC reduced the maximum wholesale prices of diesel and gasoline on 1 December and 15 December due to a fall in global crude prices during late November to mid-December.

**Exhibit 2: China's wholesale price indices of refined oil products, December 2017 to November 2018**





Source: China Logistics Information Center

### 3. Benchmark Qinhuangdao coal prices drop in November

The benchmark Qinhuangdao coal prices stayed relatively stable in early November and moderated a bit afterwards (see exhibit 3). For example, the price of coal with calorific value of 5,000 kcal/ kg stayed around 530 yuan per tonne during 29 October to 12 November, before dropping to 523 yuan per tonne on 26 November.

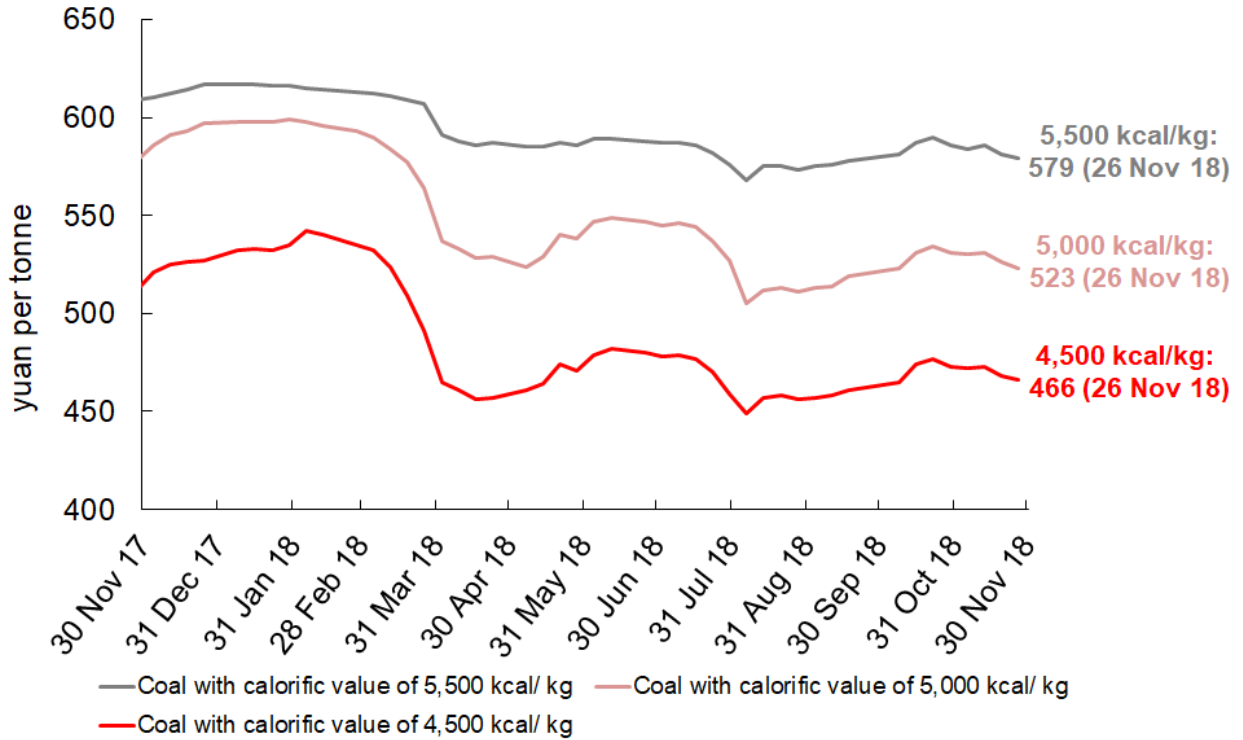
The slight fall in the domestic coal prices in November was attributable to a weak downstream demand for coal given the low consumption of coal of power producers. According to media reports, daily consumption of coal by six major power producers in coastal provinces posted a deeper year-on-year decline during 17-23 November, compared to 1-16 November.<sup>4</sup>

Looking ahead, we expect the domestic coal prices to fall further in the near term due to the following reasons. First, the demand for coal has weakened amid the growth

<sup>4</sup> <https://www.cctd.com.cn/show-463-185610-1.html>

moderation of the Chinese economy. Second, inventory levels of coal held by power producers have remained high recently.

**Exhibit 3: Qinhuangdao coal prices, November 2017 to November 2018**



Source: ifeng.com, cctd.com.cn

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## CONTACT

Helen Chin  
Vice President  
[helenchin@fung1937.com](mailto:helenchin@fung1937.com)  
(852) 2300 2471

Timothy Cheung  
Senior Research Manager  
[timothycheung@fung1937.com](mailto:timothycheung@fung1937.com)  
(852) 2300 2477

Global Sourcing  
Fung Business Intelligence  
10/F LiFung Tower  
888 Cheung Sha Wan Road  
Kowloon, Hong Kong

T: (852) 2300 2470  
F: (852) 2635 1598  
E: [fbicgroup@fung1937.com](mailto:fbicgroup@fung1937.com)  
W: <http://www.fbicgroup.com>



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