



# China Sourcing Update

November 22, 2018

## Energy Costs

### 1. Crude prices fall in October

In line with the movement of global crude prices, China's crude prices soared in early October and plunged afterwards.<sup>1</sup> For instance, the Daqing<sup>2</sup> crude price jumped from US\$71.4 per barrel on 28 September to its recent peak of US\$78.2 per barrel on 4 October, before falling markedly to US\$70.1 per barrel on 31 October (*see exhibit 1*).

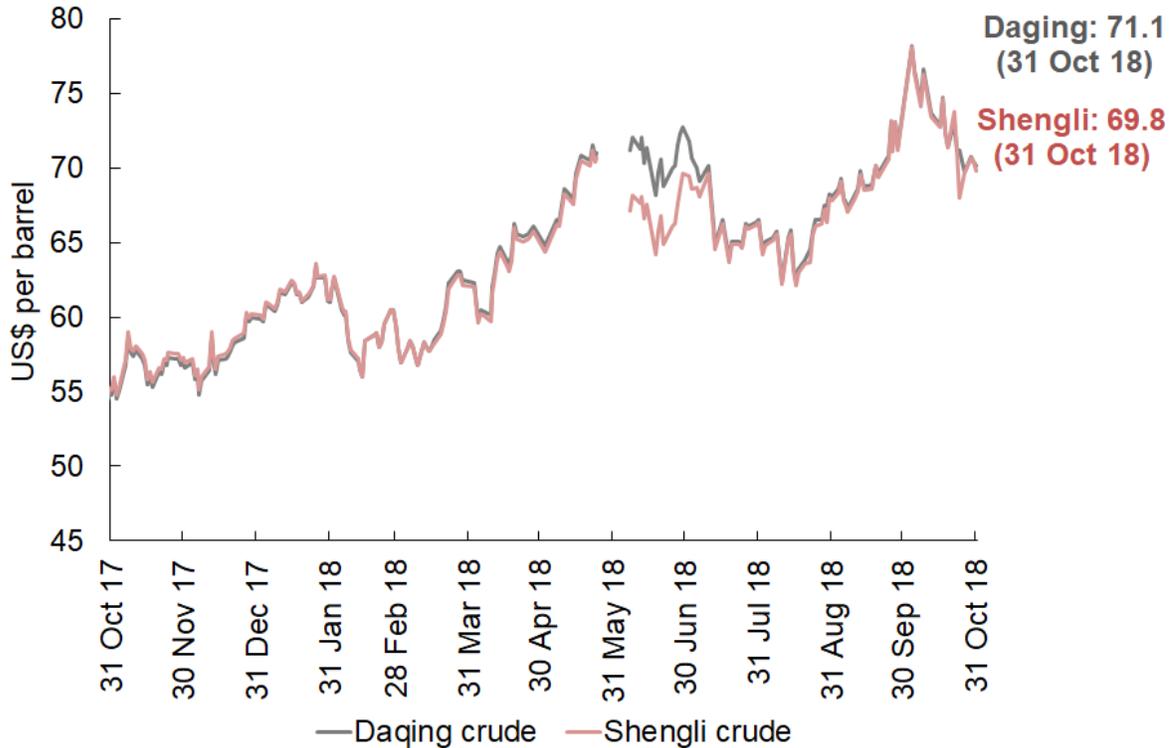
The marked fall in the global prices in October was caused by two main reasons, in our view. First, a rise in US bond yields triggered a sell-off in risky assets, including equities and commodities, in October. Second, the US and Saudi Arabia increased their crude output to offset the potential loss of Iran's crude supply due to the sanctions on the country's oil exports, which took effect on 4 November.

On 5 November, the US government unexpectedly announced to allow eight countries to continue to import crude oil from Iran. The announcement reduced the market expectations of a sharp drop in future supply of crude. Meanwhile, the latest figures suggest that the global economy has shown signs of slowdown lately. For example, the real GDP growth in China fell to 6.5% yoy in 3Q18 from 6.7% yoy in 2Q18, while that in the Eurozone dropped to 1.7% yoy in 3Q18 from 2.2% yoy in 2Q18. All in all, we expect the global crude prices to fall further soon.

<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.

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



Source: ifeng.com, gcec.com.cn

## 2. Wholesale price index of refined oil products rises in October

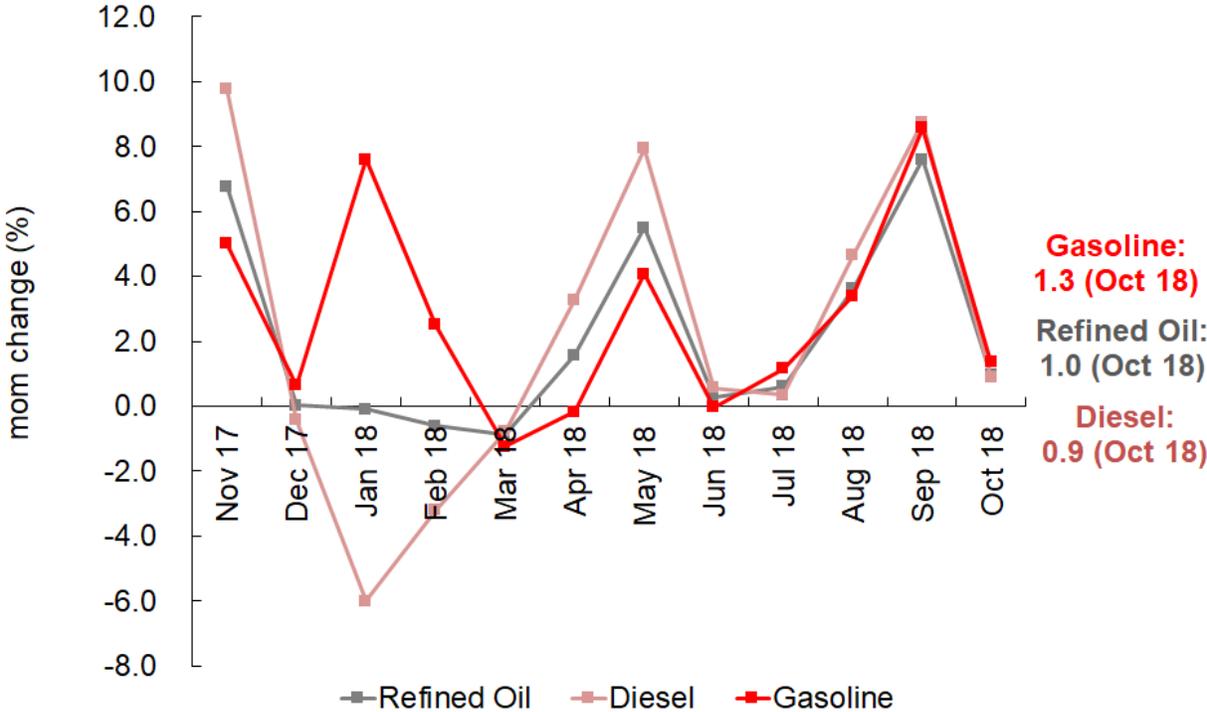
The wholesale price index of refined oil products gained 1.0% mom in October (see exhibit 2).<sup>3</sup> Specifically, the wholesale price index of diesel rose by 0.9% mom, while that of gasoline increased by 1.3% mom.

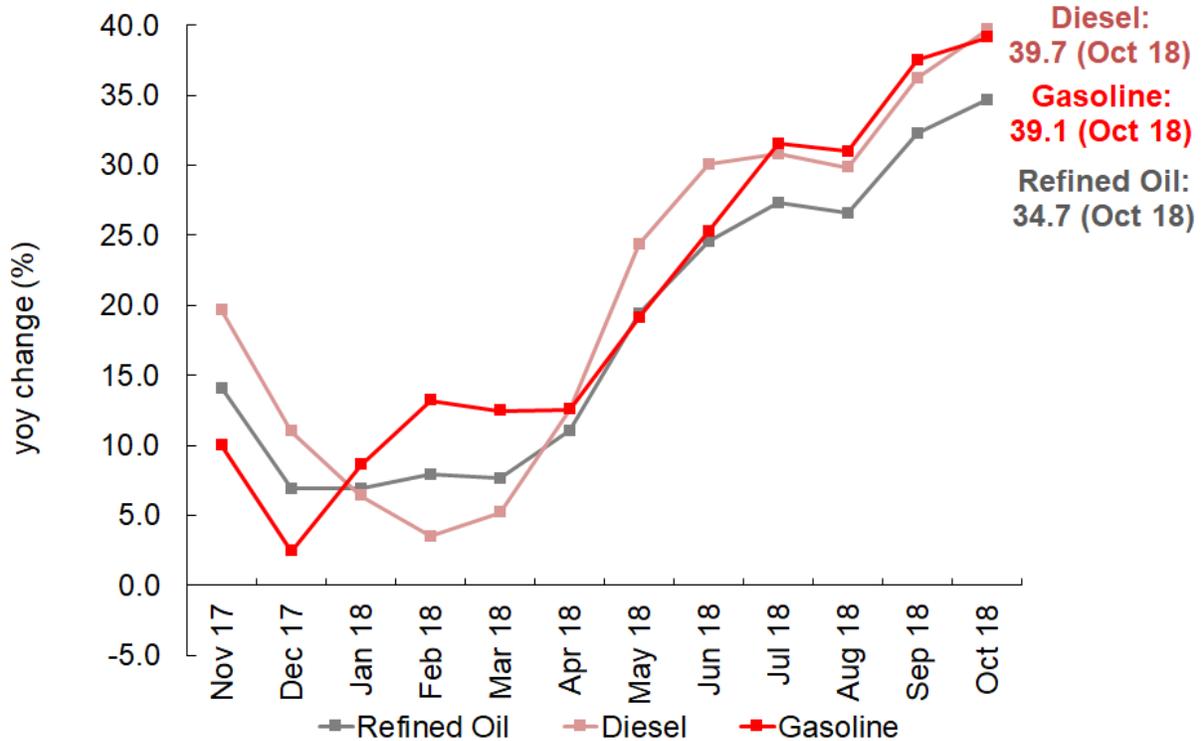
Following a rise in global crude prices during late September to early October, the National Development and Reform Commission (NDRC) made upward adjustments to the maximum wholesale prices of refined oil products on 1 October and 20 October. According to the pricing mechanism for refined oil products, the maximum prices of diesel and gasoline are adjusted every 10 working days, based on the change in a basket of global crude prices.

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

Looking ahead, we expect the wholesale price index of refined oil products to go down in November, as the NDRC reduced the maximum prices of diesel and gasoline on 3 November and 17 November in response to a drop in global crude prices during mid-October to mid-November.

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





Source: China Logistics Information Center

### 3. Benchmark Qinhuangdao coal prices rise in early to mid-October

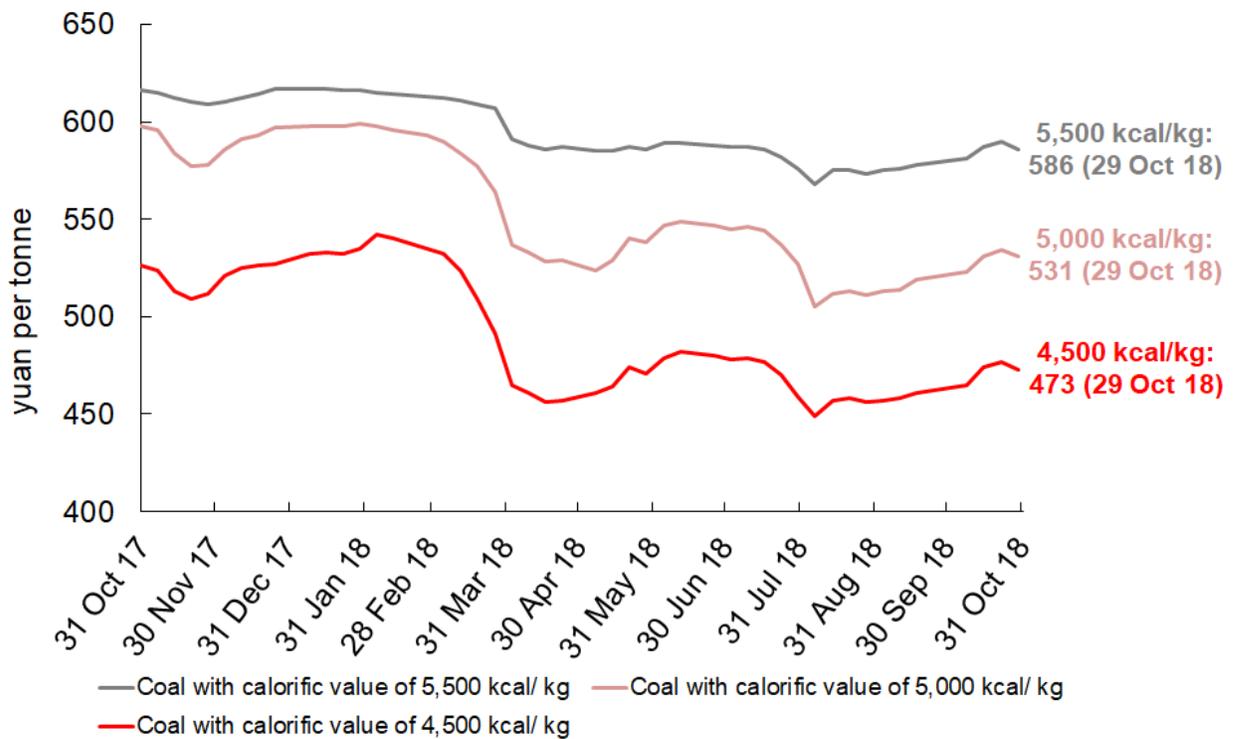
The benchmark Qinhuangdao coal prices went up in early to mid-October and moderated a bit afterwards (see exhibit 3). For example, the price of coal with calorific value of 5,000 kcal/ kg climbed from 523 yuan per tonne on 8 October to 534 yuan per tonne on 22 October, before dropping slightly to 531 yuan per tonne on 29 October.

The increase in the domestic coal prices in early to mid-October was due mainly to a tightened supply, as the Datong-Qinhuangdao Railway, the major rail line transporting coal from major coal-producing regions such as Shanxi and Inner Mongolia to Qinhuangdao, began a 25-day maintenance on 29 September until 23 October, leading to a drop in coal delivery to Qinhuangdao. Moreover, according to media, power producers in Anhui, Jiangsu, Zhejiang and Shandong increased purchases of coal in October. The purpose of the move was to increase their inventories of coal by early November. As the Chinese government had to ensure air quality in Shanghai where the China International Import Expo was held during 5-10 November, thermal power

producers in the abovementioned provinces were not allowed to transport coal via vehicles and ships during 1-14 November.

Looking ahead, we do not expect the uptrend of domestic coal prices to continue in the near term due to the following reasons. First, the maintenance of the Datong-Qinhuangdao Railway completed in late October. Second, the demand for coal has weakened amid the growth moderation of the Chinese economy. Third, inventory levels of coal held by power producers have been high recently.

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



Source: ifeng.com, cctd.com.cn

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