



China Sourcing Update

October 25, 2018

Energy Costs

1. Crude prices jump in the second half of September

In line with the movement of global crude prices, China's crude prices fluctuated within a narrow range during early to mid-September and rose in the second half of September.¹ For instance, the Daqing² crude price hovered around US\$68 per barrel in the first half of September, and then went up to US\$73.1 per barrel on 25 September, before retreating to US\$71.4 per barrel on 28 September (see *exhibit 1*).

Global crude prices surged in the second half of September on market concerns over a tightening global crude supply. First, the US crude oil inventories fell continuously: the US Energy Information Administration (EIA) reported on 19 September that commercial crude oil inventories (excluding those in the Strategic Petroleum Reserve) in the US dropped for the fifth consecutive week in the week ending 14 September.

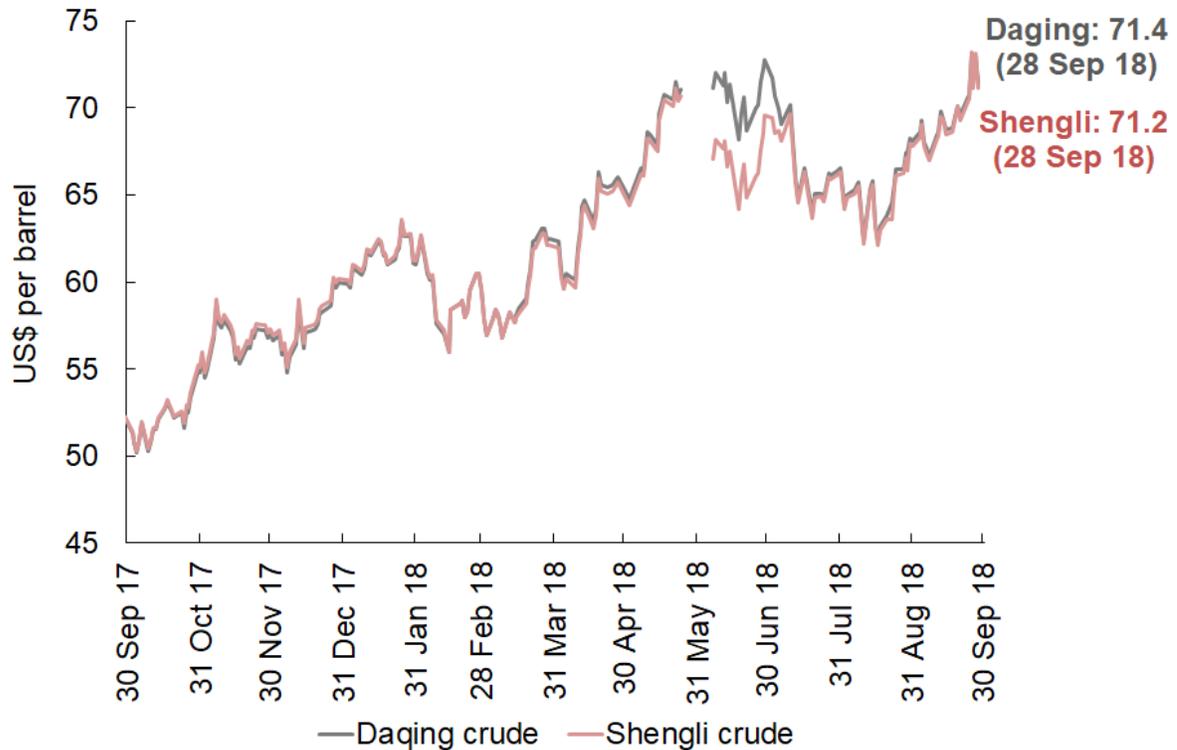
Second, member countries of the Organization of the Petroleum Exporting Countries (OPEC) and other major oil producers including Russia met on 23 September and ruled out any immediate increase in crude output. This is despite the US's repeated calls for output increase to offset the potential loss of Iran's crude supply due to the US sanctions on the country's oil exports, which will take effect on 4 November.

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.

Looking ahead, we expect that global crude prices will trend downward in the near future amid the recent increased volatility in global financial markets.

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



Source: ifeng.com, gcec.com.cn

2. Wholesale price index of refined oil products jumps in September

The wholesale price index of refined oil products soared by 7.6% mom in September (see exhibit 2).³ Specifically, the wholesale price index of diesel surged by 8.8% mom, while that of gasoline rose by 8.6% mom.

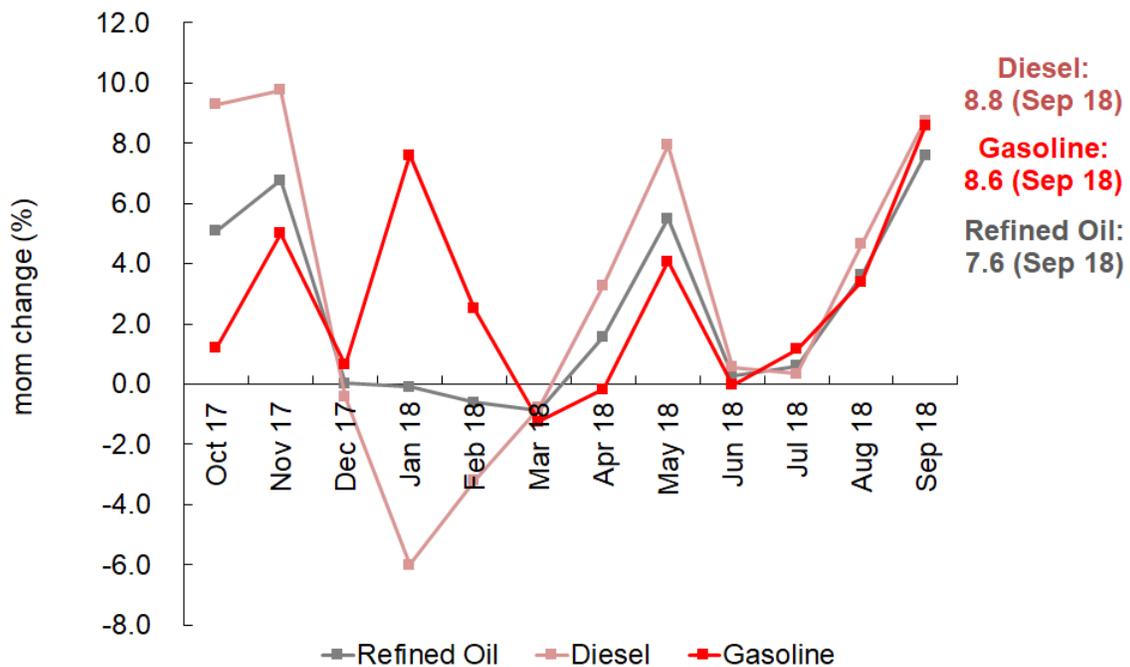
Following a rise in global crude prices during late August to mid-September, the National Development and Reform Commission (NDRC) made upward adjustments to the maximum wholesale prices of refined oil products on 4 September and 18 September. According to the pricing mechanism for refined oil products, the maximum

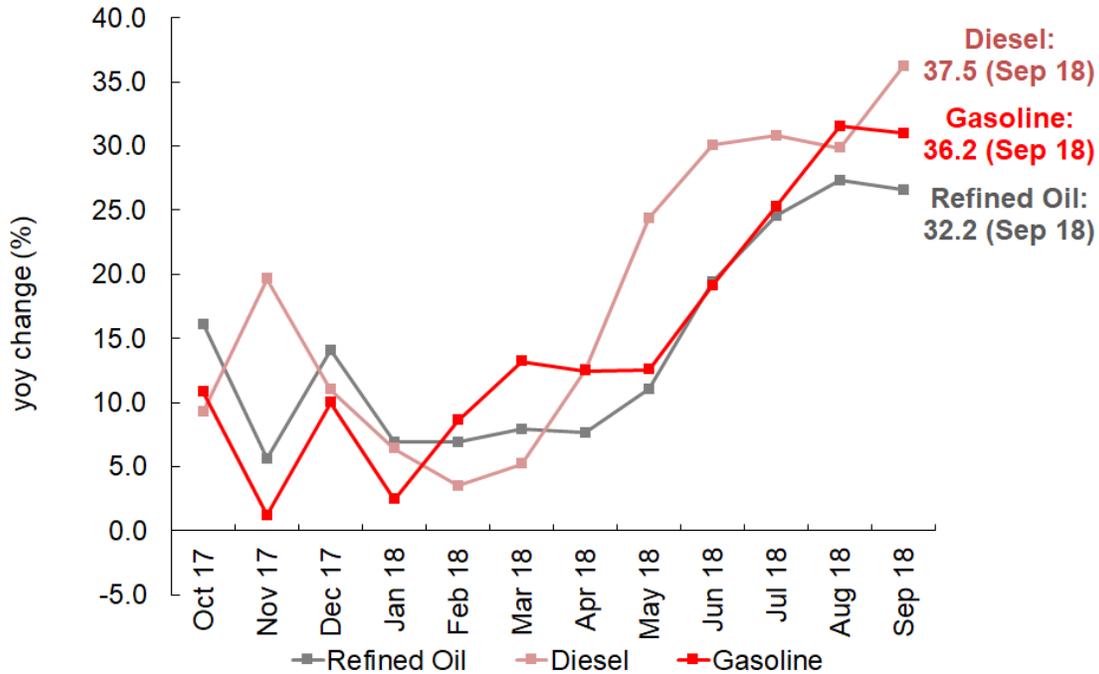
³ The index is compiled by the China Logistics Information Center (CLIC).

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 up further in October, as the NDRC raised the maximum prices of diesel and gasoline again on 1 October and 20 October in response to an increase in global crude prices during late September to early October.

Exhibit 2: China's wholesale price indices of refined oil products, October 2017 to September 2018





Source: China Logistics Information Center

3. Benchmark Qinhuangdao coal prices rise in the first half of September

The benchmark Qinhuangdao coal prices went up during early to mid-September (see exhibit 3). For example, the price of coal with calorific value of 5,000 kcal/ kg climbed from 511 yuan per tonne on 27 August to 519 yuan per tonne on 17 September.

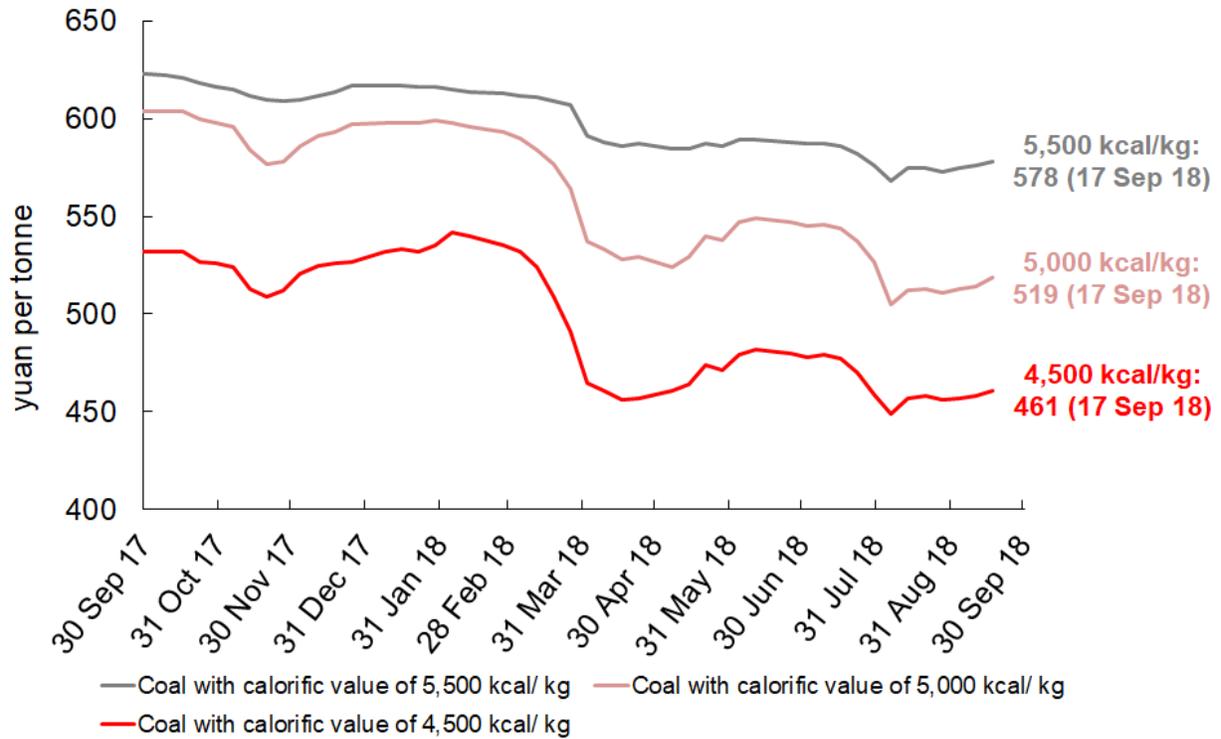
The increase in the domestic coal prices in the first half of the month was due mainly to a tightened supply, as safety checks were conducted on coal mines in major coal-producing provinces across China during 20 August to 20 September. Moreover, the ‘mispricing’ of coal in coal producing regions and in Qinhuangdao⁴ led to a reduced transportation of coal to Qinhuangdao, thereby pushing up coal prices there.

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, during which coal delivery to

⁴ ‘Mispricing’ arises when coal prices in Qinhuangdao are lower than the sum of coal prices in coal-producing regions and the transportation costs from these regions to Qinhuangdao.

Qinhuangdao would drop. Thus, we expect that domestic coal prices will continue to trend upward in the near term amid a tight supply of coal.

Exhibit 3: Qinhuangdao coal prices, September 2017 to September 2018



Source: ifeng.com, cctd.com.cn

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