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Copper: LME getting long, SHFE still liquidating

With LME copper surging back above $7,150, it's interesting to look at how open interest has changed over the past month or so and also the differences between the LME and SHFE contracts.

The LME copper contract was dominated by long liquidation beginning of June, though this has given way first to short covering activity and then the addition of fresh long positions from around June 19th. Steady buying interest has been present since then, with prices again surging higher as we head into July on the back of further fresh buying interest. Over the same period, the SHFE contract has seen quite a significant amount of short covering and position squaring activity, with a wide nearby backwardation continuing to hurt remaining shorts. While there have inevitably been new long positions put on over the same period, they have not made an impact on the open interest figures and are likely being covered back intraday, with short covering dominating overall.

There are suggestions that some elements of the Chinese speculative community are looking to get short again, in spite of the cost of rolling those shorts in a backwardation. Certainly, looking at open interest and price action, the big moves have tended to be participants getting short, with episodes of stronger prices generally short covering related in the face of rising international prices. Since 2012, there have been no clear instances of a long position building up on the SHFE. A portion of this might be due to the hedging activity of stock holders, but the pattern still seems very odd nevertheless.

With the SHFE-LME arbitrage window sporadically opening up, the flow of Chinese bonded metal is slowly towards domestic China, keeping the LME market tight and helping boost LME spreads and prices. Chinese economic data has been decent enough, with the government mini-stimulus measures starting to bear fruit and altering the usual seasonal pattern. Physical premia for copper in bonded warehouse in Shanghai are back around the $100 mark, while on the concentrate side of things the continued halt on exports of Indonesian concentrate (except to the Gresik smelter) is impacting not only on copper availability but also on the copper industry's ability to adequately blend some of the more complex and dirty concentrates being produced.

The slow drip feed of metal from bond into the domestic Chinese market is already impacting on the domestic physical premium and is also likely the reason why SHFE exchange stocks have started to stabilise and pick up a little. Theoretically, this should help ease the backwardation on the SHFE too, though whether this is enough of a reason to get short again is debateable. Overall it seems that there is still an imbalance, with shorts looking to borrow the spread still far outweighing any natural length.

From an LME perspective, the fact that, ~4kt aside, most of the metal that participants feared might flood into LME Sheds in the wake of the Qingdao investigation (CRU reportedly saying that there has been a 30 kt reduction in Qingdao bonded inventory in the past 2 months), simply hasn't emerged is bullish for the spreads. This in turn lends support to prices. Coupled with decent economic data from the US and China, lacklustre refined supply (so far at least) along with reasonable demand, and the case for stronger LME prices is fairly solid in our view.

For the LME and SHFE, the debate over which one is the dog and which is the tail and who's wagging who will go on. For the moment, however, unless we are missing something more serious in China, it seems that the LME is in charge.

By Leon Westgate

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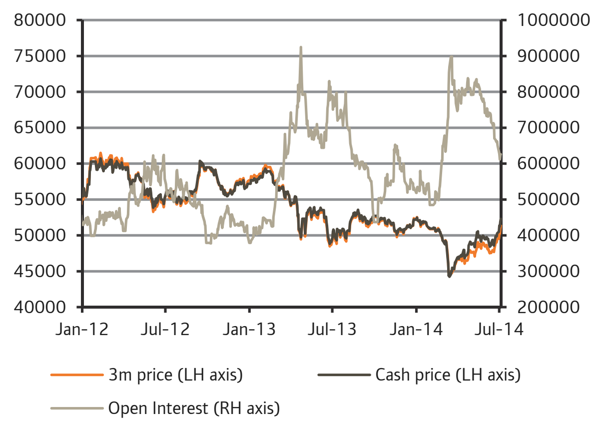
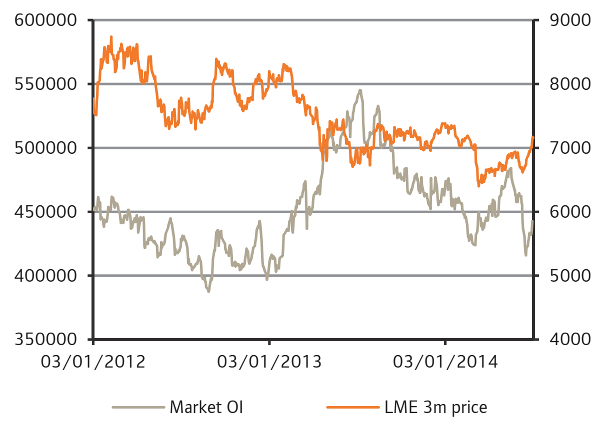
SHFE Open Interest vs. price



Source: SHFE; Standard Bank Research

LME Copper Market Open Interest vs. 3m price



Source: LME

Base metals

With the US on holiday, celebrating their independence from British rule 238 years ago, trading conditions are unsurprisingly pretty quiet, with thin volumes in evidence across the base metals complex. The metals have generally drifted sideways to lower in the absence of US trade, with very little going on.

Copper has drifted lower into Friday afternoon on the back of very thin volumes, holding on around $7,150. In China, the domestic physical copper premium declined to flat against the July SHFE contract, reflecting the increase in copper prices over the past few days (so all-in price moderates) and drip-feed of bonded material into the country, helping alleviate some of the tightness in the physical market. SHFE exchange inventory meanwhile increased by a net 2.4kt with bonded inventory falling 3.9kt, while domestic inventory increased by 6.3kt. LME inventory was unchanged.

Nickel has come under a bit of pressure heading into Friday afternoon, falling around 1% from yesterday's close. Volumes are light, however, and the metal is still managing to hang on to most if not all of Wednesday afternoon's rally, trading around $19,650 heading into the LME Second Ring session. Elsewhere, the rest of the base metals are trading sideways, on the back of very thin turnover.

By Leon Westgate

Precious metals

The precious metals are understandably pretty quiet given the absence of US trade. Strong US data yesterday had only a short-term impact on both gold and silver, with both metals bouncing back strongly into yesterday's close.

The exception has been palladium, which has rallied to the highest level since 2001, when prices were falling back after having surged to all-time record highs. Solid auto demand and the impact of strike action have helped provide a supportive backdrop, with the impact of fresh buying, technical factors and options-related acidity doing the rest. Platinum is also higher this morning, though prices remain range bound. The strike by members of NUMSA union in South Africa are ongoing but are not directly impacting on PGM production and are more of a factor for the currency and general economy.

By Leon Westgate

Bulks

Chinese financial steels rallied in the Asian afternoon, after absorbing yesterday's news that Chuanwei Steel will have its credit maintained by Minsheng and BOC, which will each inject RMB 100m to cover off creditors. As we commented yesterday, the market will gain greater acceptance of micro steel industry-restructuring dynamics, as the "flight to quality" by debt and equity holders continues to take hold. Iron ore also traded well, while coking coal and coke were hit by further oversupply negativity, following recent subsidies. Next week will see the usual monthly raft of economic releases begin, with CPI due on Wednesday, Trade on Thursday and FAI, IP & GDP 2Q (7.4% exp) etc. potentially out next Friday.

Shanghai Equities fell 0.19% to 2059 points. Beijing, Tianjin and Hebei are planning to announce an infrastructure & logistics development plan. Shanghai 7-day interbank rates fell to 3.37%, after the PBOC injected a net RMB 55bn in liquidity this week, the 8th week in a row. Next week, China has RMB 80bn in maturing repos. Spot Currency fell to 6.2050, while the PBOC reference rate set up at 6.1642.

Shanghai Rebar Futures Oct-14 contract closed up RMB 1/t at RMB 3,084/t, while the Jan-15 contract closed RMB 3/t higher at RMB 3,102/t. Dazong HRC July-14 futures shifted up RMB 9/t to RMB 3,307/t, while SHFE HRC Oct futures fell RMB 4/t to RMB 3,306/t.

Among physical steels, Tangshan billet prices rose RMB 20/t to RMB 2,730/t. Despite the billet rise and drop in weekly warehouse stocks, rebar prices traded unchanged in Shanghai and Beijing. Rebar stocks fell 0.044mt to 6mt. HRC prices also traded flat in Shanghai and Beijing, while dropping RMB 10-20/t over the week, with weekly warehouse stocks falling 0.023mt to 3.14mt.

Dalian Commodity Exchange IO active Sept-14 contract prices fell RMB 1/t to RMB 711/t, while the Jan-15 contract dropped RMB 3/t to RMB 707/t. China IO port stocks lifted 1.37mt to 116.18mt this week.

Among physical iron ore, globalORE traded a PB fines (Fe 62% equiv) July-cargo at $96.50/t. Local Chinese platform CBMX traded a PB fines Fe 61% late July cargo at $95.80/t. MAC and Newman fines Aug-cargoes traded at similar prices to yesterday in private deals. Ports saw prices off RMB 5/t.

The TSI Fe 62% China CFR price index remained unchanged at $96.50/t (MTD: $95.47/t). The Platts Fe 62% index fell 50 cents to $96/t (MTD: $95.56/t), while the TSI Fe 58% index rose 80 cents to $79.90/t (MTD: $78.80/t). The Metal Bulletin Fe 62% index fell 22 cents to $96.11/t, while its Fe 58% index rose 25 cents to $72.50/t. Argus Fe 62% fell 10 cents to $94.80/t. Mysteel's Fe 62% index traded flat at $96/t, while its Fe 58% index fell 50 cents to $78.25/t.

In IO supply news, Iran still plans to impose a 20% tax on concentrate exports, with the industry to be formally notified over the next 15 days. The tax will then come into force c.mid-October. Iran has been exporting c.20mtpa, although recent price falls have caused shipments to drop, due to a lack of profitability. This tax is likely to put a further nail in the coffin on the country's tradeflows. Vedanta hopes to begin ore mining in Goa from October, as the Monsoon season ends, providing its mining leases can be renewed. The state has been allowed to produce 20mtpa, following a Supreme Court directive in April. Goa's Chief Minister is proposing that a differentiated export tax be reintroduced, hitting higher Fe grades with higher taxes, rather than applying a blanket 30% rate. NMDC has kept prices flat for its July Indian domestic sales, with lump at INR 4,500/t and fines at INR 3,160/t, after raising June lump pricing by INR 300/t and fines by INR 250/t.

The Baltic Exchange Cape index shifted off 3.4% to $13,459/day, with C3 falling 1.2% to $22.123/t and C5 rising up 0.4% to $7.90/t. FFA Q3 capes are trading in the $16,000/day range.

For Q4:14 thermal coal prices, API 2 is trading at $75/t; API 4 is trading at $73/t; while Newcastle is trading at $71/t. ARA saw Aug traded at $71.50/t, off 50c, while Sept traded at $73.10/t, up 35 cents. NEWC traded a Q4 cargo at $71/t. S.China NAR 5500 prices have fallen to $68.25/t, with no certainty that a floor has been reached as yet, while Indo sub-bit (NAR 4700) was trading $58/t CFR S.China.

Spot thermal prices continue to drop, with July trading at $69/t, just above March-2010 lows of $68.85/t. RBCT shipped 4.9mt in June, compared to 5.6mt in May and inflows of 6.2mt vs 3.9mt in May, building stocks back to 3.85mt. 2.9mt were shipped to India (45.5% of totals), compared to 3.6mt in May and 3.2mt in April. June YTD shipments have totalled 31.9mt.

The US cyclone season is taking hold once again, with Cyclone Arthur moving through the mid-Atlantic region. US thermal exports fell 32% to 2.9mt in May, with YTD off 25% to 16.8mt. BHPB is cutting c.8.5% of its 18mtpa Mt Arthur workforce in NSW to reset its cost base for profitability. Australia's Senate is delaying debate on abolishing the carbon tax, which had been set as the first bill for the new sitting to debate.

Zhengzhou Futures Sept-14 contract price fell RMB 1.2/t to RMB 493/t, while the Jan-15 contract dropped RMB 1.8/t to RMB 515/t. Total port stocks fell 0.4% to 18.42mt, off 1.7% w/w, while QHD stocks fell 0.4% to 7.09mt and GZ fell 4.7% to 3.03mt, while off 7.7% w/w heading into summer restocking season. Despite this added demand, prices continue to weaken, supported by recent increases in supply, driven by miner subsidies. Shenhua is discussing shifting from its monthly pricing structure to spot-based terms.

Premium Hard Coking Coal spot prices are trading in the $108-113/t Qld FOB range, with China CFR prices ranging $118-123/t, but with significant downward pressures as domestic supplies increase in adjustment to recent subsidies. We still feel many in the seaborne coking coal industry do not adequately understand prevailing industry dynamics. Analysts seem to suggest that if seaborne supplies turn off, prices will recover. This is untrue in our view. Firstly, no miner willingly turns off if profitable. Secondly, China domestic continues to dominate supplies. Unless a significant "black swan" event occurs which can reverse the recent decision to subsidise domestic miners by $5-8/t, seaborne supplies will continue to suffer regardless. US exports fell 22% to 4.8mt in May, with YTD exports off 9.4% at 26.8mt.

On the Dalian Exchange, Sept-14 coke price traded fell RMB 9/t to RMB 1,114/t into the close, while the Jan-15 contract dropped RMB 10/t to RMB 1,178/t.
Night trading begins today at 9pm. Among Dalian HCC prices, Sept-14 contract prices closed RMB 13/t lower to RMB 787/t, while the Jan-15 contract dropped RMB 9/t to RMB 827/t.

By Melinda Moore

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