

# Copper spreads revisited

We have noted in the past the relationship between copper spreads and on-warrant inventory and the incongruous nature over the past year or so between how the nearby spreads have traded relative to LME stock levels vs. the farther-dated spreads. Historically there has been and still is a strong relationship between on-warrant stocks and how the spreads behave. Over the past 18-24 months however, as LME stocks have dwindled and indeed remained at low levels the nearby spreads have maintained that relationship and are trading within historical norms, while the farther dated spreads have remained disconnected and extremely benign.

With only 140 kt of LME on warrant stocks in the system, all it would take is a modest 5600 mt long position, which accounts for around 1% of market open interest at the moment, to take up all of that available stock were it to roll into cash. LME stock levels are low compared to open interest and it is easy to see why, in a physically deliverable market such as the LME that low levels of inventory see nearby spreads tighten dramatically.

What is different however is that the slightly farther dated spreads, for example in the 3-15m portion of copper's forward curve, are behaving in an abnormally calm manner. They are much more benign than they have traded in the past given current low levels of on-warrant and indeed total LME inventory. We have noted this disconnect in the past, with the much heralded refined copper surplus, fears over a metal exodus post Qingdao and the assumption that Shanghai bonded inventory is ultimately available to the market all being cited as reasons for the disconnect. Given that global copper inventory, including bonded inventory remains at historically low levels, and the fact that the refined surplus hasn't emerged in any real way and will likely only be drip-fed into the market (owing to issues adequately processing some of the dirtier concentrate that is coming to the market), the copper market still looks rather tight in the grand scheme of things.

With the Qingdao issue calming down, it seems that the reason for the farther dated spread behaviour is indeed hope that a refined surplus will be reflected in an increase in LME inventory, perhaps exacerbated by weaker copper financing demand. That has yet to emerge (and should have done by now). Meanwhile China will remain a net importer of refined copper for at least the next few years, and even then, assuming refined exports become the norm, that will be at the expense of Western smelting output. The farther-dated spreads in the 3-15m portion of the curve therefore continue to look good value in our view.

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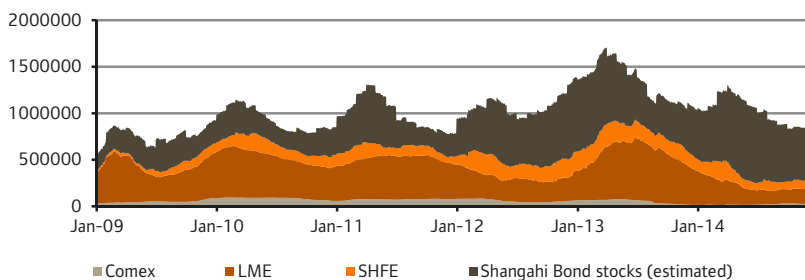
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*By Leon Westgate*

**Exchange copper inventory and SHFE bonded stock estimates**

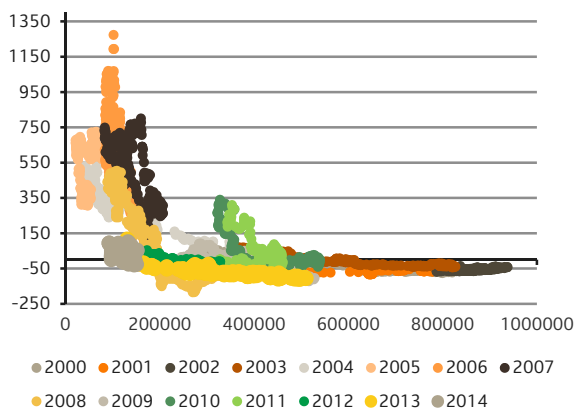


Source: LME, Comex, SHFE, Standard Bank Plc, Bloomberg

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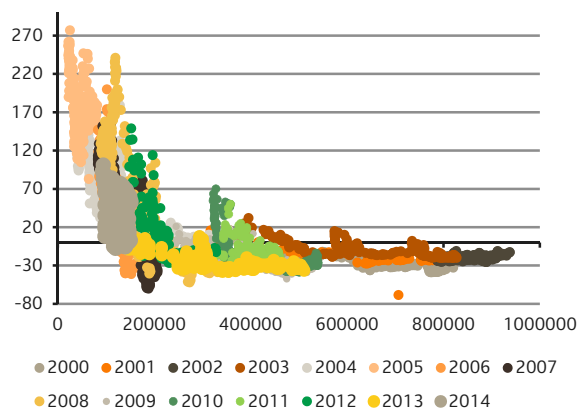
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**LME 3-15 month copper spread vs. on-warrant stock**



Source: LME, Standard Bank Plc

**LME Cash-3 month copper spread vs. on-warrant stock**



Source: LME, Standard Bank Plc

### Base metals

Quiet and choppy just about sums up the base metals complex today, with the metals generally stabilising after a few days characterised by fear and risk reduction.

Aluminium has been one of the stronger base metals with the price stabilising above \$1,900/mt. Volumes are pretty thin, with the most important bit of news perhaps being that the UK Supreme Court has refused to hear UC Rusal’s challenge to the LME’s plan to help try and ease warehouse exit queues. The new linked load-in load-out rules are now expected to come into force in February.

It’s worth noting that the LME cash price of aluminium reflects cheapest to deliver warrants in the LME warehouse system. The shorter the queue length therefore, the closer to the actual spot price the LME cash price actually represents, slowly eroding the portion of the physical premium associated with the queue length. Ultimately the LME rules will have an impact on premia (though not necessarily availability) however it will be slow and will not have any bearing on whether the flow of metal out of LME locations goes into ex-LME storage locations or “real” customers.

Nickel has finally stabilised, with the metal recovering from another dip lower this morning. Inventory-wise, on-warrant stocks fell 6,216 mt, however with most of that being a 5,088 mt jump in cancelled warrants in Johor, the data has little bearing on the realities of nickel demand. Elsewhere, tin also saw a jump in cancelled warrants, up 1,000 mt in Port Klang, 10 mt in Johor and 20 mt in Singapore, perhaps reflecting buying interest given the recent drop in prices.

*Leon Westgate*

### Precious metals

With the Fed more or less doing what was expected and altering the wording of the FOMC statement, the precious metals have recovered as shorts covered back. Light volumes and a return of some calm to the markets feels like people are already looking forward to the forthcoming holiday season. The dollar is strong, and that should limit the extent of any rally, however compared to the beginning of the week, which entered like a bit of a lion, the end of the week is exiting more like a lamb.

*Leon Westgate*

## Bulk commodities

Chinese financial steels opened higher, collapsed into lunch, before recovering back to close at relatively flat levels to yesterday, in what was a volatile day for both Chinese currency and interest rates. SHFE rebar traded in a RMB 35/t range. DCE remained benign, with stabilisation in the underlying physical markets as winter sets in, supporting prices and helping IO swaps trade up by \$1/t. Met coal and coke were slightly better bid, while ZCE thermal traded flat to down slightly. The Chinese steel export tax issue still remains up in the air.

The IO mining industry's biggest challenge now is to "start to stop". With BHPB, RioT and Vale etc all controlling significantly improved port and rail flex, the infrastructure bottlenecks which impeded the last IO price up-cycle will now become the buffer prolonging against the start of any new upward cycle, assuming we have not already hit a structural peak. The other cap to prices remains the silent, unseen, but deadly, scrap snake in the jungle, which although already beginning to bite, is likely to strike in an increasingly nasty fashion anytime from 2017.

In working to salvage ROI, cost cuts are a "damned if u do; damned if u don't" double edged sword, zero-sum game. Managements have to focus on cuts to keep up with their neighbours or risk losing their relative position on the cost curve. But as every miner initiates similar cost cutting processes, the end result is simply flat net margins, since the absolute clearing price drops to reflect the relative cost reductions achieved. However not to cut is suicide. So too can be how a miner chooses to cut costs. Those who search for efficiencies by increasing volumes; ie trying to take the easy way out by reducing variable, not fixed costs, face ruining not just their own margins, but also the margins of entire the industry, since in an already oversupplied state, each single new tonne added to the market reduces the collective value of every other tonne.

China's average monthly new home prices in November fell in 67/70 cities, compared to falls across 69 cities in October, while prices fell in 68/70 cities on an annual basis in November, compared to 67 cities in October. Beijing's new home prices fell 2.1% y/y and 0.2% m/m, while Shanghai's have fallen 2.9% y/y and 0.4% m/m. The slide in annual prices is the largest registered so far this year in both cities.

The US FOMC statement suggested that the timing of the next US rate hike cycle is based on the ongoing strength of economic data, including further falls in unemployment, and commensurate payroll gains. With a strong currency and now others able to compete with cheaper energy, conditions may actually weaken quicker than anyone is currently anticipating, with most still expecting a hike as early as March.

Shanghai Equities fell 0.11% to 3,057 points. Chinese TV sales have fallen 6.7% y/y to 42m units in 2014 and may not grow next year either, suggesting little net growth in new housing sales if true. China's apparent fuel consumption rose 0.8% y/y in November to 23.1mt, with natural gas up 9.4% y/y. China is to cut SOE executive salaries by 30% and will not exceed 7-8 times average pay rates.

Shanghai 7-day interbank rates rose to 5.6%, reaching an intraday high of 7%, on the back of the largest IPO fund lock-up for the year, with up to RMB 3 trillion of subscriptions across 12 IPOs being placed until 25 Dec. The market is potentially also coming up against end-of-quarter cash hoarding to cover other payments. The PBOC has provided RMB 1 trillion in PSL (pledged supplementary lending) loans for shantytown re-developments at a c.1% interest rate below market. The PBOC has refrained from further open-market repurchase agreement sales during its auction window again today, leading to a net zero change in funds this week.

Spot Currency traded out at 6.2095, the weakest since July, on short-covering, while the PBOC reference rate set at 6.1195. SAFE stated that capital outflows for any

single month were nothing to worry about, with 2-way moves in the RMB the “new normal”.

Shanghai Rebar Futures Jan-15 contract dropped RMB 1/t at RMB 2,646/t, while the May-15 contract closed up RMB 6/t at RMB 2,546/t. Dazong HRC Mar-15 futures shifted up RMB 1/t to RMB 2,915/t, while SHFE HRC Jan-15 futures rose RMB 4/t to RMB 2,886/t. Among physical steels, Tangshan billet prices recovered in the afternoon by RMB 10/t back to RMB 2,260/t. Rebar prices fell RMB 10/t in Shanghai, while rising RMB 10-50/t in Beijing. Hebei I&S is aiming to lift its rebar prices above RMB 2,550/t to try to hold the market up again. HRC prices fell RMB 10/t in Shanghai and in Beijing as well.

CISA says as much as 75% of all steel exports this year have relied on adding 0.008% boron to their products to gain a 13% rebate, and bypass being subjected to a 15% longs product export tax, effectively giving exporters a c.\$200/t price advantage. China produced 53.23mt of PI in November, up 0.9% y/y, while YTD PI output rose 0.4% y/y to 654.11mt.

Dalian Commodity Exchange IO Jan-15 contract fell RMB 2/t to RMB 522/t, while the May-15 contract closed up RMB 2/t at RMB 487/t. Tata expects to resume mining in Orissa from late-January, which is likely to limit its IO import requirements from the Australians, Brazilians and South Africans over the past 6 months. Posco plans to build a 2.5mtpa EAF steel mill in Oman for Sun Metals, scheduled to be online in 2017.

Among physical iron ore, globalORE traded a PB fines Jan-cargo at index plus 30 cents, together with a Yandi fines Fe 58% Jan-cargo at \$60.30/t. Local Chinese platform COREX traded a PB fines and PB lump at index plus 19.5 cents premia, followed by a PB fines Jan-cargo at \$67.70/t. Vale is hoping to settle its 2015 Pellet premia with Japanese mills at c. \$32/dmt, compared to \$38/dmt this year, given the increased supplies from Brazil, including Tubarao #8 (7.5mtpa) and Samarco #4 (8.25mtpa), while using the Fe 62% as the index for base adjustments, after clients rejected the Fe 65% index, due to liquidity concerns. FMG hopes to roll over its Dec product discounts into January, with SSF at 11% and FBF at 7.5%, while KF remains at 7%.

The TSI Fe 62% China CFR price index was up \$0.10/t to \$68.00/t (MTD: \$69.28t). The Platts Fe 62% index was up \$0.25 to \$68.50/t, while the TSI Fe 58% index was \$0.10/t lower at \$60.50/t (MTD: \$61.15/t). The Metal Bulletin Fe 62% index fell \$0.37/t to \$68.42/t, while its Fe 58% index was \$0.20/t lower at \$57.08/t. Argus Fe 62% printed at \$59.50/t. Mysteel's Fe 62% index rose 25 cents to \$68.50/t, while its Fe 58% index remained flat at \$60/t.

In IO supply news, Brazil shipped back up at 7.67mt last week, compared to 5.9mt the prior week.

The Baltic Exchange Cape index shifted 6.6% lower to \$3,838/day, with C3 at \$11.86/t and C5 at \$5.059/t, while C4 is \$4.86/t and C7 is \$6.01/t. FFA Cal15 capes are trading in the \$11,500/day range, while Dec is trading in the \$6,800/day range and 1Q15 trading in the \$7,600/day range.

For Q1:15 thermal coal prices, API 2 is trading at \$69.15/t; API 4 is trading at \$66/t; while Newcastle is trading at \$63.45/t. Among physical deals, a NEWC Jan-cargo traded at \$64.50/t, up 25c from last Friday, then at \$65/t. The falls in the Russian rouble could generate greater Russian coal exports as winter dissipates across 1Q, pushing Atlantic pricing lower.

Indonesia has lifted its 2015 coal output target to 460mt, after producing 427mt YTD November, up from 407mt y/y (+20mt), against full year forecasts for 421mt, compared to a likely run rate of 458mt (excluded any illegal output, which could

amount to a further 40mt). Exports are officially being pegged at 366mt Nov YTD, compared to 325mt last year.

Zhengzhou Futures Jan-15 thermal contract prices rose RMB 0.2/t to RMB 503.40/t, while the May-15 contract fell RMB 1.2/t to RMB 477.60/t. Total port stocks fell 1.0% to 20.02mt, while GZ stocks dropped 4.2% to 2.84mt. QHD stocks rose 0.1% to 7.35mt .

Coal stocks at China's key six coastal utilities stood at 13.38mt, enough to cover c. 20.81 days, with current daily consumption at 0.64mt/day.

China's Shaanxi province produced 44.24mt of raw coal in November, down 2.85% m/m. Over January-November, Shaanxi produced a total 461.67mt, up 3.75% y/y.

Premium Hard Coking Coal spot prices are trading in the \$110-115/t Qld FOB range, still helped by lower freight rates, with China CFR prices ranging \$118-123/t. TSI FOB Qld printed at \$113.50/t, while China CFR printed at \$121.30/t. MB FOB Qld printed at \$113.66/t, while China CFR printed at \$119.71/t. The Argus Qld fob index printed at \$112.57/t.

Maules Creek's met/thermal coal mine kicks off this week via NEWC port, with 2.5mt expected for delivery by June-15, of which very little will be met. For the FY2016 year, c.10-15% of sales will be met, increasing by 10pp each year, until 50:50 split is reached. Mine op costs are set at \$51/t fob excluding royalties.

On the Dalian Exchange, Jan-15 coke price traded RMB 17/t lower to RMB 1,074/t, while the May-15 contract rose RMB 7/t to RMB 1,032/t.

Among Dalian HCC prices, Jan-15 contract prices closed RMB 3/t higher at RMB 791/t, while the May-15 contract fell RMB 1/t to RMB 755/t.

*By Melinda Moore*

## Commodities Data

LME 3 month	Open	Close	High	Low	Daily change	Change (%)	Cash Settle	Change in cash settle	Cash - 3m
Aluminium	1,911	1,922	1,925	1,892	11	0.56	1,975.00	8	0.00
Copper	6,351	6,368	6,404	6,268	17	0.26	6,491.00	40	71.00
Lead	1,918	1,884	1,922	1,871	-34	-1.77	2,030.00	13	-5.00
Nickel	16,000	15,625	16,050	15,365	-375	-2.34	16,780.00	455	-65.00
Tin	20,040	19,450	20,145	19,399	-590	-2.94	20,415.00	-40	-7.00
Zinc	2,147	2,140	2,151	2,111	-7	-0.33	2,216.00	22	-7.00

LME inventory	Today	Yesterday	In	Out	One day change	YTD change (mt)	Cancelled warrants (mt)	Cancelled warrants (%)	Contract turnover
Aluminium	4,271,625	4,261,750	18,850	8,975	9,875	-1,186,450	2,264,250	53	275,483
Copper	170,900	172,200	475	1,775	-1,300	-195,525	30,175	18	159,891
Lead	220,800	219,825	1,000	25	975	6,350	9,175	4	59,616
Nickel	406,722	406,854	756	888	-132	145,086	103,008	25	93,057
Tin	12,190	12,190	0	0	0	2,505	2,410	20	6,507
Zinc	681,700	685,275	0	3,575	-3,575	-251,775	106,450	16	133,492

Shanghai 3-month	Open	Last	1d Change	COMEX	Open	Close	Change	Change (%)
Aluminium	13260	13170	-170	Ali Feb'14	-	-	-	-
Copper	44780	45150	-110	Cu Feb'14	287.05	287.85	0.8	0.28
Zinc	20,040	19,450	-2					

## Precious metals

	AM Fix	PM Fix	High bid	Low offer	Closing bid	Daily change
Gold	1,204.50	1,209.00	1,203.07	1,182.68	1,189.30	-42.47
Silver	-	16.42	16.08	15.61	15.74	-1.45
Platinum	1,236.00	1,239.00	1,207.05	1,189.75	1,188.60	-66.50
Palladium	801.00	798.00	793.15	775.30	777.70	-1.60

Forwards (%)	1 month	2 months	3 months	6 months	12 months
Gold	-0.0625	-0.0425	-0.025	0.0275	0.1175
Silver	0.62	0.616	0.618	0.612	0.568
USD Libor	0.162	0.2079	0.2426	0.3399	0.5993

Technical Indicators	30-day RSI	10-day MA	20-day MA	100-day MA	200-day MA	Support	Resistance
Gold	48.9	1,198.34	1,188.74	1,238.53	1,271.01	1,191.60	1,216.98
Silver	45.1	16.36	16.19	18.04	19.05	15.82	16.34
Platinum	46.43	1,223.22	1,214.18	1,329.79	1,392.68	1,195.47	1,218.77
Palladium	51.62	801.24	786.49	822.47	818.46	780.93	798.53

Active Month Future	COMEX GLD	COMEX SLV	NYMEX PAL	NYMEX PLAT	DGCX GLD	TOCOM GLD	CBOT GLD
Settlement	1203.6	16.44	804.65	1245.9	1203.8	4653	1207.7
Open Interest	369713	147954	31487	64684	737	#N/A Tim	21
Change in Open Interest	-24719	14667	-4851	3650	-529	#VALUE! error	-292

## Energy

Energy futures pricing	1 month	Change	2 month	Change	3 month	Change	6 month	Change
Sing Gasoil (\$/bbl)	77.362	-0.23	73.956	-0.40	74.03	-0.48	75.227	-0.52
Gasoil 0.1% Rdam (\$/mt)	564.5	16.50	578	15.75	581.25	16.00	589.25	15.75
NWE CIF jet (\$/mt)	648.16	-0.74	621.54	-2.07	618.05	-2.48	626.08	-2.96
Singapore Kero (\$/bbl)	78.791	-0.10	75.736	-0.08	75.88	-0.17	76.647	-0.42
3.5% Rdam barges (\$/mt)	315.91	1.94	293.821	5.97	296.041	5.73	303.952	5.16
1% Fuel Oil FOB (\$/mt)	324.29	1.72	303.63	5.91	306.04	5.42	314.45	4.97
Sing FO180 Cargo (\$/mt)	353.054	2.20	326.321	5.74	326.458	5.57	333.702	5.08

Thermal coal	Q3 14	Change	Q4 14	Change	Q1 15	Change	Cal 15	Change
API2 (CIF ARA)	74.50	-0.50	77.05	-0.45	78.65	-0.35	80.45	-0.40
API4 (FOB RBCT)	73.85	-0.15	74.05	-0.20	75.25	-0.05	76.75	-0.10

Source: LME, Comex, Nymex, SHFE, Standard Bank Plc

18 December 2014

**Commodity Data cont.****Bulks**

	Latest Price	1-day	1-week	1-month	3-month	6-month
Turkish Scrap 80:20 (Iskenderun CFR) \$/t	304.55	3.93%	3.93%	-16.46%	-16.20%	-21.55%
China Tangshan Steel Billet \$/t	378.00	-4.79%	-6.44%	-5.26%	-13.70%	-25.00%
China HRC export (Shanghai FOB) \$/t	457.00	-1.08%	-3.99%	-8.60%	-10.39%	-14.26%
North Europe HRC domestic (ex-works) \$/t	390.00	-2.50%	-6.59%	-8.24%	-7.14%	-9.30%
North America HRC domestic (Midwest FOB) \$/t	616.00	0.00%	-4.50%	-8.06%	-8.06%	-9.14%

**Steel—Futures**

LME Billet Cash \$/t	490.00	0.00%	6.52%	9.38%	25.64%	66.10%
LME Billet Futures (1-mth) \$/t	490.00	0.00%	6.52%	8.65%	24.05%	66.67%
LME Steel Billet Stocks—change	0.00	-	-	-	-	-
Shanghai Rebar Futures (Active contract) \$/t	425.13	0.08%	-0.81%	-2.29%	-6.53%	-26.87%
Shanghai Rebar Futures On-Warrant Stocks—change	0.00	-	-	-	-	-
China Steel Inventory (million tonnes)	9.79	-1.25%	-5.33%	-20.49%	-28.55%	-23.00%

**Iron ore**

China Iron Ore Fines (62% Fe; CFR Tianjin) \$/t						
China Iron Ore Fines (58% Fe; CFR Tianjin) \$/t						
SGX AsiaClear IO Swaps 62% Fe \$/t (1-mth)	68.58	-1.51%	-7.44%	-18.11%	-24.57%	-49.57%
China Iron Ore Inventory (million tonnes)	98.30	-0.40%	-1.64%	-6.77%	-7.75%	23.14%

**Coking coal**

Premium Hard Coking Coal (Qld FOB) \$/t	114.05	0.00%	0.00%	0.75%	-1.04%	-17.89%
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**Capesize freight**

Saldanha South Africa-Beilun China	8.35	0.00%	-41.61%	-42.61%	-46.13%	-63.70%
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**Financials pricing**

RMB Currency	6.22	0.43%	1.54%	1.21%	-0.25%	2.38%
China 7-day repo	5.61	-3.28%	80.97%	65.98%	81.55%	-16.27%
Shanghai Equities Composite	3057.52	4.50%	24.47%	32.02%	48.75%	42.32%

Source: LME, Bloomberg, Standard Bank Plc

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