Weak Copper Awaits Infrastructure Boost for Revival

- Metalworld Research Team

India's copper production doubled between April and July this year despite falling global demand. Existing copper smelters including the public sector Hindustan Copper Ltd intensified copper production in the first four months of the current financial year in anticipation of upcoming demand from domestic infrastructure boost. While the Bharatiya Janata Party (BJP) led National Democratic Alliance (NDA) government focuses on infrastructure development with fresh capital infusion, the housing and construction sector is set to get a revival by the end of the current or early next financial year. Since growth in infrastructure sector drives proportionate upsurge in electrical and electronic equipment, copper demand from this segment is also expected to take a fillip. India's electrical sector consumes 34% of the annual demand of copper.

Production

According to the Data compiled by the Ministry of Mines India's copper production was 231,836 tonnes between April and July this year as compared with 112,949 tonnes in the corresponding period last year. Of this, however, Aditya Birla Group's company Hindalco Industries shared more than half to the tune of 127742 tonnes while Anil Agarwal controlled Vedanta Resources Group company Sterlite Industries contributed 99483 tonnes. The public sector Hindustan Copper, however, shared a negligible 4611 tonnes, still double of the previous year's comparative cumulative four month figure of 2375 tonnes. If this production continues during the rest of the year's period, India's total copper output would achieve around 1 million tonnes for the financial year 2014-15.

The sudden spurt in copper production surprised many stakeholders of the industry due to falling prices of the red metal in global markets. On the benchmark London Metal Exchange (LME), copper is currently trading at $6600 a tonne, around the cost of production. The red metal has witnessed a sustained pressure in the last few months due to weak global demand. The average copper price in July 2014 stood at $7104 a tonne compared with $6806 in June 2014 and $7104 a tonne for the financial year 2013-14. The average LME cash price for July 2014 was US$7,000.55 per tonne, down from the July 2014 average of US$7,104.50 per tonne. The 2014 high and low copper prices through the end of August were US$7,439.50 (on 2nd Jan) and US$6,434.50 per tonne (on March 20), respectively, and the annual average was US$6,952.04 per tonne. As of the end of August, copper stocks held at the major metal exchanges (LME, COMEX, SHFE) totalled 253,190 tonnes, a decline of 253,314 tonnes from stocks held at the end of December 2013. Compared with the July 2014 levels, stocks were up at all exchanges.

Refined copper production was around 6.52 lakh tonnes, as compared to 6.93 lakh tonnes in FY 2012-13.The consumption of refined copper in the year 2013-14 is estimated around 5.5 lakh tonnes as compared to 6.10 lakh tonne in 2012-13. The consumption was affected due to sluggish growth of the Indian economy.

The industrialization & rapid urbanisation will lead to high energy demand, hence it is essential to have constant power supply. Therefore, demand of copper will grow as copper is critical for transmission and distribution of electricity. Furthermore, the US 1.2 trillion dollar investment that the government has planned for the infrastructure sector in the 12th Five-Year Plan which is metal intensive is set to improve the demand of copper in coming years. It is expected that demand will touch 1.0 million tonne by 2017.

India's per capita copper consumption was less than 0.5 kg in 2010 compared to 4.6 kg in China and a world average of 2.4 kg. If India's per capita copper consumption moves towards the per capita copper consumption levels in the rest of the world, India's copper market has the potential for significant growth. Globally, China continues to dominate the market consuming around 40% of the global demand. There has been no sign of slowdown of

Chinese economy; IMF has predicted that Chinese economy will expand by 9.7% in the next five years.

Change in Global Economic Environment

The global economic environment has witnessed a significant change in the last few quarters. The large economies like USA, Japan and Euro Zone are showing distinct signs of recovery from the prolonged recession these countries were suffering. On the other hand, growth in the emerging economies like Brazil, Russia and China has moderated. Overall, global economic activity is expected to strengthen further during 2014-15 with most of the momentum coming from the mature market economies. According to World Economic Outlook of International Monetary Fund (IMF), global growth is projected to increase to 3.6% in 2014 from 3.0% in 2013. This is projected to further increase to 3.9% in 2015. The last few years have been very challenging for Indian Mining and Minerals sector. Indian economy which has seen the growth of below 5% in the past year requires huge investment in infrastructure sectors like energy, railways, roads, telecom, ports and airports to get out of this downturn. The growth of the manufacturing sector has always lagged the overall GDP of the Country. Given the circumstances, demand potential of metals and mineral sector of the Country has not been realized. Already, green shoots are visible in the manufacturing sector, and the first signs reflected in the Q1 GDP growth of the fiscal 2014-15. GDP growth during the period April-June 2014 is estimated to be 5.7 which is a sign of a pickup. Apart from an uptick in mining, manufacturing and electricity, we find that capital goods were up 23% in June and Inflation is also now showing clear signs of moderation. The government of India has taken several initiatives to improve the Indian economy, which has been responsible for a number of positive outcomes. One of them is to build a vibrant manufacturing sector with key mission of 'Make in India', another one is reform in labor laws, and improved access to land & finance. These measures will also help small and medium size enterprises that are critical for the creation of jobs in the country.

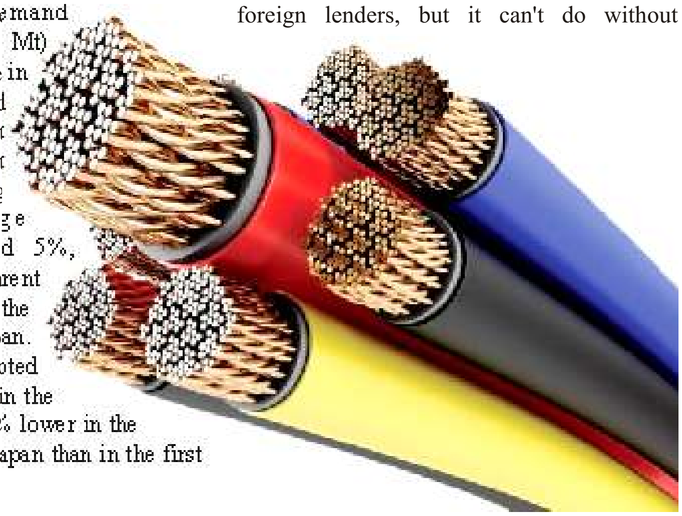
World Scene

The International Copper Study Group (ICSG) released preliminary data for June 2014 world copper supply and demand in its September 2014 Copper Bulletin. The Bulletin is available for sale upon request. In developing its global market balance, ICSG uses an apparent demand calculation for China, the leading global consumer of copper, accounting for about 40% of world demand. Apparent copper demand for China is based only on reported data (production + net trade +/- SHFE stock changes) and does not take into account changes in unreported stocks [State Reserve Bureau (SRB), producer, consumer and merchant/trader, which may be significant during periods of stocking or de-stocking and which could significantly alter supply-demand balances.

Historically, ICSG has only accounted for reported stock data in its statistics. In recent years anecdotal evidence has suggested that there have been substantial fluctuations in Chinese bonded stock levels, and apparent usage based on trade, production, and changes in exchange inventories may not adequately reflect industrial use in a given time period.

According to preliminary ICSG data, the refined copper market balance for June 2014 (excluding the adjustment for changes in China's bonded stocks) showed an apparent production deficit of 27,000 metric tonnes, lower than that of the previous few months of 2014. When making seasonal adjustments for world refined production and usage, June showed a production deficit of only 1,000 tonnes. The refined copper balance for the first half of 2014, including revisions to data previously presented, indicates a production deficit of 526,000 tonnes (a seasonally adjusted deficit of 470,000 t). This compares with a production surplus of 139,000 tonnes (a seasonally adjusted surplus of 227,000 tonnes) in the same period of 2013.

In the first half of 2014, world usage is estimated to have increased by around 14.5% compared with that in the same period of 2013, supported by strong apparent demand in China. Chinese apparent demand increased by 27% (1.1 Mt) based on a 47% increase in net imports of refined copper from the low net import level in the first half of 2013. Excluding China, world usage increased by around 5%, supported mainly by apparent usage growth of 15% in the EU and 12% in Japan. However, it should be noted that comparative usage in the first half of 2013 was 5% lower in the EU and 4.7% lower in Japan than in the first half of 2012.



World mine production is estimated to have increased by around 5% (410,000 tonnes) in the first half of 2014 compared with mine production in the same period of 2013. Concentrate production increased by 6% while solvent extraction-electrowinning (SX-EW) increased by 1%. Almost all major copper-mine producing countries had greater output, including Indonesia (+5%) where production remained constrained by the ban on concentrates exports; comparative production in May-June 2013 had been reduced by a tunnel collapse at Grasberg. Production increased by 2.6% in Chile, 10% in Peru, 15% in the United States (where production in the first half 2013 was impacted by the landslide at Bingham Canyon mine), 15% in the DRC and 60% in Mongolia.

World refined production is estimated to have increased by almost 8% (800,000 tonnes) in the first half of 2014 compared with refined production in the same period of 2013: primary production was up by 7.5% and secondary production (from scrap) was up by 8%. The main contributor to growth was China (+19%, 580,000 tonnes), followed by India, the Democratic Republic of Congo, the United States and Japan, where aggregated production increased by 16% (287,000 tonnes). Output in Chile, the second biggest world refined copper producer, declined by 3% owing to an 8% decline in electrowon production.

Future Outlook

Gnanasekar Thiagarajan, Director, Commtrendz Research believes that the faith in metal-backed lending in China is corroding – and so is confidence in the country's giant credit system. Authorities are investigating whether traders at Qingdao port used the same lot of copper and aluminium to back multiple loans. China can just about manage without foreign lenders, but it can't do without collateral and confidence. These underpin the explosion in non-bank lending, including trusts and investment products sold to individuals, which has now reached huge proportions.

The size of unreported copper stockpiles in China has been a source of mystery and confusion for years, particularly as the country's booming credit market has created pent-up demand for metal imports as collateral against loans. That has bolstered prices and tightened supply. LME stocks are below 170,000 tonnes for the first time since 2008 and cash prices were as much as $100 higher than forward prices last month. So far, there is no sign of the metal's showing up. LME stocks have fallen by 2,000 tonnes since the Qingdao crackdown was reported on June 2. Nervous traders are watching the daily data closely. However, large and well-established importers have been seen to survive previous crackdowns and it is largely expected that there will not be any major repercussions.

On the positive side, China's central bank said that it would keep monetary policy steady in 2014, even as the finance ministry said fiscal spending had surged nearly 25% in May from a year earlier, highlighting government efforts to energise the slowing economy.

China's cabinet also revealed that it was now planning bigger infrastructure projects, including highways, train networks and oil and gas distribution and storage facilities, as part of its efforts to keep the economy growing at a stable rate. This means higher demand for the metal going forward. The higher spending comes after the world's second-biggest economy got off to a soft start to the year, growing at its slowest pace in 18 months in the first quarter. The economy has since shown some signs of stabilising, but the recovery appears patchy and markets do not rule out further stimulus measures, especially if the cooling property market starts to deteriorate rapidly.

The present situation could sentimentally affect copper for some time till the market gets tired of the crackdown and starts focusing on depleting LME inventories and potential demand from China and a recovering U.S economy. Technically, weakness should continue and LME copper could drift lower towards $6,000-$6,100 from where a possible turnaround can be seen.