

Commodity views: Chinese commodity inventory



Significant rise in commodity inventory a cause for concern?

We have discussed on a number of occasions the incredible role that China has played in global commodity markets in recent years. Over the last decade, China has accounted for more than 50% of global energy demand growth. China's crude imports last year were up 11%yy, at a fresh all-time record high. Meanwhile gas imports were up 10%yy and coal imports were up 62%yy last year at an all-time high.

However, the list of records does not stop there. Chinese imports of copper ore were up 10%yy at a fresh all-time high in 2023. China's imports of unwrought aluminium plus products were up 28%yy and finally imports of iron ore were up 6.6%yy at a fresh all-time record high.

The huge rise in commodity imports has been driven by record after record refined metals production. China's refined copper production was up 17%yy at a fresh all-time record high last year, while Chinese primary aluminium production was up 3.5%yy at a fresh all-time high. Chinese steel production was the third highest on record last year, with the 1st and 3rd quarters seeing the 2nd highest steel production on record.

So, wherever you look 2023 was a massive year for Chinese imports and Chinese production of refined metals. That's especially the case since China accounted for circa 45% of global refined copper output last year; 55% of crude steel production and 59% of primary aluminium production.

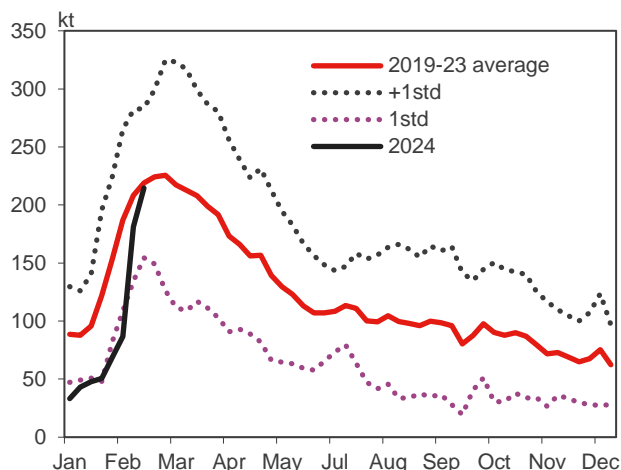
All the above then makes the recent and very sharp rise in commodity inventory all the more noticeable. Shanghai copper inventory is up by a factor of almost 7 so far this year, rising from more than 1std below the 5yr average to the 1st standard deviation. Iron ore port inventory has risen for the last 11 consecutive weeks with our measure of average port inventory up 27% since the 3 year low in October last year to close to average levels. And it doesn't matter whether we look at crude steel inventory at major mills or finished steel product at dealers and warehouses, we have seen a sharp rise in recent weeks there too.

Now a major caveat here is the combination of LNY landing much later than the last 2 years, a bout of very cold weather through February followed quickly by the National People's Congress which commenced yesterday. These factors could have partially been behind the above sharp rise in inventory coupled with expectations of rising demand post LNY and NPC.

However, there are other telltale signs of waning demand here for metals like copper. Physical copper cathode prices are trading at the some of the steepest discounts to the futures contract in Shanghai seen over the last year to a year and a half. Chinese copper smelters are also facing a collapse in processing fees to the lowest in more than a decade according to data from Fastmarkets. The slump in pricing is exacerbated by overcapacity in China and disruptions in supply from mines in Panama and Brazil. In addition, given elevated raw material prices and weak steel prices, our measure of rebar profitability has remained in negative territory since August of last year implying steel mills have been running at a loss through much of the last 6 or so months, even if profitability has improved more recently with the slid in iron ore prices.

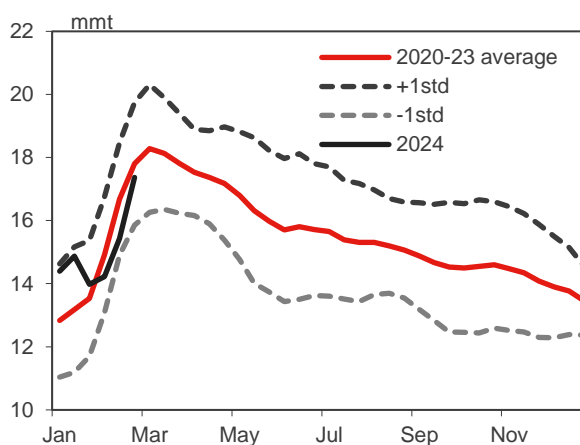
Bottom line, we tend to see the violent and significant rise in Chinese commodity inventory as a sign that the slump in property starts and sales into the end of last year to the lowest since 2006 and 2008 respectively, and the slow start to sales for 2024, is having an impact on metals demand. This should remain a weight on commodity prices at least until we have a better understanding of Chinese activity levels through Q1 and into Q2.

SHFE on warrant copper inventory



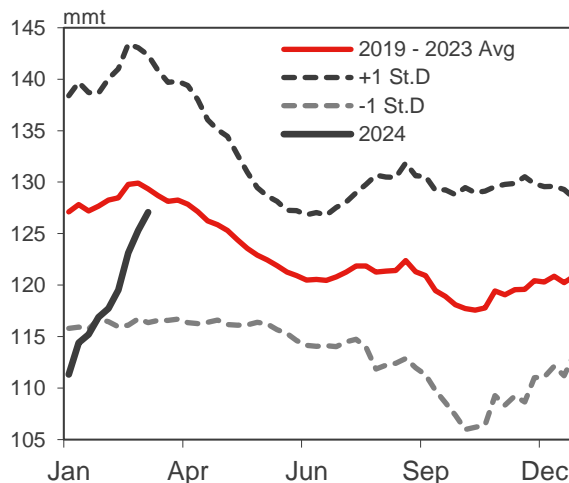
Source: Bloomberg, Westpac Strategy

CISA Steel Inventory at major mills



Source: CISA, Westpac Strategy

Iron ore port inventory



Source: Bloomberg, Westpac Strategy



Financial Markets Strategy



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