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CHINA STEEL INTELLIGENCE REPORT

Will China have to rip up its targets?

IN THIS MONTH'S ISSUE

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WILL CHINA HAVE TO RIP UP ITS TARGETS?

BY TOMAS GUTIERREZ

China had entered 2021 with a plan to deal with the slowing economy and ensure stability. Even as it announced its targets in early March however, the world was changing. Covid in China and the Russian invasion of Ukraine have made achieving those targets much more difficult. Nevertheless, the targets set the direction of travel for this year and are already having a material impact on the steel industry.

Further impacts could be coming, in particular in terms of stimulus and trade. There is no longer such a thing as a normal year, but without doubt this year will thrown a number of new challenges at the industry.

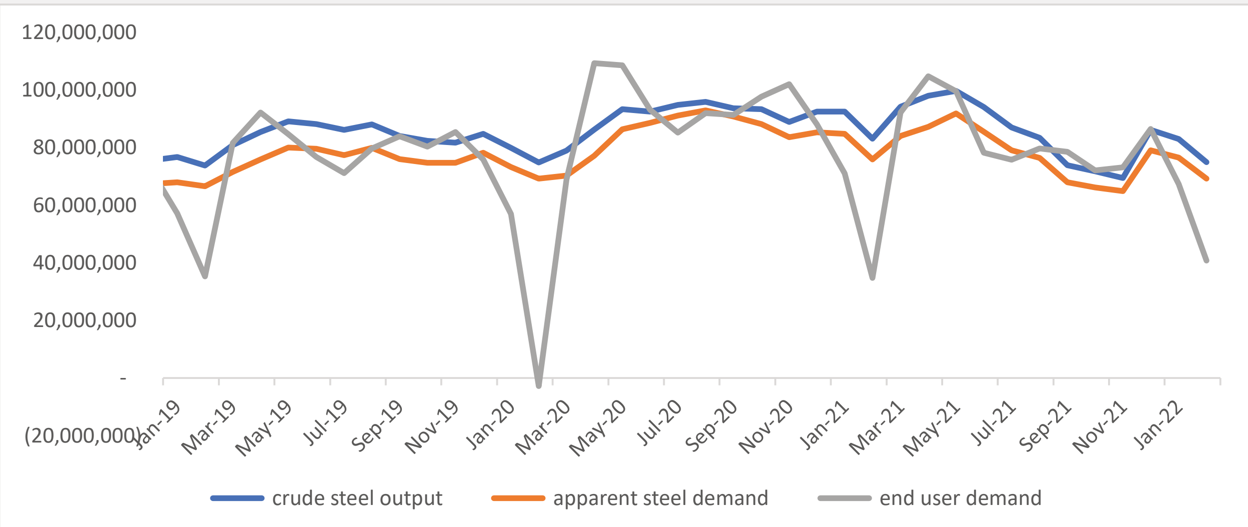
China's Two Sessions political meetings in March set the policy tone for a difficult year. China's government is facing an impossible balance between reforming the economy and ensuring stability, and is caught between reacting to Covid and the economic slowdown, and focussing on the political process of finalising the leaders for Xi Jinping's third term as Party Chairman. The balance set is already altering China's medium terms goals, though policies are likely to shift regularly over the coming years, which are likely to throw up numerous new challenges, as well as many familiar ones. The government work report, the last to be delivered by outgoing premier Li Keqiang, and renewed plans for the steel industry contain a number of shifts that will impact markets.

TABLE 1. SUPPLY AND DEMAND

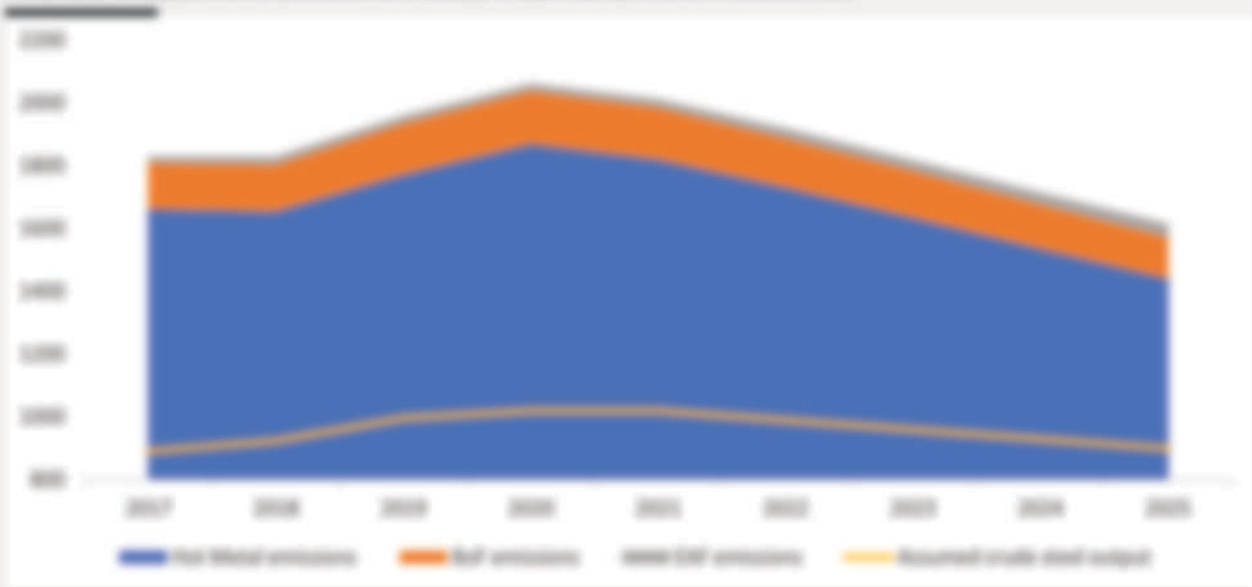
	2021	Jan-Feb 2022	Y-o-y	2022 Outlook	Y-o-y
Official Crude Steel Output	1,033	158	-10.00%	1,016	-1.60%
Apparent consumption	943	146	-9.29%	913	-3.10%
End user demand	946	108	-2.24%	913	-3.50%

Source: Kallanish. Million Tonnes

FIGURE 1. STEEL PRODUCTION AND DEMAND 2019-2021



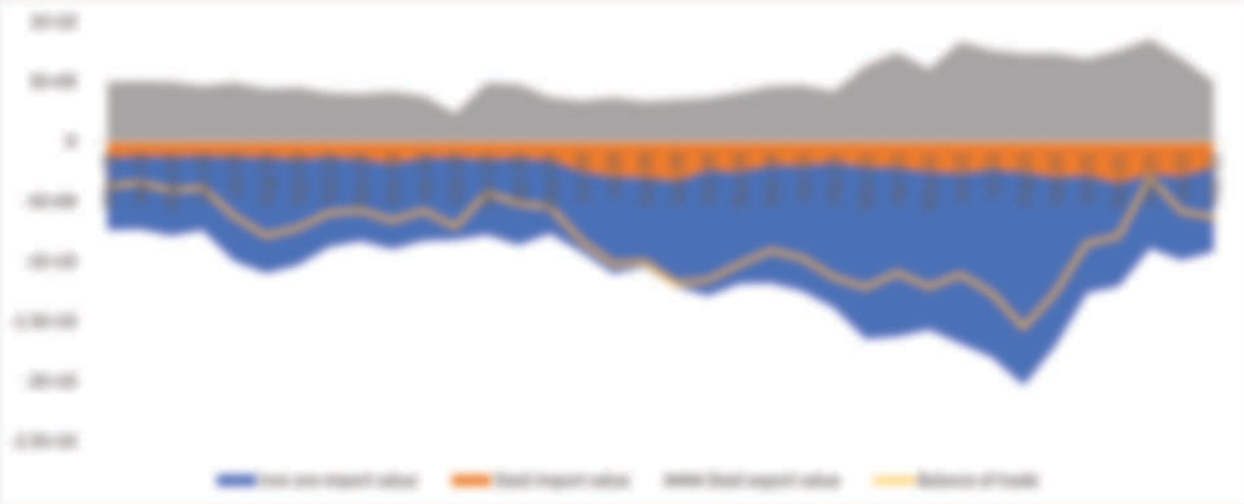
Source: Kallanish. Million Tonnes



2022 targets: Trade

China aims to see 'steady increases in both the volume and quality of imports and exports' this year. For steel, this suggested a continued focus on supporting high end exports but discouraging low end exports. From late 2021 this took place mainly behind the scenes, with major mills being discouraged from pushing hot rolled steel exports but no official measures or taxes. The global imbalance of prices however has seen China re-emerging as an exporter of commodity grade steels, including not only hot rolled but semi-finished steels. This has triggered rumours of tax increases on steel exports. Some mills are even again asking for clauses in their export contracts that ensure the customer is liable for the cost of any tax change. There are reasons to doubt the imposition of export taxes however, and the decision would be a complex one. Traders were talking about a National Development and Reform Commission meeting in late March at which export controls had been mentioned. A source at a mill which was represented at the meeting however said that specific measures such as export taxes had not been mentioned.

FIGURE 5: STEEL IS A NET IMPORT INDUSTRY BY VALUE



Source: NBS

One important factor is to understand that restricting steel exports may not contradict the macro-goal of boosting total exports. This is particularly so in the context of commodity price inflation and a drive towards resource security. If steel exports are seen as boosting Chinese steel prices above a 'natural' domestic level, and are therefore also 'artificially' boosting output and demand for iron ore, then limiting steel exports could be seen as sensible. Breaking the link to high international steel prices could help China's goal of lowering iron ore prices, and because of the larger scale of iron ore imports, could mean China's overall net export position in USD terms is boosted.

Focussing policy on lower value products would further improve China's overall net export position. China has been actively exporting billet and slab. Much of this has been the re-export of earlier billet imports, but China-produced semis are also being shipped. If these volumes become large enough for regulators to become concerned, then China could return to its policy of staggered export costs. Semis would become more expensive to export than hot rolled steel, and potentially hot rolled steels could be more expensive than coated or further processed steels. Without a change in VAT rebates, this would likely be achieved through export taxes or administrative or political barriers. From a government viewpoint, a tax on semis would be in line with both reform goals and supporting the balance of trade this year. It is therefore something that markets should be watching out for. Overseas steelmakers should be monitoring this with some optimism. Chinese moves to cut raw material costs and to limit semis exports can leave room for steelmakers elsewhere to earn bigger margins.

SUPPLY & DEMAND OVERVIEW

Data for the first two months of the year, which China releases together, showed a weak start to 2022. China produced 157.96 million tonnes of crude steel over January-February, according to the National Bureau of Statistics (NBS), down 10% year-on-year. The decline is largely due to very strong output a year earlier as China's post-first-Covid-19-wave recovery boosted steel markets. The data also implies a slowdown in production from December, however, with average daily output of 2.68m t/day over January-February compared to 2.78m t/d in December. This was more of a surprise as the China Iron and Steel Association (CISA) reported fairly steady output over the same period. Blast furnaces were increasing production, but electric arc furnaces saw very weak output, especially in February, which may account for the discrepancy. Alternatively, as the y-o-y comparison is in line with expectations, it may be that December data will be revised.

FIGURE 6: JAN-FEB STEEL OUTPUT/DEMAND DISAPPOINTS

Source: CISA, Kallanish

The official data implies apparent steel demand over January-February was down 14.07% y-o-y at 138mt, once net exports have been taken into account. The picture looks less bleak, however, once the change in inventories is added. Inventories have followed historical trends, and have been stubborn in coming down, but peaked at a much lower level than in the previous two years. As a result, end-user demand is estimated to be down just 3.73% y-o-y at 101.23mt. The decline on-year was small considering the trouble that has been seen in real estate and across the economy more broadly.

FIGURE 7: CISA DATA SHOWS MARCH OUTPUT RECOVERY

Source: CISA, Kallanish

In March, output at CISA member mills started the month with a dip but recovered by the end of the month to the highest level since summer 2021. The Russian invasion of Ukraine has given mills confidence to produce at higher rates as export markets have opened up, which within China mills do not expect restrictive policies as China is relying on supply-side stimulus to support the ailing economy. CISA mill output at the end of March still remained almost 11% lower than highs reached in early 2021 however, as Covid disruption continues to impact output in some areas.

Satellite analysis based on data supplied by TathyaEarth meanwhile reveals some of the difference in performance across various mills. Overall, mills in Tangshan began to reduce output as Covid restrictions resulted in reduced supply of raw materials in the city. Handan also saw disrupted supplies from Tangshan ports impact production there. Shougang Jingtang saw output decline through most of the month, but appears to have gotten a head start on other mills restarting thanks to its captive port, with output ticking higher at the end of March. Benxi Steel in the northeast meanwhile saw a jump in output mid-month, as restrictions in the northeast began to ease. Other mills appear to be less affected, including Baosteel's plant in Shanghai, which has been able to keep some operations at its port despite the strict lockdown across the city. Overall, the CISA and satellite data suggest higher output in March than at the start of the year, despite severe disruptions to the economy from lockdowns.

FIGURE 8: SATELLITE DATA CONFIRMS END-MARCH OUTPUT RECOVERY

Week ending	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Benxi Steel	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Baoshan Iron & Steel Shanghai Base	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Handan Iron & Steel	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Jiangsu Shagang Group	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Wuhan Iron and Steel	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Shougang Group	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Source: Kallanish, TathyaEarth

END USERS

REAL ESTATE

China's real estate sector saw another set of bumpy official data released for January-February. Expectations had been set so low however that markets were relieved the picture was not any worse. Completed investment in the sector over two months was up 3.7% year-on-year to CNY 1.45 trillion ($228 billion). Although that is the lowest year-to-date growth rate since July 2020, on a month-by-month basis it marks an improvement from the second half of 2021 when investment was consistently down y-o-y. Real estate sales however were down 9.6% y-o-y to 157.03 million square metres, marking the eighth straight month of y-o-y declines in sales by area. New starts were also down 12.2%, the 11th straight month of decline. Completions were down 9.8% over January-February.

One brighter note was realised average prices, which were up slightly from December at CNY 9,845/sqm. This was still down 10.7% y-o-y, however. A survey of 70 cities showed new apartment prices falling in 40 cities in February, one more than in January. This indicator suggests the most widespread real estate downturn since 2015.

Economic data for the first two months of the year came in generally stronger than expected, but the economy now faces new challenges including the new outbreak of Covid-19. On the other hand, China is also increasingly committing itself to sustaining economic growth. That may require strong credit growth. Even if reformers want stimulus to go mainly to small and medium enterprises, the greater the need for stimulus, the more is likely to leak to sectors with low returns.

FIGURE 9: REAL ESTATE INVESTMENT GROWTH

Source: NBS, Kallanish (% y-o-y)

AUTOMOTIVE

Despite a month-on-month drop due to the Chinese New Year holiday in early February, China's February automotive production still rose significantly compared to a year earlier, according to data from the China Association of Automobile Manufacturers (CAAM). February output reached 1.81 million units, down 25.2% from January but up 20.6% year-on-year. Year-to-date output thus rose to 4.24m units, up 8.8% y-o-y. Production of new energy vehicles (NEVs) fell 18.6% from December to January, but then registered a surge of 197.5% from January to February. Year-to-date output stood at 820,000 units, soaring 158.2% y-o-y. The continuous improvement of NEVs and exports is the main factor for the y-o-y growth, as well as demand driven by inventory replenishment.

February implied finished steel demand calculated by Kallanish from the CAAM data was down 30.71% m-o-m at 2.76 million tonnes, leaving January-February demand at 6.75mt, up 2.3% y-o-y. At the end of last month, CAAM announced its annual auto sale prediction of 27.5m units over 2022, compared to 26.275m units sold in 2021. Sales and output are both being impacted by the extended outbreaks of Covid however. Initial outbreaks in Jilin province brought production in the automotive hub of Changchun to a halt. Ongoing outbreaks in and around Shanghai are slashing output from car factories across eastern China. Automotive production data is expected to weaken in the coming months, before a stimulus-fuelled recovery later in the year.

FIGURE 10: AUTOMOTIVE STEEL DEMAND

Source: CAAM, Kallanish (tonnes/month)

WHITE GOODS

China's white goods production in he first two months of the year saw a slight decline from December but was still up from a year earlier. Different products saw different performances however. Air conditioner output was down slightly y-o-y, after driving growth in output over the last two years. Refrigerator and freezer output was also sliding on-year as a result of weak consumer demand and house buying. Washing machine output however has made up for weakness elsewhere.

Kallanish estimates finished steel demand from the sector over two months was around 2.24mt, up 2.1% y-o-y. The impact of Covid has not appeared in this data. Considering the importance of eastern and southern Chinese manufacturers of white goods, March and April data are likely to be impacted.

FIGURE 11. WHITE GOODS DEMAND

Source: NBS, Kallanish (tonnes/day)

SHIPBUILDING

China's shipbuilding completions fell year-on-year in the first two months of 2022, with new orders also slumping markedly. In the reporting period, shipbuilding completions declined by 9.6% on-year to 6.53 million deadweight tonnes, which suggests around 2.26 million tonnes of finished steel was consumed in the two months based on Kallanish estimates. According to the China Association of the National Shipbuilding Industry (CANSI), China's shipbuilding completions in 2022 should reach 40m dwt.

New orders meanwhile lost 17% on-year to 5.65m dwt. This is within CANSI's previous expectations that this year's new orders will decline as demand gradually becomes saturated. Orders in hand increased by 38.8% on-year to 97.8m dwt by the end of February 2022. From January to February, China's shipbuilding completions, new orders and orders-in-hand accounted for 49.9%, 49.0% and 47.7% respectively of the world's total in deadweight tonnes.

FIGURE 11. SHIPBUILDING COMPLETIONS

Source: CANSI (tonnes/month)

TRADE

China's export situation has changed dramatically in the last month, driven by the global upheaval from Russia's invasion of Ukraine. The latest available data however still reflects deals from before the war, with Chinese output lower than expected, and Chinese prices uncompetitive. Net exports were therefore down despite weak demand impacting import volumes. China's net steel exports in February were 2.024mt, a 14% m-o-m and 33% y-o-y decrease, China's customs data shows. Over January-February, net exports totalled 4.369mt, a decrease of 29% y-o-y. Exports in February were down 21% m-o-m and 26% y-o-y at 3.623mt. Over January-February, exports were down 19% y-o-y at 8.235mt.

FIGURE 13. CHINESE EXPORTS BY REGION

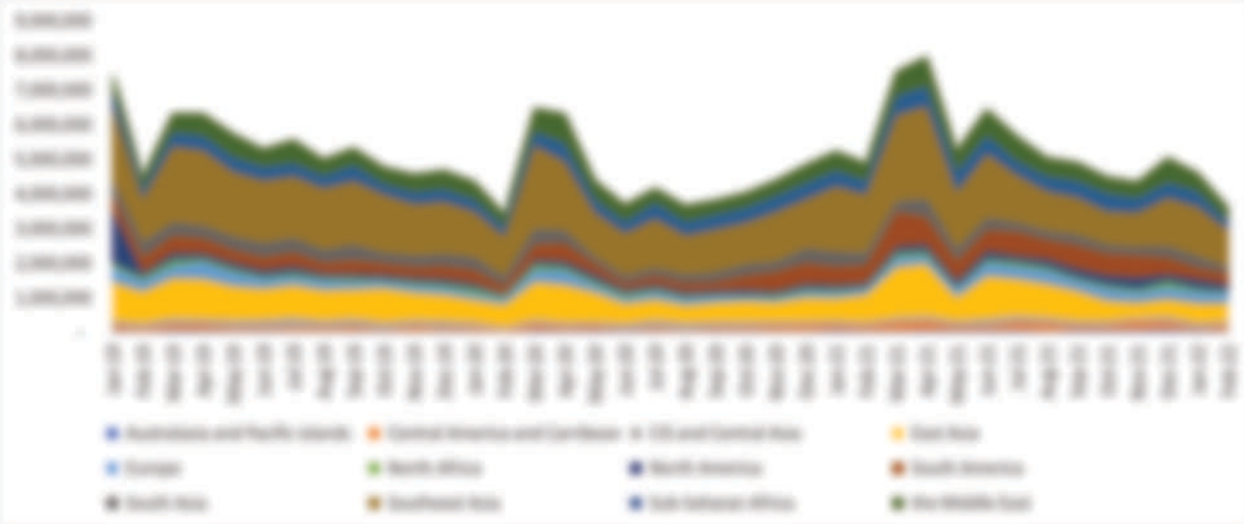
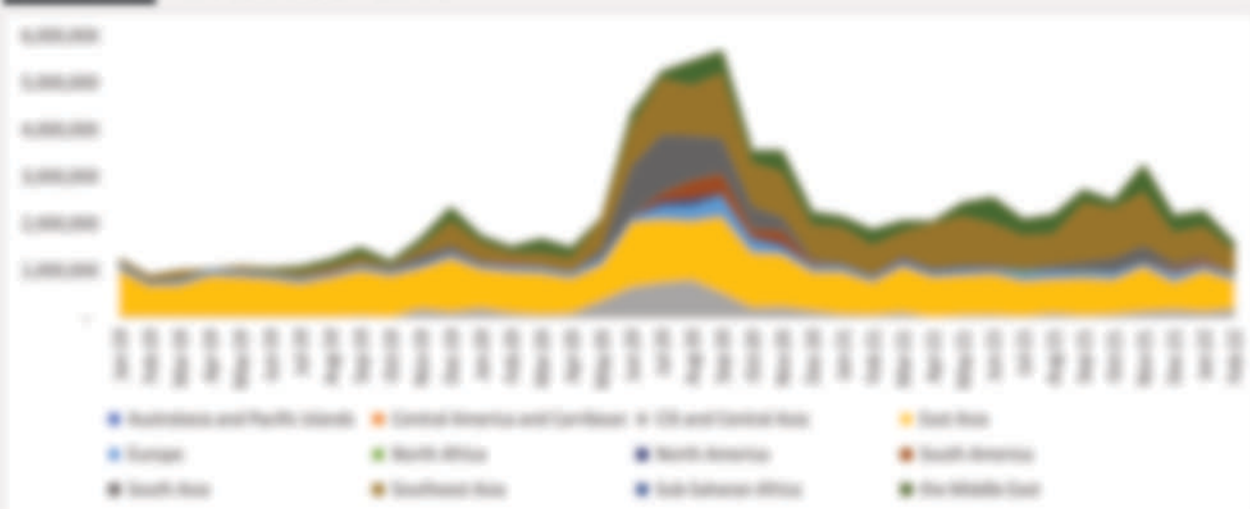


FIGURE 14. CHINESE EXPORTS BY PRODUCT

Source: GTT, Kallanish



692,846t in February, a dip of 25% m-o-m and 12% y-o-y, while over January-February combined flats imports were down 6% to 1.622mt. Japan supplied 157,507t of China's February carbon and alloy steel HRC imports, down 16% m-o-m and 11% y-o-y. During January-February, these inched 1% higher to 344,301t.

China meanwhile reported February semis imports of 644,238t, down 37% m-o-m and 18% y-o-y. However, two-month combined semis imports were 1.66mt, up 2% y-o-y. Of this total, China imported just 19,523t of semis from Vietnam in February, a fall of 41% m-o-m and 92% y-o-y. Between January-February, imports from Vietnam reached 52,504t, a fall of 89% from last year. Its February imports of semis from Indonesia, driven by stainless steel shipments, meanwhile reached 221,198t, down 12% m-o-m but up 131% y-o-y. Through January-February, it sourced 471,216t of Indonesian semis, a climb of 53% on-year. In February, the Middle East supplied another 161,337t of semis to China, a reduction of 48% m-o-m and 48% y-o-y, meaning imports of Middle Eastern semis were down 8% over January-February at 472,951t.

China's long product imports saw a 16% decline from January but a 12% increase y-o-y to 240,979t in February. Over two months longs imports were 527,992t, down 12% y-o-y. China also saw pipe imports of 20,774t, dipping 42% m-o-m and 14% y-o-y. Over the opening two months of 2021 pipe imports totalled 58,340t, down 9% on-year.

FIGURE 16: CHINESE IMPORTS BY PRODUCT

Source: GTT, Kallanish

MARKETS

March has been a dramatic month for global steel prices, and yet Chinese prices have appeared strangely steady, ending the month only a couple of hundred CNY higher than the end of February. This has largely been due to significant domestic market disruption, in particular due to Covid. The disease had been a relatively distant threat for most of the time since China got on top of the first outbreak in 2020, but its new variants have shut down many of its key cities and regions, some of which are likely to remain under some form of restriction throughout April. Even before Covid however there was some disappointment in the recovery in end user demand, and the government is showing growing concern about the economy. Stimulus is now the great hope for anyone long in the market, as well as a reopening post-Covid.

LONGS

The first week of March saw a CNY 100/t jump in spot rebar prices as post-New Year demand finally began to pick up. The recovery stalled however as Covid began to disrupt more and more regions, starting in the northeast and then spreading to the east of the country. Construction activity in the key urban hubs of Shanghai and the surrounding cities has now been stalled for weeks. 20mm HRB400 rebar was trading at CNY 4,760-4,780/t at the end of March, CNY 140/t higher than at the end of February. Steelmakers are trying to drive prices higher with new offers, supported by stronger export markets, but domestic markets remain quiet due to restrictions.

Chinese wire rod export offers fared much better, buoyed by global markets. Although export activity has remained relatively muted compared to HRC, wire rod orders picked up as global markets have become extremely tight since the Russian invasion of Ukraine. Even export offers retreated a little at the end of the month however, due to domestic weakness and a slowdown in orders. 6.5mm diameter mesh-grade wire rod ended the month at $840/t fob, up from $770/t at the end of February.

TABLE 2: LONGS PRICES

	2021	y-o-y	Feb-22	Mar-22	M-o-m	Y-o-y
Rebar (CNY/t)	4,878	29.5%	4,688	4,750	1.3%	4.4%
Wire rod fob ($/t)	783	58.7%	760	835	9.9%	15.3%

Source: Kallanish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FLATS

Chinese flat steel prices have continued to fare better than rebar for to reasons. Firstly manufacturers continued to buy HRC for longer than construction sites were able to continue operations, and secondly they have had more success on export markets. Domestic prices fluctuated through the month, but 5.5x1,500mm Q235 HRC in Shanghai ended March at CNY 5,230-5,250/t fot, up CNY 340/t from a month earlier. Although many key manufacturing and construction hubs are now shut down because of Covid, a combination of geographically shifting demand and production disruptions have kept HRC market inventories from rising, and China's focus on supply-side stimulus means expectations for later in the year remain high.

Chinese export HRC prices moved rapidly higher in the first half of March following Russia's war in Ukraine. Global HRC markets suddenly tightened as countries began to block Russian steel imports and seek replacements from elsewhere, as well as replacing supply lost to the disruption of the war and rising production costs. As a result, China again became active in export markets, aggressively targeting a wide range of buyers. Chinese HRC has found lucrative markets in the GCC and in Europe, as well as in Southeast Asia where much Indian material has also been diverted to Europe. 2mm SAE 1006 HRC was assessed at $895-905/t fob at the end of March, up $85/t from a month earlier. Price increases are now slowing. Booking of Chinese material is now slowing as shipments from ports have been disrupted by Covid measures, and buyers cannot guarantee when they will receive their cargos.

TABLE 3: FLATS PRICES

	2021	y-o-y	Feb-22	Mar-22	M-o-m	Y-o-y
HRC (CNY/t)	5,339	40.9%	5,003	5,168	3.3%	3.1%
HRC fob ($/t)	834	70.4%	808	878	8.7%	20.3%

FIGURE 16: FLATS PRICES

Source: Kallanish

RAW MATERIALS

Seaborne iron ore prices were also driven higher by geopolitics at the start of March, before fluctuating through the following weeks. Internationally, the disruption to exports from Ukraine, in particular pellet, and from Russia due to sanctions tightened iron ore markets. The surge in steel prices and rush to produce in other regions then also drove prices higher. Domestically, hopes for stimulus and a recovery in domestic markets contributed to the spike. But markets soon became less certain. In China, Covid began to disrupt output, including in key cities such as Tangshan, while overseas mills struggled to cope with surging energy prices. The Kallanish KORE 62% Fe index ended March at $156.82/dry metric tonne cfr Qingdao, $20.72/dmt higher than the end of February and just slight below the month's peak of $157.80/dmt on 8 March. The KORE 65% Fe index closed March at $182.83/dmt cfr, up $18.57/t on-month, and the KORE 58% Fe index increased $17.49/t over the month to $134.82/dmt cfr.

Iron ore port stocks have fluctuated due to disruptions. At the end of March, stocks across 35 ports were 149.35mt, according to SMM, down from 154.07mt at the end of February. Disruption in unloading however have left long queues of ships outside ports waiting to offload their cargo. As Chinese ports open up from Covid restrictions, there will be a race between mills restocking and higher unloading rates that will determine how much pressure inventories put on prices.

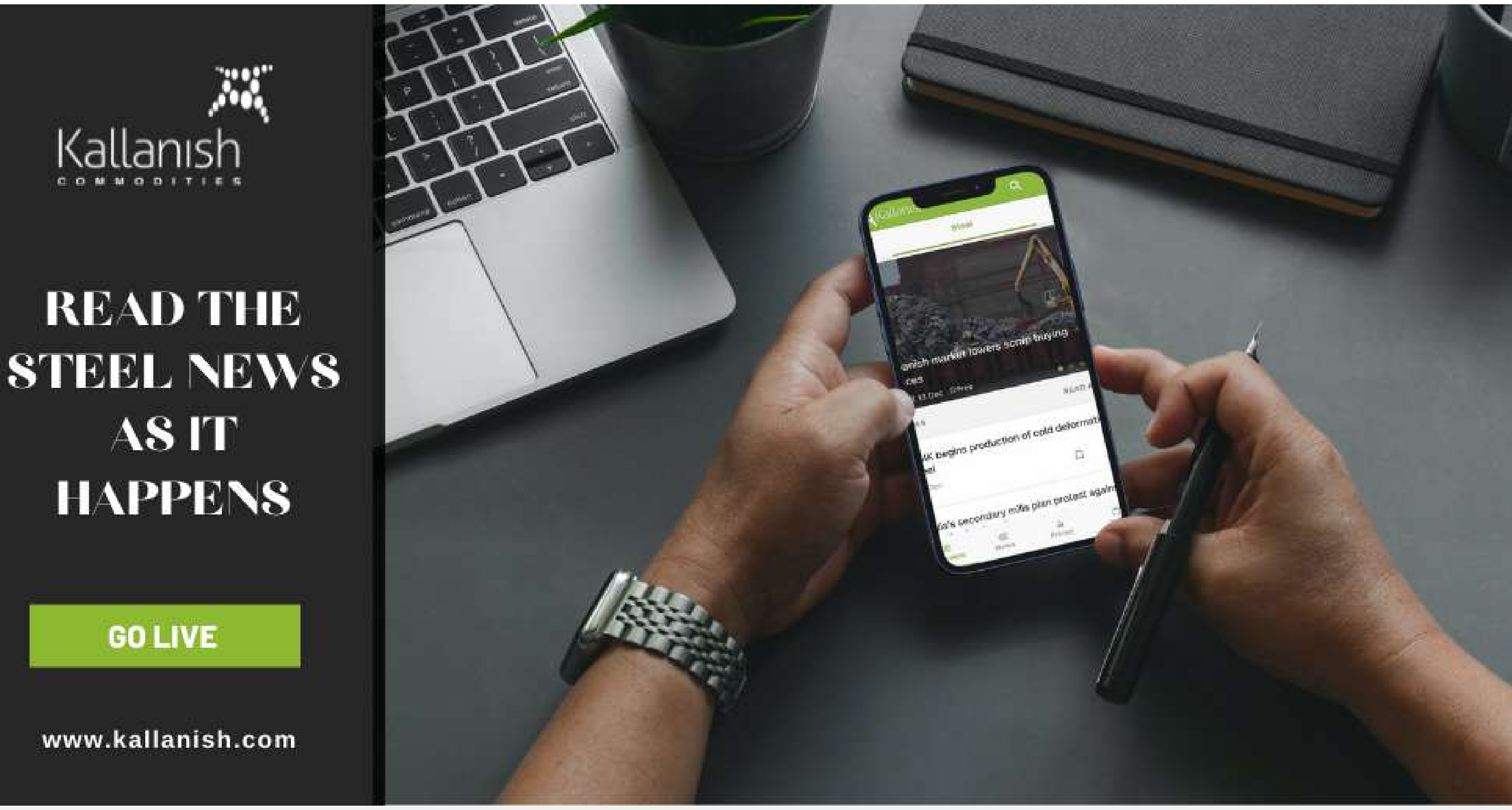
Chinese scrap prices meanwhile have increased in two phases over the past month. The start of March saw domestic scrap prices move higher following other raw materials and supported by the resumption of activity at EAFs, which had been struggling with profit margins through much of February. In the second half of the month, Covid brought collection and transportation to an end across many key scrap-generating regions, and tight supply pushed prices higher again. 6mm+ scrap delivered to mills in the Yangtze River Delta ended the month at CNY 3,828/t, up from CNY 3,635/t at the end of February.

International prices meanwhile have been driven up so far that imports to China have become even less competitive. HRS101 heavy melting scrap was assessed at $640/t cfr at the end of March, up $45/t over the month. Trading levels have dropped to almost nothing however.

TABLE 4. RAW MATERIALS PRICES

	2021	y-o-y	Feb-22	Mar-22	M-o-m	Y-o-y
KORE 62% Fe iron ore ($/dmt)	159	71.4%	142	150	5.4%	-11.0%
KORE 65% Fe iron ore	185	76.9%	171	179	4.7%	-7.5%
KORE 58% Fe iron ore	136	62.3%	120	130	8.1%	-17.1%
Yangtze delta heavy scrap	3,526	34.2%	3,651	3,721	1.9%	11.4%

Source: Kallanish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Steel Data:	Nov	Dec	Jan	Feb
Crude steel production	69.31	86.19	82.99	74.96
Steel exports	4.38	5.06	4.61	3.62
Steel imports	3.26	2.17	2.27	1.60
Apparent steel consumption	64.74	79.02	76.53	69.22
Calculated real demand	72.91	86.45	67.34	40.81

INFLATION

Macro data:	Nov	Dec	Jan	Feb
Manufacturing PMI (NBS)	50.10	50.30	50.10	50.20
Manufacturing PMI (Caixin)	49.90	50.90	49.10	50.40
CPI	2.30%	1.50%	0.90%	0.90%
PPI	12.90%	10.30%	9.10%	8.80%
FAI (CNY trillion)	49.41	54.45		5.08
Industrial Value-added	3.80%	4.30%		7.50%

MANUFACTURING PMIS

Downstream data:	Nov	Dec	Jan	Feb
Real estate investment *	13.731	14.760	14.760	1.450
New Construction starts ytd**	1.828	1.989	1.989	150
Completed construction ytd**	688	1.014	1.014	122
Real estate sales ytd**	1.581	1.794	1.794	157

*(CNY billion) **million square metres

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