



China Sourcing Update

September 17, 2018

Energy Costs

1. Crude prices fall and then rise in August

In line with the movement of global crude prices, China's crude prices trended downward during early to mid-August and went up afterwards.¹ For instance, the Daqing² crude price dropped from US\$66.5 per barrel on 31 July to US\$62.4 per barrel on 16 August, before rising to US\$68.1 per barrel on 31 August (see exhibit 1).

There were two main reasons behind the fall in global oil prices during early to mid-August. First, there were market worries that the escalating trade war between the US and China could hurt global economic growth and thus the demand for oil. Second, the US crude oil inventories rose sharply: the US Energy Information Administration (EIA) reported on 15 August that commercial crude oil inventories (excluding those in the Strategic Petroleum Reserve) in the US increased by 6.8 billion barrels in the week ending 10 August.

Crude prices surged in the second half of the month on renewed market concerns over a tightened global crude supply, in particularly after reports surfaced that Iran's oil exports dropped in the first half of August due to the re-imposition of US sanctions against the country.³

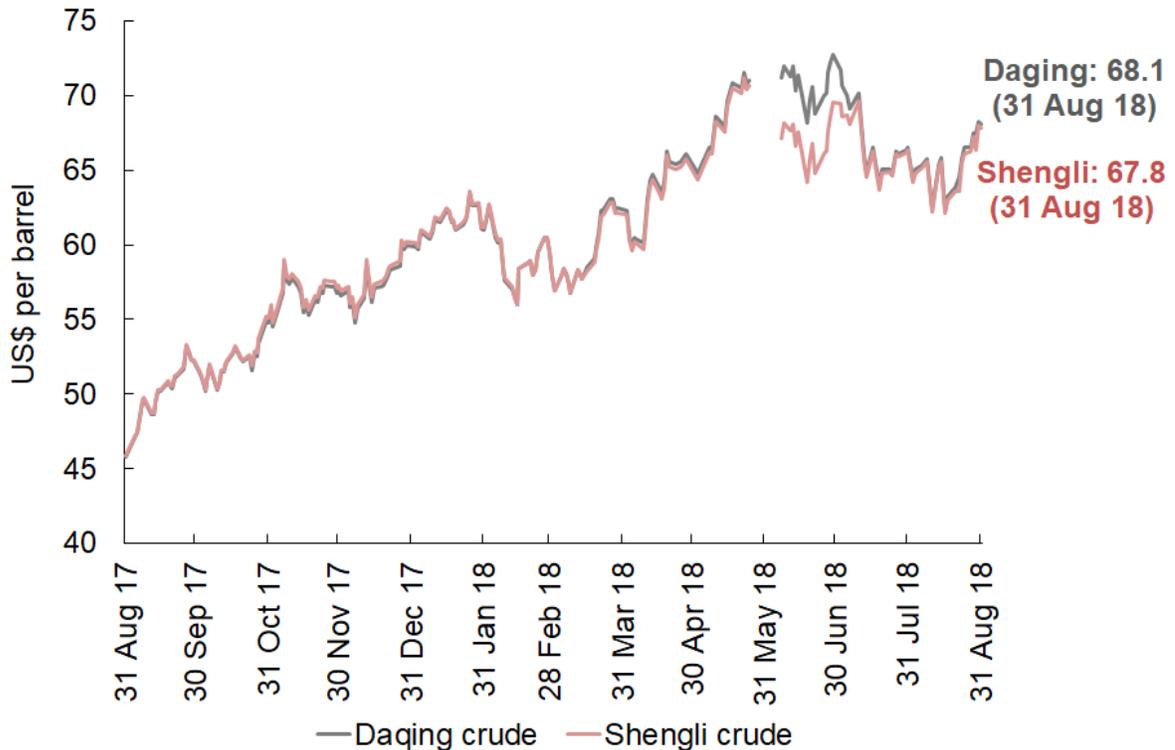
¹ From the year 2000 onwards, China's crude prices were determined with reference to global crude prices.

² Daqing Field is the largest oil field in China.

³ The first round of renewed US sanctions against Iran entered into effect on 7 August, while the next round of sanctions, including restrictions on Iran's oil exports, will take effect on 4 November.

Looking ahead, we expect that global crude prices will continue to fluctuate in the near future amid developments in the China-US trade war as well as geopolitical tensions in the Middle East.

Exhibit 1: China's crude prices, August 2017 to August 2018



Source: ifeng.com, gcec.com.cn

2. Wholesale price index of refined oil products goes up in August

The wholesale price index of refined oil products rose by 3.6% mom in August (see exhibit 2).⁴ Specifically, the wholesale price index of diesel jumped by 4.7% mom, while that of gasoline gained 3.4% mom.

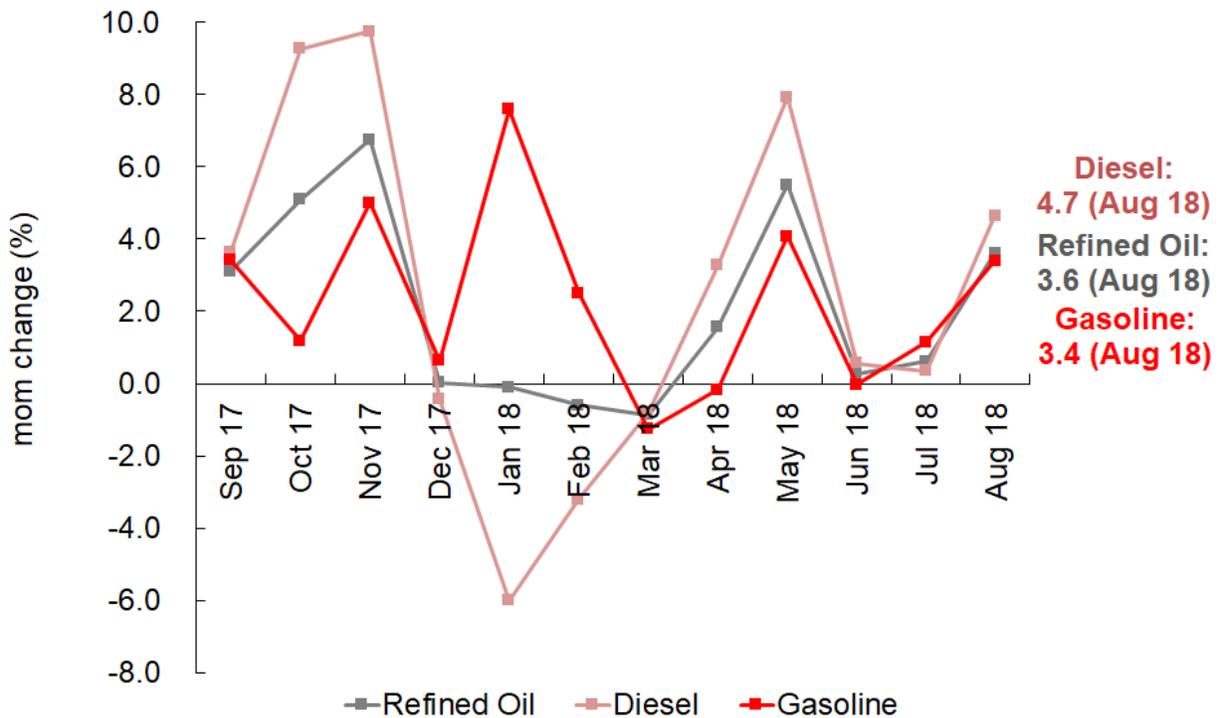
The National Development and Reform Commission (NDRC) made an upward adjustment to the maximum wholesale prices of refined oil products on 7 August and a downward adjustment on 21 August, resulting in higher average prices of refined oil products in August than in July. According to the pricing mechanism for refined oil

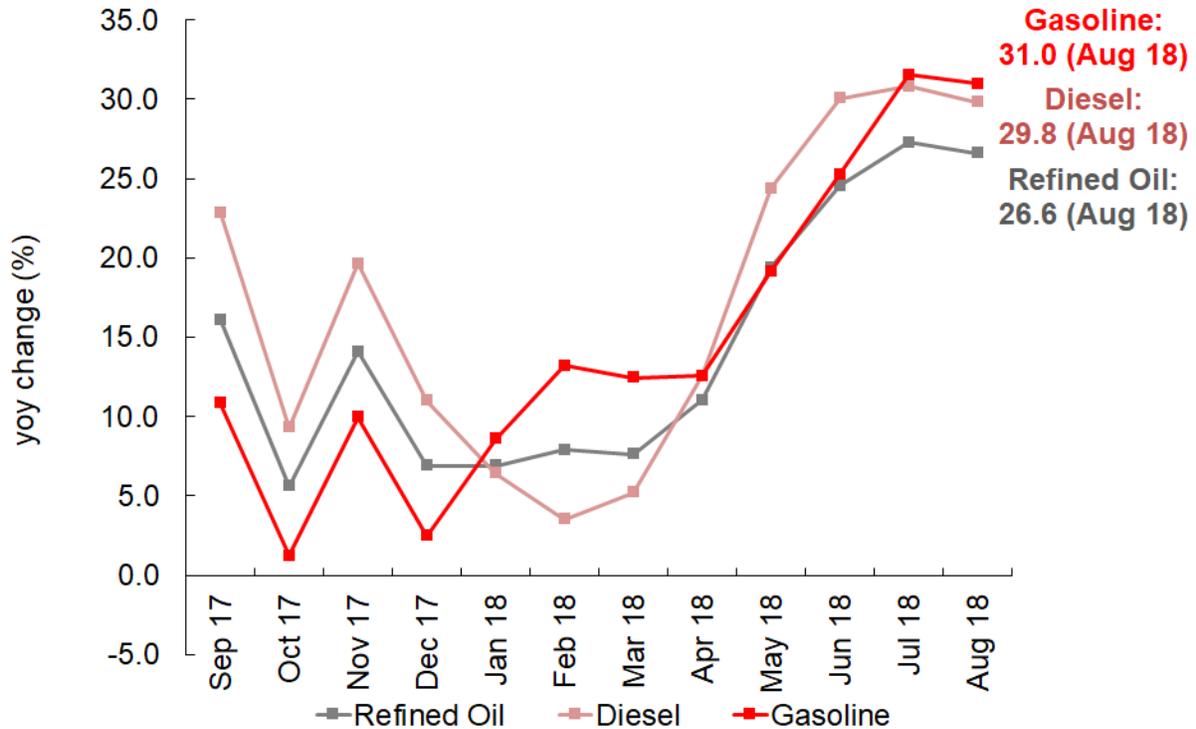
⁴ The index is compiled by the China Logistics Information Center (CLIC).

products, the maximum prices of diesel and gasoline are adjusted every 10 working days, based on the change in a basket of global crude prices.

Looking ahead, we expect the wholesale price index of refined oil products to increase further in September, as the NDRC raised the maximum prices of diesel and gasoline again on 4 September in response to higher global crude prices during late August to early September.

Exhibit 2: China's wholesale price indices of refined oil products, September 2017 to August 2018





Source: China Logistics Information Center

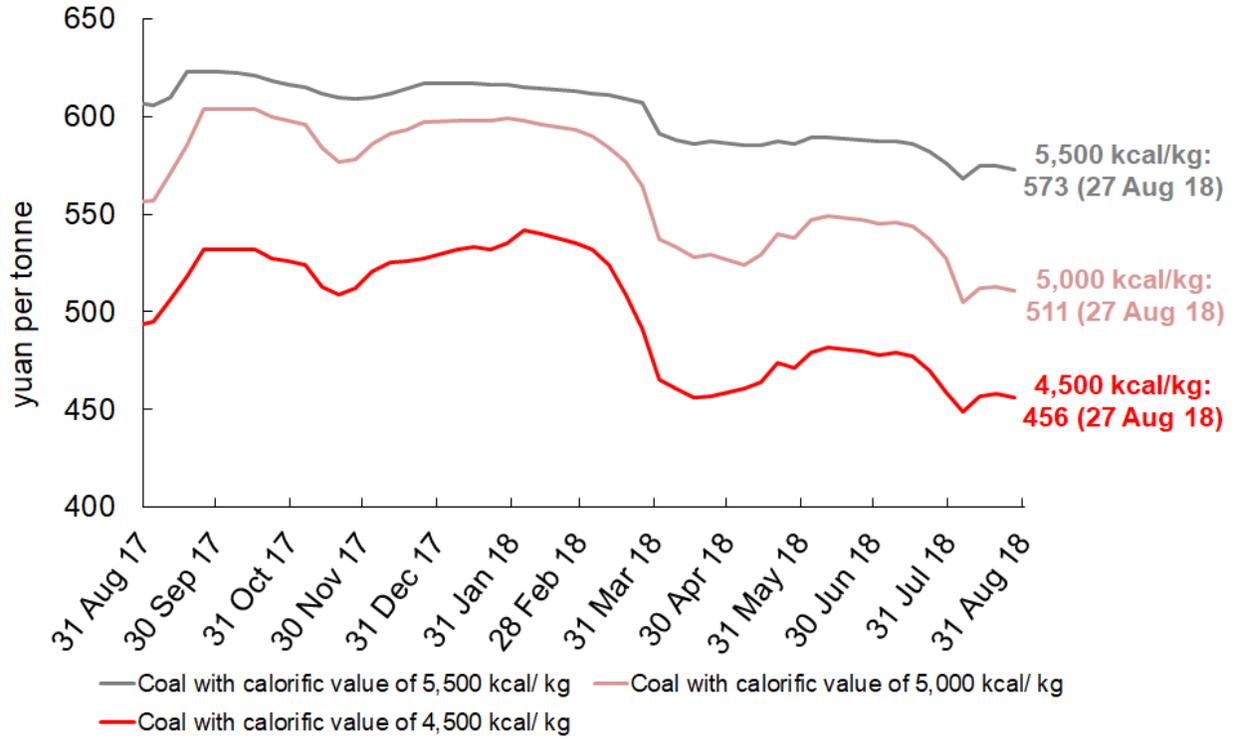
3. Benchmark Qinhuangdao coal prices bottom out in August

The benchmark Qinhuangdao coal prices fell in early August and picked up afterwards (see exhibit 3). For example, after going down from 527 yuan per tonne on 30 July to 505 yuan per tonne on 6 August, the price of coal with calorific value of 5,000 kcal/ kg rebounded to 511 yuan per tonne on 27 August.

The bottoming-out of domestic coal prices in the month was triggered by an improved demand for coal from power producers in the current high season for power consumption, and a surge in the prices of coal futures in China in early August.

From 20 August to 20 September, safety checks would be conducted on coal mines in major coal-producing provinces across China. As the domestic coal supply is likely to tighten, we expect coal prices to trend upward in the foreseeable future.

Exhibit 3: Qinhuangdao coal prices, August 2017 to August 2018



Source: ifeng.com, cctd.com.cn

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