



China Sourcing Update

November 5, 2015

Energy Costs

1. Crude prices fluctuate

In line with the movement of global crude prices, China's crude prices fluctuated during September, before rising in early October. For example, the Daqing¹ crude price fluctuated between US\$ 38.2 per barrel and US\$ 43.2 per barrel during September.² Afterwards, it went up from US\$ 38.5 per barrel on 2 October to US\$ 44.1 per barrel on 9 October, before dropping back to US\$ 41.2 per barrel on 13 October (see exhibit 1).

The increase in global oil prices in early October was largely due to the expectation that the oil output in the US will decline, as the number of operating oil-drilling rigs in the US drops. According to the US-based oilfield services provider Baker Hughes Inc., the number of operating oil-drilling rigs in the US decreased to 605 on 9 October, the lowest since August 2010.

Since mid-October, however, the concerns over the lingering oversupply from the Organization of the Petroleum Exporting Countries (OPEC) have triggered a drop in global oil prices again. According to secondary sources quoted by the *Monthly Oil Market Report* published by the OPEC on 12 October, oil production from the OPEC member countries increased by 109,000 barrels per day from the previous month to reach 31.57 million barrels per day in September, higher than its target of 30 million barrels per day.

Looking forward, according to the International Energy Agency (IEA)³, the growth of oil demand is projected to be slower in 2016, compared to this year.⁴ Also, the crude

¹ Daqing Field is the largest oil field in China.

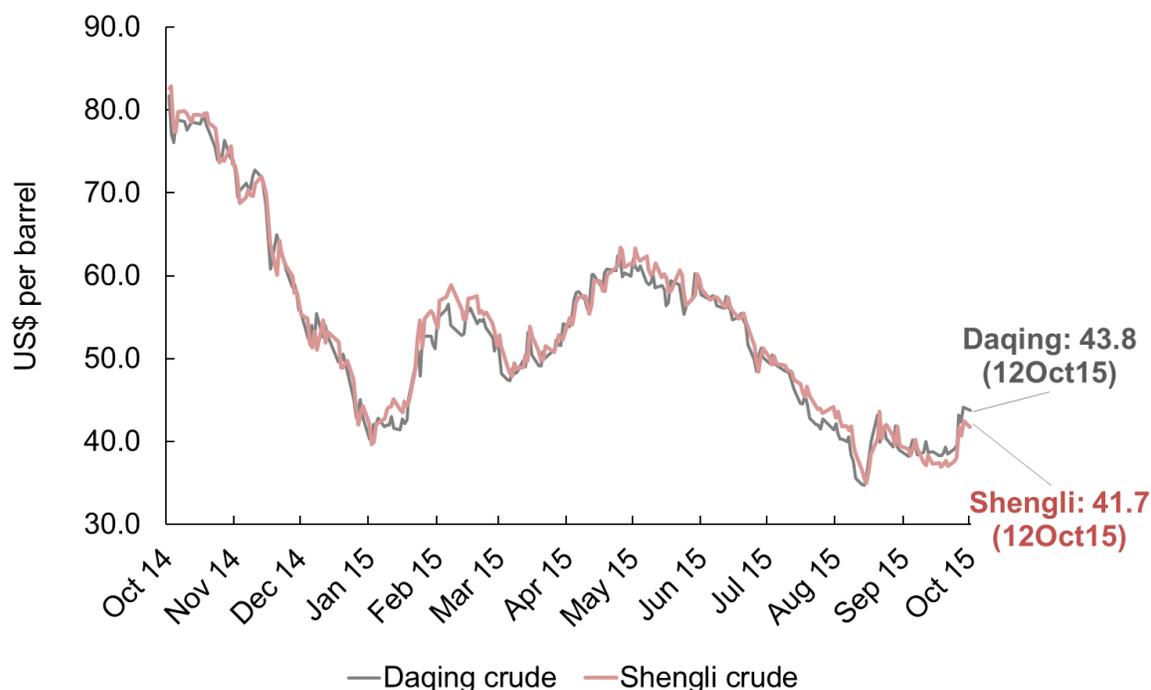
² From the year 2000 onwards, China's crude prices were determined with reference to global crude prices.

³ The International Energy Agency (IEA) is an organisation which works to ensure reliable, affordable and clean energy for its 29 member countries, representing some of the world's largest oil consumers.

⁴ <https://www.iea.org/oilmarketreport/omrpublic/>

supply from Iran is expected to return to the international market soon, which will add to the oversupply woes. Thus, we expect the oil prices to remain at low levels in the near future.

Exhibit 1: China's crude prices, October 2014 to October 2015



Source: ifeng.com

2. Wholesale price index of refined oil products rises

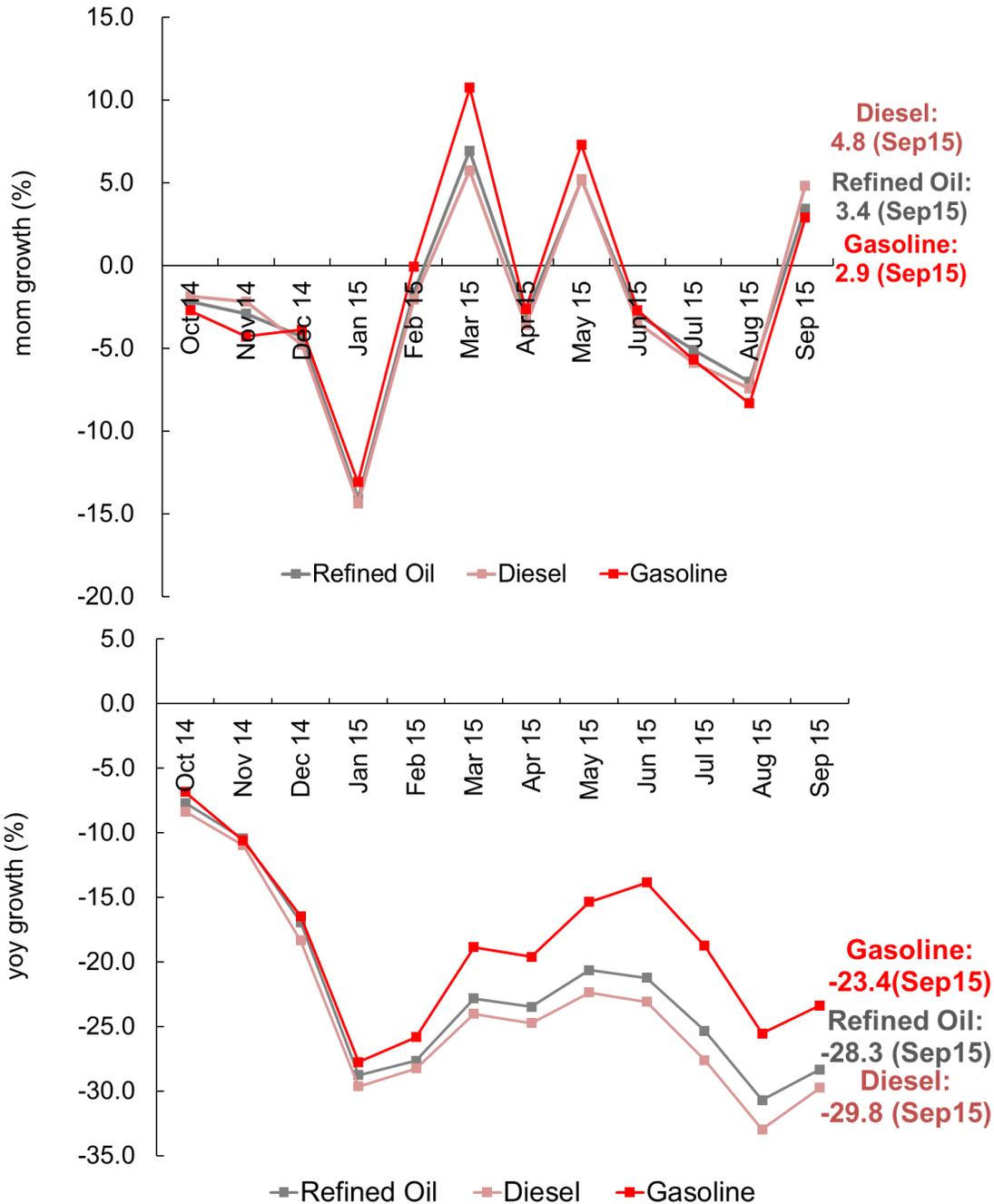
The wholesale price index of refined oil products rose by 3.4% mom in September (see exhibit 2).⁵

The movement of the price index in the month was mainly driven by the government moves to adjust the wholesale prices of refined oil products. The National Development and Reform Commission (NDRC) made an upward adjustment on the wholesale prices of refined oil products on 17 September, in response to the rise in global crude prices in the first half of September.

Looking ahead, the future movement of the wholesale prices of refined oil products will depend mainly on the movement of global crude prices. According to the pricing mechanism of refined oil, the fuel prices are adjusted every 10 working days, based on the change in a basket of global crude prices. If the computed amount of fuel price change is less than 50 yuan per tonne, no adjustment will be made, and the amount will be accumulated for the next round of adjustment.

⁵ The index is compiled by the China Logistics Information Center (CLIC).

Exhibit 2: China's wholesale price indices of refined oil products, October 2014 to September 2015



Source: China Logistics Information Center

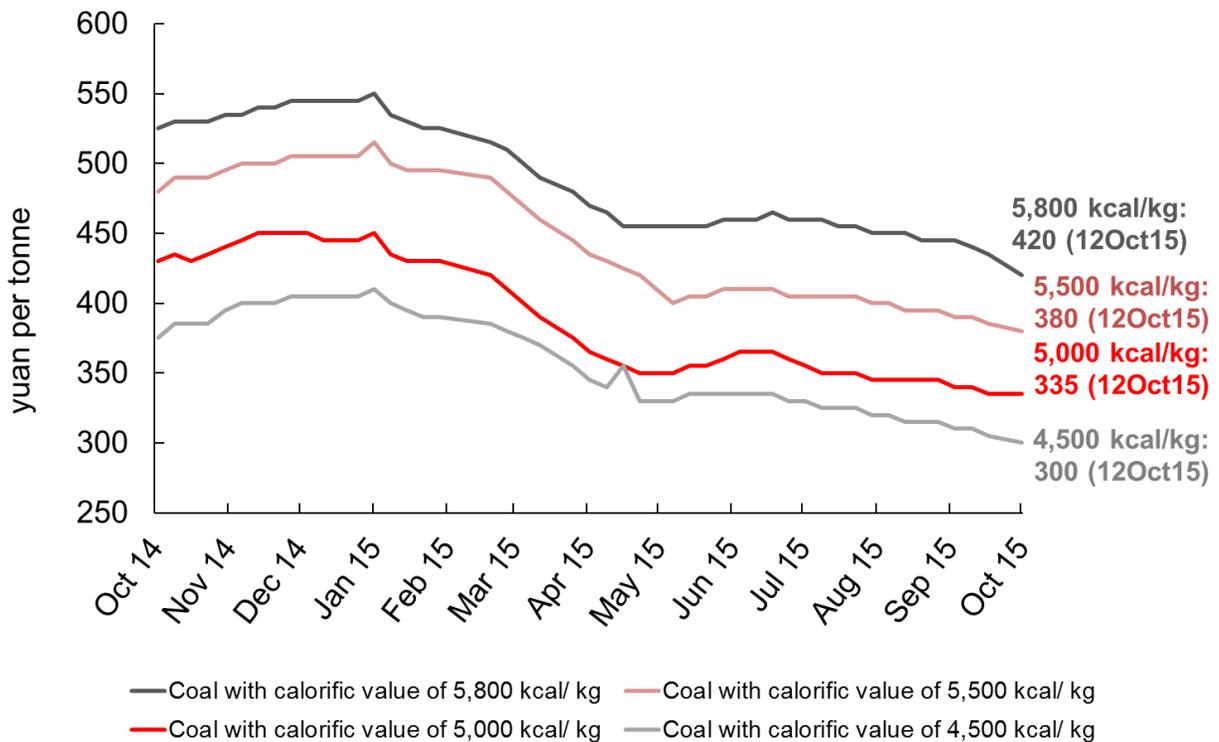
3. The benchmark Qinhuangdao coal prices fall

The benchmark Qinhuangdao coal prices have continued to drop in recent months (see exhibit 3). For instance, the price of coal with calorific value of 5,500 kcal/ kg came in at 380 yuan per tonne on 12 October, the lowest level since November 2004.

According to the local media, although September and October are the traditional high season for the coal market, the domestic demand for coal was weak during the period, amid the moderating growth of China's economy. Also, the overcapacity problem in the coal industry still remains severe, and the coal inventory levels of many power producers are high.

Looking ahead, the heating demand will increase during the coming winter, which will help support the coal prices. Thus, domestic coal prices may show a mild rebound in the near term.

Exhibit 3: Qinhuangdao coal prices, October 2014 to October 2015



Source: Cqcoal.com

THE FUNG BUSINESS INTELLIGENCE CENTRE

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