



China Sourcing Update

November 17, 2017

Energy Costs

1. Crude prices climb in October

In line with the movement of global crude prices, China's crude prices fell in early October and increased afterwards.¹ For example, after falling from 52.2 per barrel on 29 September to US\$ 50.2 per barrel on 4 October, the Daqing² crude price rose to a two-year high of US\$ 54.9 per barrel on 30 October (*see exhibit 1*).

The main reason for the jump in global oil prices in the month were geopolitical tensions in the Middle East. In mid-October, Iraq's central government took military action to regain control of oil fields in the Kurdistan region, which held an independence referendum in late September. Crude oil supplies from Iraq dropped amid production disruptions and ongoing tensions over the region. Meanwhile, the US President Donald Trump refused to certify Iran's compliance with a 2015 international agreement that limits its nuclear development, and announced a new strategy on Iran that includes new sanctions on the country. These moves raised market concerns that Iran's oil export capacity could be undermined.

Moreover, expectations of an extension of the oil production cuts led by the Organization of the Petroleum Exporting Countries (OPEC) drove oil prices higher in late October. It was reported that Saudi Arabia and Russia, the top two crude producers

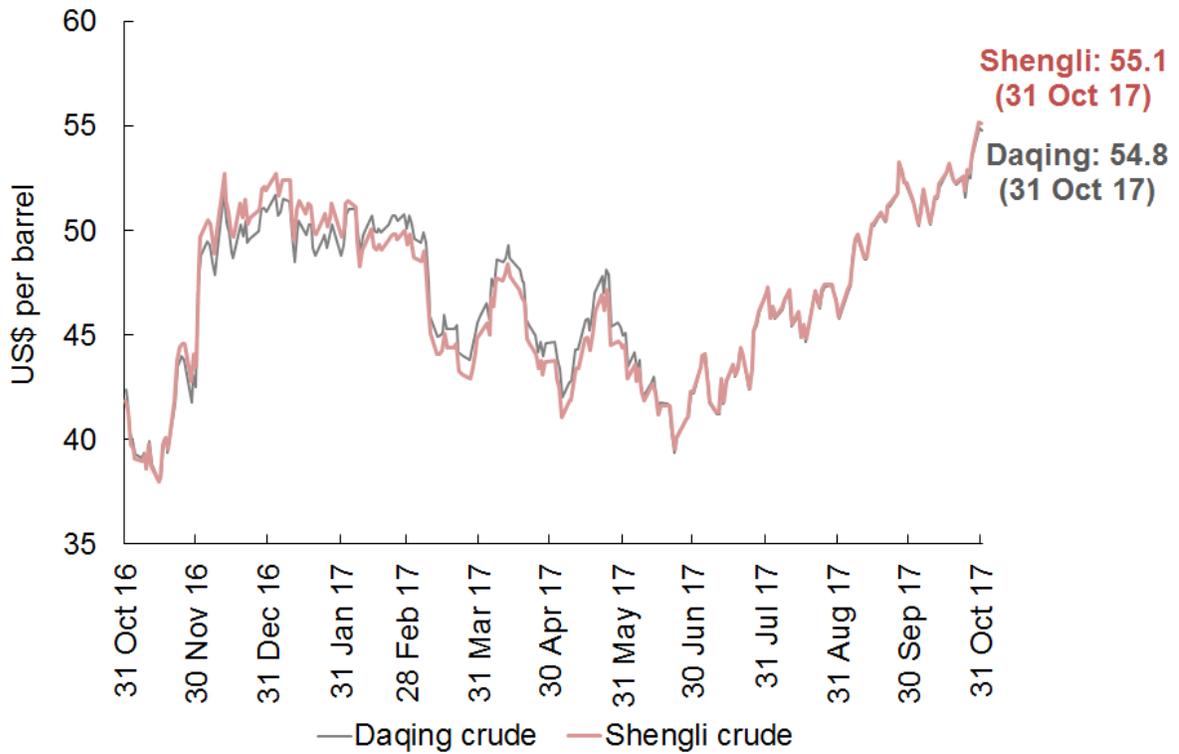
¹ From the year 2000 onwards, China's crude prices were determined with reference to global crude prices.

² Daqing Field is the largest oil field in China.

in the world, intended to extend the OPEC-led output cuts through the end of next year, further easing market fears over an oil supply glut.

Looking ahead, we expect global oil prices to stay high in the near future as the positive factors mentioned above are expected to persist.

Exhibit 1: China's crude prices, October 2016 to October 2017



Source: ifeng.com

2. Wholesale price index of refined oil products advances in October

The wholesale price index of refined oil products jumped by 5.1% mom in October (see exhibit 2).³ Specifically, the wholesale price index of diesel surged by 9.3% mom, while that of gasoline went up by 1.2% mom in the month.

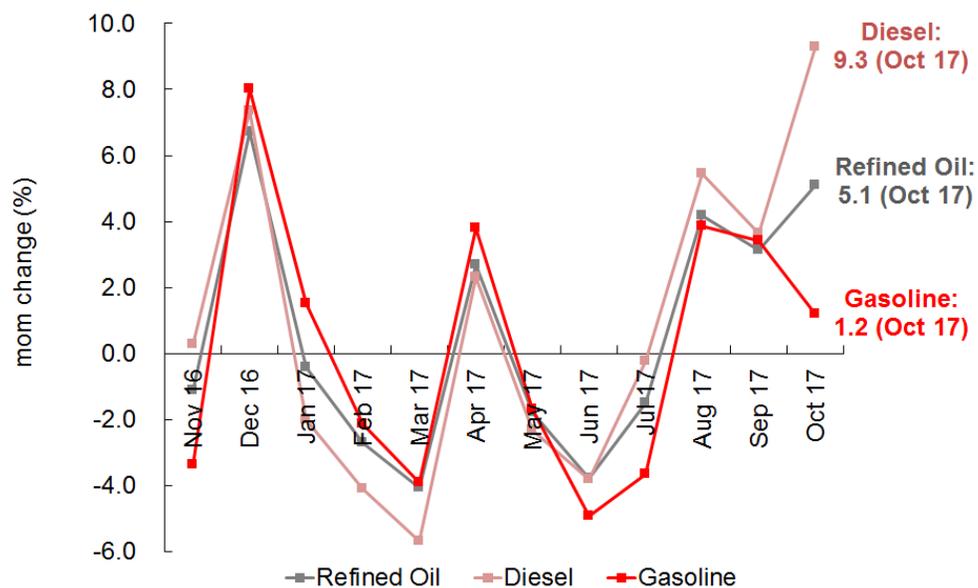
The movement of the price index in the month was mainly driven by the government move to adjust the wholesale prices of refined oil products. The National Development

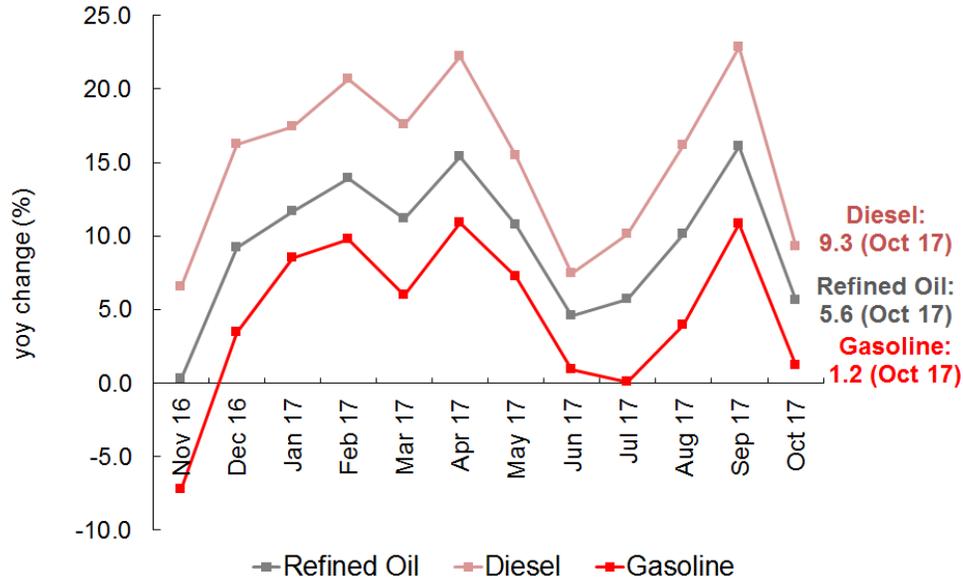
³ The index is compiled by the China Logistics Information Center (CLIC).

and Reform Commission (NDRC) made an upward adjustment to the maximum wholesale prices of refined oil products on 30 September, which translated into higher wholesale prices of refined oil products in October.

Looking ahead, we expect the wholesale price index of refined oil products to continue to rise in November, as the NDRC raised the maximum prices of diesel and gasoline again on 3 November and 17 November following a further increase in global crude prices during mid-October to early November. According to the pricing mechanism for refined oil 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.

Exhibit 2: China's wholesale price indices of refined oil products, November 2016 to October 2017





Source: China Logistics Information Center

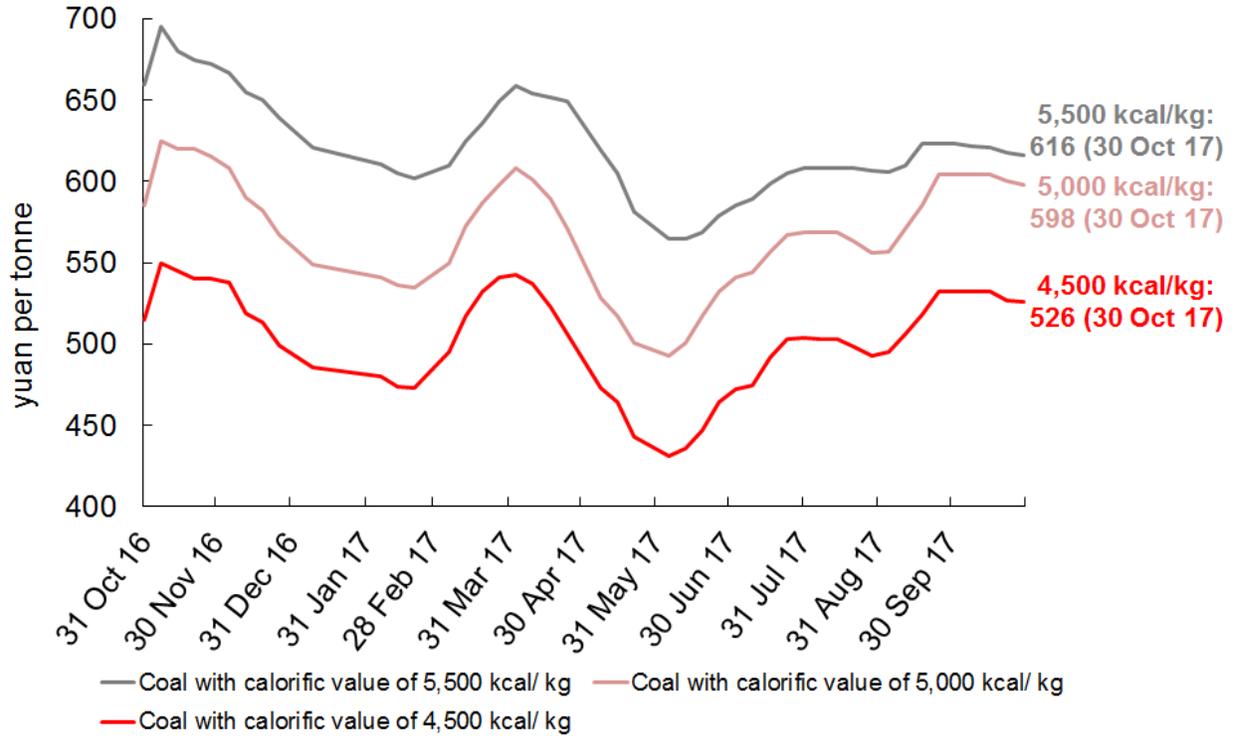
3. Benchmark Qinhuangdao coal prices edge down in October

The benchmark Qinhuangdao coal prices fell slightly in October (see exhibit 3). For instance, the price of coal with calorific value of 5,500 kcal/ kg went down from 623 yuan per tonne on 25 September to 616 yuan per tonne on 30 October.

In our view, the main reasons for the slight drop in domestic coal prices in the month were a decline in demand for coal from power producers and a rise in the domestic supply of coal.

Looking ahead, we believe that domestic coal prices will trend slightly downward in the near future, as the demand from power producers is likely to remain soft in the current low season for power consumption.

Exhibit 3: Qinhuangdao coal prices, October 2016 to October 2017



Source: ifeng.com, cctd.com.cn

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