

## Green Shoots

Macro Drivers of China's Industrial Metals Demand – 13<sup>th</sup> March, 2019



## Financial market rally could precede fundamental improvement

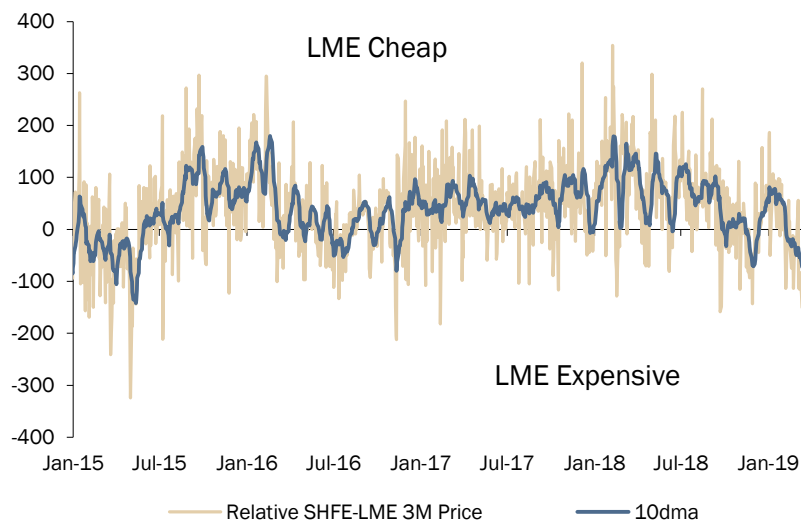
- In our 5<sup>th</sup> February report – *What's in the price?*<sup>1</sup>, we noted that “Once short covering has played out, we will need to see confirmation that growth – and, hence, commodities demand – is picking up, if another leg higher in prices is to be justified.”
- Since then, micro indicators have remained relatively subdued, with SHFE-LME “arbs” broadly closed and physical metal premiums in the doldrums.
- Nevertheless, a number of metals have made further gains, with copper prices up 4% and palladium 11% higher.
- This therefore remains more of a financial than fundamental rally – indeed, low volatility and steady momentum mean much of the buying has likely been systematic in nature – but we think the macro conditions for an improvement in Chinese demand are now falling into place.

### Physical copper premiums remain subdued



Source: ICBC Standard, Bloomberg, LME, SMM

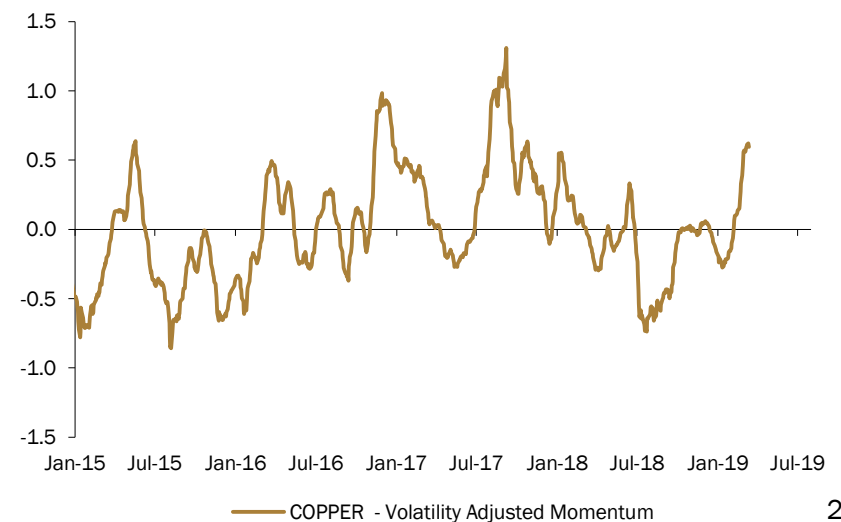
### And the China import arbitrage for copper is closed



Source: ICBC Standard, Bloomberg, LME, SHFE

1: See - <https://www.icbcstandardbank.com/CorporateSite/ResearchStrategy/Reports>

### Much of the recent buying likely to be systematic

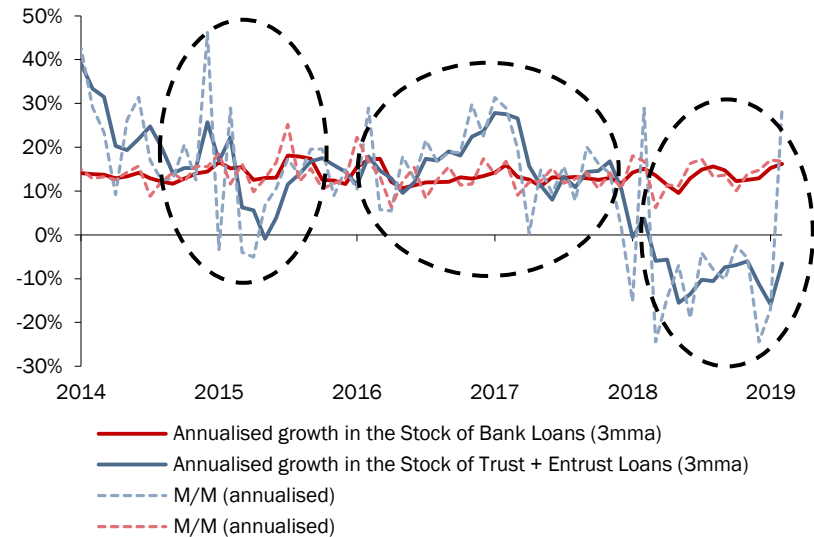


Source: ICBC Standard, Bloomberg, LME

## Changing composition of credit growth a potential “green shoot”

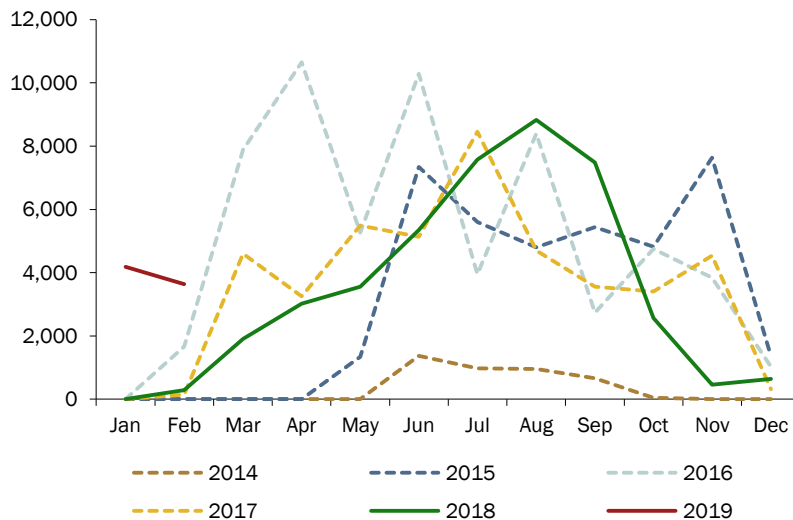
- January’s 4.6trn RMB total social financing (TSF) figure topped consensus estimates by 40%. However, anyone who believed that heralded the starting gun for a dramatic credit stimulus will have been bitterly disappointed by February’s consensus missing 0.7trn RMB TSF figure.
- We have not expected aggressive stimulus but, as per our January 25th note – *Stimulus, where art thou?*<sup>1</sup>, we have been looking for signs that more dovish rhetoric would lead to a policy shift from tightening in 2018 to loosening in 2019.
- For three reasons, we think that is now the case:
  - Deleveraging of trust and entrust lending appears to have paused, this was a major headwind in 2018.
  - Local government bond issuance was abnormally strong in January/February, this should precede increased infra spend.
  - Long-term household loans surged in January, we therefore expect housing sales to stabilise.

### Non-bank deleveraging taking a pause in Jan and Feb



Source: ICBC Standard, Bloomberg, China NBS, PBoC

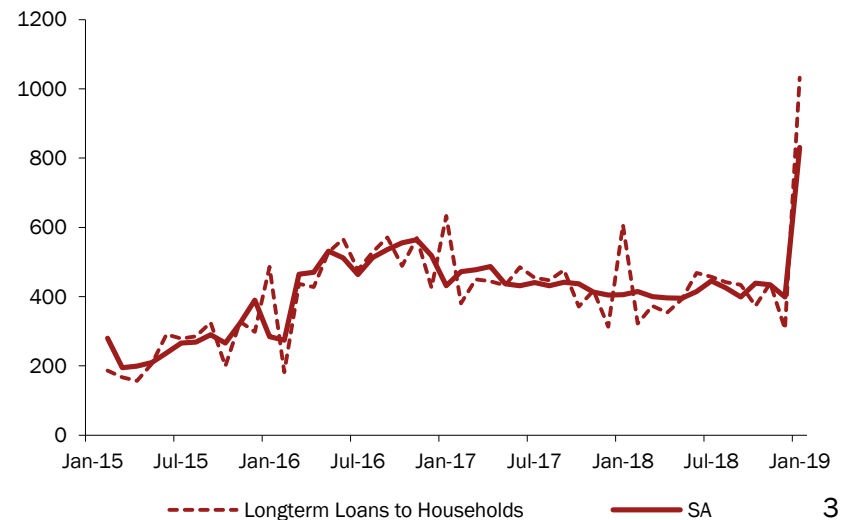
### Local government bond issuance off to a strong start



Source: ICBC Standard, Bloomberg, China NBS, PBoC, Chinabond

1: See - <https://www.icbcstandardbank.com/CorporateSite/ResearchStrategy/Reports>

### Long-term household loans jumped in January

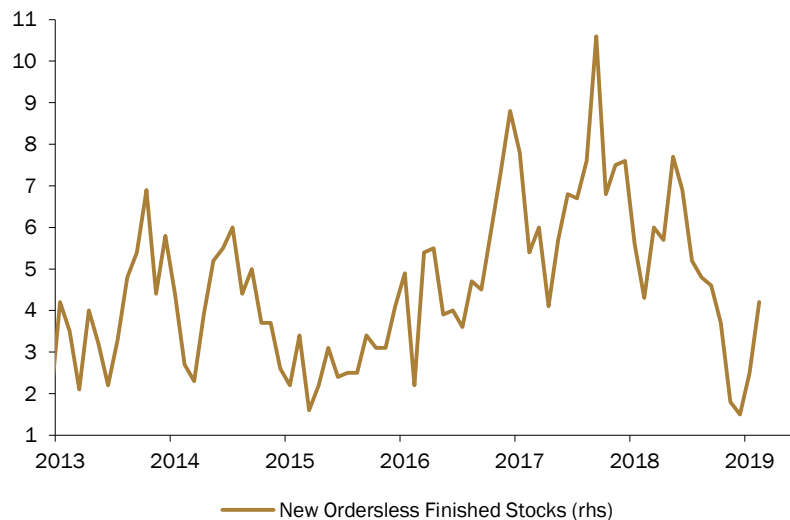


Source: ICBC Standard, Bloomberg, China NBS, PBoC

## PMIs register flicker of an upturn

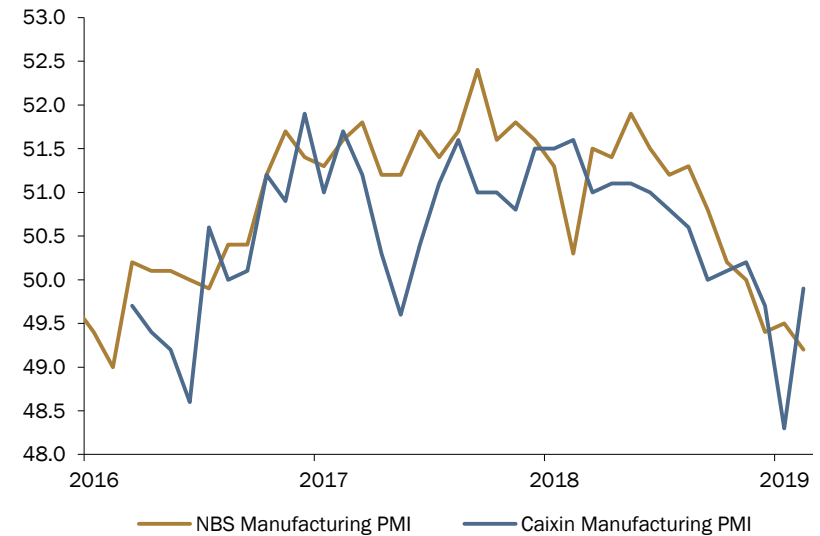
- In addition to this, the underlying detail of February's PMIs offered signs of marginal improvement.
- Beyond the Caixin PMI's headline bounce, it should be noted that the official PMI's new orders sub-index rose to 50.6 from 49.6 in January, while manufacturers' finished inventories declined to 46.4 from 47.1.
- Taking the spread of these two indicators as a proxy for demand, December's 1.5 may have marked the recent trough.
- Although the output index reading of 49.5, down from January's 50.9, remained soft, it would be natural for demand to turn first and manufacturers' activity to then follow.
- Nevertheless, for any cyclical recovery to prove sustainable, it will still require an improvement in liquidity conditions for the private sector and small companies in particular.

### And signs of a demand improvement in the official PMI's details



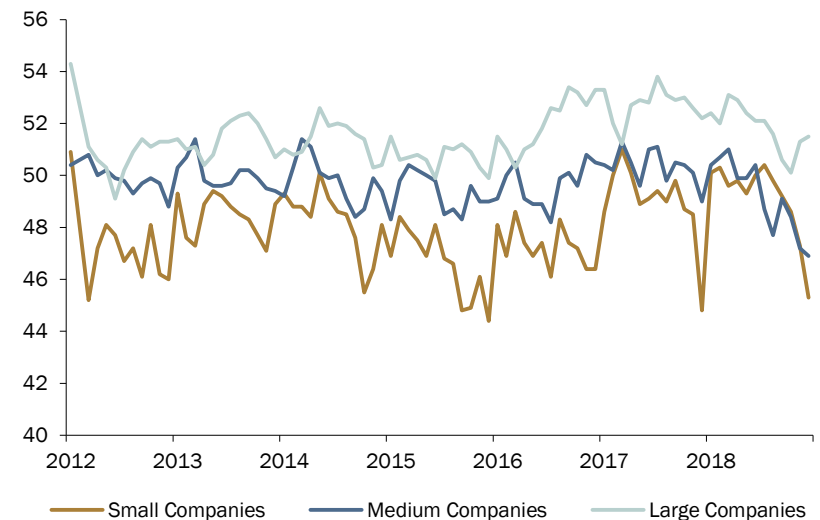
Source: ICBC Standard, Bloomberg, China NBS

### Caixin PMI potentially turning the corner



Source: ICBC Standard, Bloomberg, China NBS, Caixin

### But small companies continue to struggle

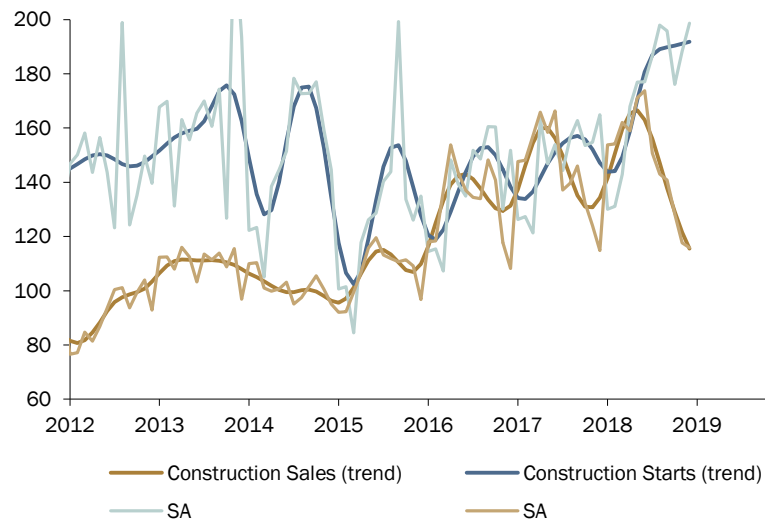


Source: ICBC Standard, Bloomberg, China NBS

## The market will need to look through February data distortions

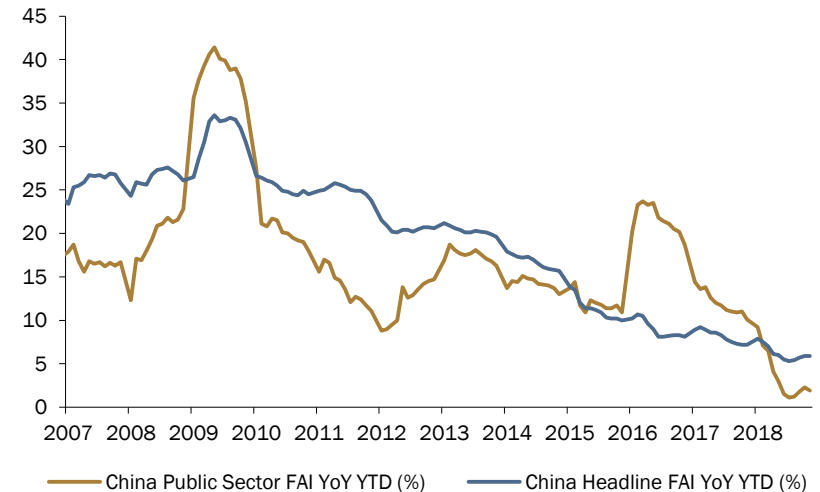
- The remainder of February's macro figures, the majority of which are to be published on Thursday, will still suffer from the usual seasonal distortions that plague data around lunar new year.
- With markets already moving higher, however, market participants understandably cannot wait until March figures for greater clarity on whether or not this nascent cyclical recovery has legs.
- We will therefore be looking for two particular developments:
  - Increased public fixed asset investment, particularly from infrastructure spending.
  - A bottoming out of housing sales. Although starts will need to stall in order to limit inventory build-up, better housing sales would reassure us of upcoming sectoral commodity demand.
- We do not though expect an improvement in the autos sector. Until there is policy clarity on what support will be forthcoming, it is likely to remain a drag.

### Housing sales should bottom but starts could still catch down



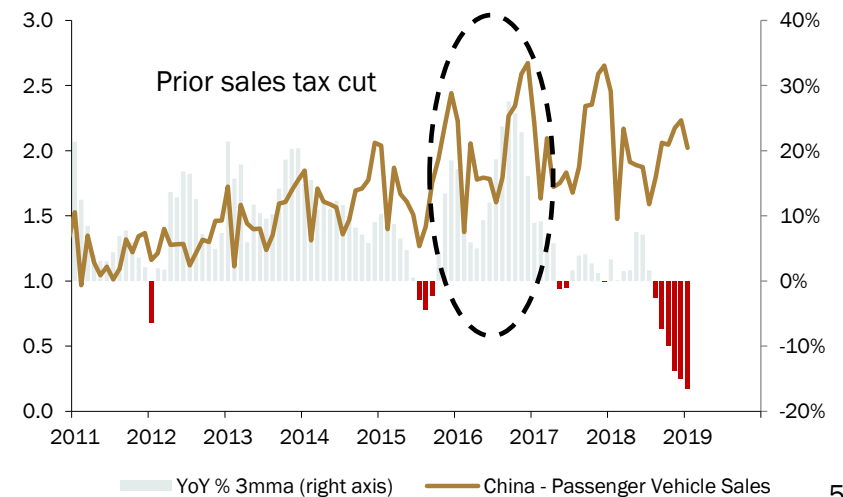
Source: ICBC Standard, Bloomberg, China NBS

### Public FAI growth may have bottomed but is yet to truly bounce



Source: ICBC Standard, Bloomberg, China NBS

### Weak auto sales, waiting for a policy response



Source: ICBC Standard, Bloomberg, China NBS, CAAM

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