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21 March 2022

CHINA MACRO-WEEKLY

Table of Contents

Date	Indicator	Latest	Last Month	MoM Change
Leading Economies' Economic Performance				
28/Feb	Global Manufacturing PMI	53.6	53.2	0.4
28/Feb	US Manufacturing PMI	58.6	57.6	1.0
28/Feb	China Manufacturing PMI	50.2	50.1	0.1
28/Feb	Caixin Manufacturing PMI	50.4	49.1	1.3
28/Feb	EU Manufacturing PMI	58.2	58.7	-0.5
Global Demand				
18/Mar	Philadelphia Semiconductor Index, %YoY	15.3%	9.7%	5.6%
28/Feb	South Korea Export %YoY	20.6%	15.2%	5.4%
28/Feb	China Export, %YoY	6.2%	24.1%	-17.9%
China Economic Indicators				
28/Feb	Import, %YoY	10.4%	19.8%	-9.4%
28/Feb	Industrial Production, %YoY	12.8%	3.9%	8.9%
28/Feb	Fixed Asset Investment, YTD%YoY	12.2%	4.9%	7.3%
28/Feb	Social Financing, %YoY	-30.8%	19.0%	-49.8%
28/Feb	M1 %YoY	4.7%	-1.9%	6.6%
28/Feb	M2 %YoY	9.2%	9.8%	-0.6%
Other Commodities' Prices				
18/Mar	Gold Spot Price, $/oz	1,922	1,854	3.7%
18/Mar	WTI Crude Oil, $/bbl	105	92	14.1%
18/Mar	ZCE Thermal Coal	829	775	7.0%
18/Mar	LME 3-Month Copper, $/t	10,306	9,974	3.3%
18/Mar	SHFE Copper, CNY/t	72,650	71,070	2.2%
18/Mar	SHFE Rebar, CNY/t	4,953	4,728	4.8%
18/Mar	SHFE HRC, CNY/t	5,129	4,843	5.9%
18/Mar	DCE Iron Ore, CNY/t	834	699	19.2%

China's Housing Sales are Bound to Recover with Continuous Support from Policies

Report Highlights

- **China's land investments and newly started floor space will be weak in 2022.** Housing sales remain in contraction despite improving from -16% YoY decline in December 2021 to -10% in January and February. The March-to-date floor space of buildings sold in 30 mid to large-sized cities fell by -50% YoY. However, sales are bound to recover if the regulators are consistent with their loosening efforts. Sales recovery will help sustain under-construction activities, supporting construction and installation investments. On the other hand, land purchases will be weak without a relaxation of leverage controls.

- **China's 2022 flat glass consumption will be flat YoY, with supply in excess due to new capacity.** The real estate sector accounts for 80% of flat glass demand. There is a misconception that flat glass demand will be robust in 2022 due to an expected increase in completed floor space. Doors and glass window installations are completed before floor space gets completed, leading to flat glass production preceding finished floor space by eight months. On the other hand, newly started floor space provides a leading indication for flat glass production. Under a 20-month leading relationship, flat glass consumption will be flat YoY.

Commodity Development and Market Outlook: Ferrous

Commodity	Near-Term Outlook	Market Overview and Trading Recommendations:	Active Futures	Latest	Average		
					Feb-22	Jan-22	Mar-21
Ferrous				CNY/t			
Steel	Positive to Neutral	-China's Omicron containment may delay consumption, but once the condition improves, there may be a rush to complete backlogs, similar to 2020's post-COVID-19 situation (assume no change in total demand). This will lead to a steel price rebound during the period. -That said, construction work is only suspended for a week and should resume this week. Logistics are affected more during the containment. -China's weak real estate sector will weigh down 1H 2022 downstream steel consumption. -Recent rebar price movements are affected more by expectations than fundamentals, as the market agrees that demand will be weak and the seasonal rebar inventory drawdown will be slow. Weak demand and a steady increase in production will serve as a cap for near-term steel prices, which shall hover close to the current high. The market may only trade on fundamentals after the virus gets contained or policy supports slow down. -Production profits have narrowed but still not enough to lead to a production cut. On the other hand, raw materials supply shortages, such as coking coal, can slow down steel production recovery. Trading Recommendations: 1. Rebar prices to fluctuate at CNY 4,800-4,970/t. HRC to fluctuate at CNY 4,980-5,285/t. Based on production costs. 2. Weak demand and a steady increase in production will narrow production profits. Short steel production profits based on active futures. Risk: Coking coal shortage. 3. Better demand outlook in 2H 2022: SHFE 05-10 rebar futures to narrow. Entry point: >CNY 120/t.	SHFE Rebar	4,953	4,892	4,618	4,773
			SHFE HRC	5,129	5,025	4,736	5,043
Iron Ore	Positive	-Brazil has ordered Vale to evacuate workers at its Northern Brazil Carajas iron ore mining area within 60 days due to heavy rainfalls, which raises a risk at the dam. The dam is used to store transiting products and will have minimal impact on Vale's output (for now). Furthermore, the rainy season will end after 60 days. Nevertheless, wet weather will lead to a YoY decline in Brazil's 1H 2022 shipments. Along with a suspension of Ukraine's shipments, high-grade iron ores supplies have tightened. -Northern China's pig iron production continues to recover, but containment measures and logistics problems could affect iron ore transportation and demand, pressuring near-term spot prices. Stricter containment measures are enforced in Tangshan. Some Tangshan mills' production will be affected as they hold onto low inventory, and the containment measures hinder iron ore transportation to mills. -Meanwhile, low iron ore arrivals and steel mills' production resumption have brought forward the seasonal drawdown of port stocks. China's port stock may fall by 20Mt to around 140Mt by end-Q2 2022. Trading Recommendations: 1. Consider buying DCE 09 iron ore after slight corrections driven by a delay in steel mills' iron ore purchases. 2. Basis spread to widen after the end of March as the virus gets contained.	DCE Iron Ore	834	737	735	1086
Coking Coal	Positive	Coking Coal -China's coal and steel production are picking up. Last week's average hot metal production was 2.2Mt/day, and coking coal output was 6.2Mt. Coking coal inventory dropped by 20Kt WoW, suggesting that 6.2Mt of coking coal is enough to fulfill 2.2Mt/day of pig iron production. If coking coal production rose to 6.5Mt, it can meet 2.3 to 2.33Mt/day of hot metal production. There is a risk that a slow domestic coking coal supply (output and imports) recovery will disrupt steel output, driving up the prices of products in the supply chain. -Buying coking coal is akin to bullish expectations for coal prices. Coking coal on-warrant prices are CNY 3,200, and coke prices are CNY 3,750/t. -Overall, China's coking coal supply remains tight, with inventory drawn down to a historic low. -Risk: 1) China's policy intervention on thermal coal prices will affect coking coal and coke prices. 2) Weak downstream steel consumption.	DCE Coking Coal	3,051	2,484	2,277	1,541
Coke	Positve	Coke: -High coking coal prices, steel mills' production profits, and a rise in restocking interest with pig iron production bottoming out are supportive of spot coke prices. Traders' buying interest has increased with more supplies shifted to ports. -Coke futures prices will be lifted when steel mills lift pig iron production further. Trading Recommendation: 1. Market will continue to trade on the buoyant coking coal demand until steel mills complete their resumption by 1H-April. Then the strength of downstream steel consumption will impact coking coal. 2. Coking coal balance sheet is healthier than coke.	DCE Coke	3,691	3,213	3,049	2,305
Flat Glass	Positive to Neutral	-China's flat glass inventories are building up with Omicron disrupting downstream demand. However, if there is demand, it will return after the virus gets contained. -High factory inventory puts a lid on price, while delay in downstream demand forms a floor to prices. If the production to sales ratio improves in the near term, investors can consider buying at a small amount to trade on potential price rebound. In the medium term, inventory needs to be drawdown to see support. -On the other hand, macroeconomic improvements support the far-month September contract. Trading Recommendation: 1. 05 futures to range-bound. Inventory drawdown may bring upside. 2. 05-09 flat glass price spread to narrow.	CZCE Glass	1,916	2,127	2,018	2,066
Soda Ash	Positive to Neutral	-Soda ash inventory drawdown will come before flat glass as factories plan to lower selling prices. Last week's spot prices were offered at CNY 2,620. -Prices have sufficiently priced into the high soda ash production and inventory, 400Ktpa of capacity restarts, and weak downstream demand. Production profits have returned to a reasonable level with good settlements recently. -If inventory starts to drawdown this week, there may be price support for soda ash. -There is room for flat glass factories to stock on soda ash as inventory has fallen to 36 days. Trading Recommendation: 1. In the near term, 05 soda ash will fluctuate with flat glass prices. 2. Long 09 soda ash contract when inventory starts to drawdown. Watch for demand recovery from April to May and new photovoltaic capacity. Risk: Weak flat glass fundamentals.	CZCE Soda Ash	2,526	2,871	2,548	1,912

Commodity Development and Market Outlook: Non-Ferrous

Commodity	Near-Term Outlook	Market Overview and Trading Recommendations:	Active Futures	Latest	Average		
					Feb-22	Jan-22	Mar-21
Non-Ferrous					CNY/t		
Copper	**Positive**	-The FED has confirmed to increase the FED rate to 0.25% to 0.5% and will finalize balance sheet plans in May. The FED has also lowered its economic growth projection and raised its inflation projections, suggesting that it is expecting stagflation in the U.S. - While the U.S. 10-year expected inflation has risen to 2.9%, supporting a valuation of $12,000/t for LME copper, it is becoming apparent that copper prices cannot keep up with the surging expected inflation. At the same time, crude oil prices are also looking at a correction. Expected inflation may exhibit the same trend as 2015, gradually easing from its peak. SHFE 3-Month Copper should fluctuate close to CNY 73,500/t with upsides from geopolitical risks and U.S. stagflation. -China's Omicron spread has disrupted the seasonal copper inventory drawdown. We will need to monitor the virus impact on downstream demand in the near term. -Local governments are working on providing more clarity on the enforcement of the cancellation of copper scrap tax rebate for unapproved recyclers. Trading Recommendation: SHFE 3-Month Copper should fluctuate close to CNY 73,500/t with upsides from geopolitical risks and U.S. stagflation.	SHFE Copper	72,830	71,213	70,317	66,517
Nickel	**Positive**	-Smelters continue to increase nickel matte production while NPI remains in shortage. -Upstream nickel ore is also in shortage as smelters increase NPI production due to lucrative profits. -Refined nickel settlements are awaiting prices to stabilize. Once it does, inventory drawdown will continue which will provide firm support for prices. Trading Recommendation: Await prices to stabilize before buying.	SHFE Nickel	219,620	174,918	162,549	124,065
Stainless Steel	**Positive**	-China's stainless steel inventory remains low after excluding the on-warrant stocks. Inventory did not build up despite an increase in March production, suggesting that downstream demand is firm. -Stainless steel production profits are at CNY 100/t, and the reasonable profits are at CNY 600-800/t. There is upside if inventory maintains a drawdown -High production costs, upstream raw materials shortage, high nickel prices, and firm stainless steel demand are bullish for stainless steel. Trading Recommendation: Buy at a low with high production costs as support at CNY 19.9K/t.	SHFE Stainless Steel	20,035	18,429	17,595	14,255
Aluminum	**Positive**	-Aluminum prices are boosted by the Chinese government's intention of relaxing Omicron control measures to minimize disruptions to economic activities. At the same time, downstream demand proves to be healthy, with inventory seeing a 53Kt WoW drawdown. -Supply: 1) TRIMET's Essen aluminum smelter (170Ktpa) in Germany plans to suspend 50% of production to push aluminum prices up. 2) China's aluminum supply at Binzhou may be affected by logistics disruptions due to stricter containment measures in the area. -TRIMET has indicated that Germany's aluminum production may face further cuts due to high natural gas and energy prices. Out of 631Ktpa of capacity in Germany, 154.3Ktpa of production has been suspended. In Europe, 936Ktpa of capacity has cut production. -On the other hand, if Russia cannot export its aluminum and China have to make up for the loss in supplies, its inventory will fall to 1.4 days, with production profits at CNY 5,500/t. Based on CNY 18,000/t costs, aluminum prices should be at CNY 23,500/t. -Not considering Russian exports, based on an expected 5.4% production fall in China due to the omicron spread and rising demand, the reasonable profits are at CNY 3,100. Based on CNY 18,000/t costs, aluminum prices should be at CNY 21,100/t. Trading Recommendation: 1. SHFE aluminum valued at CNY 21,100/t. 2. SHFE 1-month and 3-month aluminum price spread to widen. Risk: 1) China's COVID-19 condition, 2) Escalation of Russia and Ukraine war, and 3) FED rate hike.	SHFE Aluminium	22,830	22,743	21,222	17,309
Zinc	**Neutral**	-Nyrstar has announced plans to restart its Auby plant in France, following its maintenance in January 2022. However, the producer has indicated that high energy prices will continue to affect utilization. -Some European countries such as France have proposed to provide subsidies for smelters due to the high energy costs. As long as energy costs are high, European plants' utilization rate will remain low. Meanwhile, Europe's non-renewable energy prices have started to ease due to the end of winter. Zinc production is making a loss despite energy costs returning to pre-war levels. Production costs will support overseas zinc prices, which shall be range-bound. -China's downstream zinc demand has improved after prices stabilize, inventory has started to drawdown. Zinc production costs are at CNY 25,300 to CNY 25,500/t. Trading Recommendation: Zinc prices will hover at a high level, with production costs of CNY 25,300 to CNY 25,500/t as support.	SHFE Zinc	25,535	25,141	24,713	21,571

Commodity Development and Market Outlook: Energy and Chemicals

Commodity	Near-Term Outlook	Market Overview and Trading Recommendations:	Active Futures	Latest	Average		
					Feb-22	Jan-22	Mar-21
Energy					CNY		
Crude Oil	Positve to Neutral	-Two factors affecting near-term crude oil prices: 1) Supply: Sanctions on Russian supplies and U.S negotiations with Iran on lifting its sanctions (1M to 1.2M Bbl/day). 2) Demand: COVID-19 spread in China (short-term). -The lifting of Iran sanctions will not lead to supply excess as it will be under OPEC+ production controls. There is news saying that there will be an agreement within 72 hours, which can narrow Iran to China crude oil discounts of $5 to $5.5. -The U.S. has confirmed that it will ban crude oil imports from Russia. Its imports from Russia are small at 20 to 30 Bbl/day compared to the E.U. -Russia is Europe's biggest crude oil supplier. European countries' decisions on sanctions against Russian energy products will be crucial (especially Germany, Poland, Netherlands, and Finland). -China's Q3 2021 lockdown in Nanjing and Yangzhou (1.43% of China's GDP) due to the delta variant has led to a fall in crude oil consumption by 500 Bbl/day. The omicron containment is not as severe as Q3 2021. Still, it affects Shenzhen, Shanghai, Tianjin, and Jilin, which accounts for 8% of China's GDP, the expected fall in China's consumption is estimated at between 1M Bbl/day and 1.4M Bbl/day. Once the virus gets contained in April, there may be a rebound in demand. Trading Recommendation: Crude oil prices will correct and only bottom out when: 1) China COVID-19 gets contained, 2) There may be a rebound after U.S. finalizes the lifting of Iran sanctions. China's demand recovery will also provide upside.	WTI Crude Oil ($/Bbl)	105	92	83	62
Asphalt	Neutral	-Shandong independent refineries have reduced their operating rate to a low of 50.6%. At the same time, high asphalt prices have also reduced downstream restocking interest, with factories' inventory rising YoY. Demand will only pick up between the end of March and the start of April. -Based on seasonal patterns, asphalt inventory will only drawdown in 2H 2022. Without support from a pick-up in demand, asphalt prices face pressure. -However, there is production costs support for asphalt; even when crude oil prices eased to $90/bbl, the market continues to buy at a low for asphalt. Some traders are looking at CNY 3,600 spot prices. CNY 4,000 is the lid for spot prices. Trading Recommendations: High inventory will limit spot price upside, fluctuating between CNY 3,200 and CNY 4,000. Futures prices to be at CNY 100 to CNY 200 premium.	SHFE Asphalt	3,693	3,601	3,473	3,006
Chemical							
Polyester	Neutral to Positive	-Due to the Omicron spread, China's weaving enterprises have reduced their utilization, affecting polyester's operations. -Demand is expected to be healthy in Q2 2022, driven by overseas demand and domestic summer clothing orders. -Post-China's containment, downstream industries restocking demand will be supported as orders have improved (though below last year). -High production costs will limit the downside for polyester and short yarn. Trading Recommendations: 1. Buy at a low as demand will recover after the COVID-19 situation improves. Price support is at CNY 6,700 to CNY 6,900. 2. Short yarn will be affected more than raw materials. Long PTA, Short PF, until polyester stocks declines.	CZCE Polyester Staple Fiber	7,742	7,594	7,407	7,367

Commodity Development and Market Outlook: Chemicals

Commodity	Near-Term Outlook	Market Overview and Trading Recommendations:	Active Futures	Latest	Average Feb-22	Average Jan-22	Average Mar-21
Chemical				CNY			
PTA	Positive	-PX inventory to decline as 2.66Mt of capacity is expected to suspend production. The utilization rate has been easing to 73%. This forms support to PTA. -More PTA facilities are going on maintenance in March and April, further improving the PTA balance sheet. High crude oil prices are also supportive of PTA. -PTA production profits based on active futures are making profits, based on $940 naphtha and $1,173 PX. PTA production costs are $5,940. -MEG production is making losses based on futures prices and should rise to improve profits. Based on Brent $108/bbl (naphtha $949), thermal coal CNY 826, MEG production costs are at CNY 5,850. Futures production is making a loss of CNY 600. Utilization may be affected in the coming weeks with one facility already suspended. -Furthermore, in Q2 2022, there will be a seasonal MEG facilities upgrade, which will lead to a fall in operating rates. Trading Recommendations: 1.Long TA05. Risk: Fall in crude oil prices and downstream orders. 2. Long MEG at a low due to expected supply fall: A facility has suspended production + increased maintenance in Q2.	CZCE TA	6,026	5,612	5,300	4,501
MEG	Positive		DCE EG	5,311	5,156	5,261	5,313
PVC	Neutral to Negative	-In the next one to two weeks, the market will continue to trade on the Omicron impact on downstream demand and decline in production costs -Last week's PVC apparent consumption and exports eased as China tightens measures to contain the virus. Shenzhen, Jilin, Shandong factories have closed, affecting raw materials demand. Construction works and logistics were also affected. -Overseas' demand will ease seasonally, with May being the traditional lull season, and FOB prices will decline. -China's PVC operating rate increased to 81%, with little maintenance scheduled in March and April. There will be 700Ktpa of capacity restarting production in April. If prices remain above CNY 9,000 due to bullish macroeconomics expectations and crude oil prices, but production costs eased due to coal prices, then there will be supply excess pressure for PVC Trading Recommendation: Prices to hover close to CNY 8,500 to CNY 9,200.	DCE PVC	9,074	8,802	8,619	8,687
Methanol	Positive to Neutral	-Methanol prices will fluctuate with production costs (crude oil and coal) as its fundamentals are weak. -Meanwhile, due to the Omicron spread in China, the seasonal pick-up of downstream demand and logistics may be delayed. -Ex-factory methanol price support is at CNY 2,200. There is a high possibility that factories will try to sell quickly due to the rising logistics costs (omicron disruptions), causing downstream restocking interest to weaken. -April and May maintenance will lead to methanol supply reduction. However, before Omicron gets contained, the price rise may not sustain without demand support. Trading Recommendations: Prices will fluctuate with production costs. After the virus gets contained in China, there may be support from demand.	CZCE Methanol	3,020	2,799	2,705	2,447
Polyolefin	Positive	-More facilities suspended production last week. Inventory has built up a little due to the omicron containment impact on downstream demand. -Even as downstream demand is not strong, post-containment, April demand will improve WoW, with a fall in supplies to provide support. -Unless inventory drawdown remains slow in April, suggesting downstream consumption weakness, there is price upside in March and April. -In April, PP and PE prices should recover on the back of 1) high production costs, 2) low production willingness due to weak margins, 3) Demand to recover, and 4) Low imports. Trading Recommendations: 1. Buy PP and PE after prices ease due to COVID-19 related fall in demand. Based on >$95/Bbl crude oil prices, PP and PE price floor is estimated at CNY 8,500 and CNY 8,700, respectively. Risk: 1) Fall in production costs and 2) weak consumption.	DCE PP	8,870	8,528	8,408	9,172
			DCE PE	8,941	8,984	8,838	8,764
Benzene and Styrene	Positive	-High crude oil prices have led to a fall in ethane crackers' utilization rate. Benzene output has declined. PX utilization rate has also fallen by -4% WoW to 74%. Hydrogenation of benzene, which has been relying on drawing down crude benzene inventory, will not be able to sustain the current operating rate, -Styrene production profits have been weak as new capacity added over the last two years weighs on supplies. The soft profits suggest that styrene operating rates will remain low. -High styrene production costs and low operating rates limit the room for styrene prices to correct. Trading Recommendation: Styrene should hover at CNY 9,300-9,800/t. Wait for an opportunity to buy when the COVID-19 situation improves.	DCE Styrene	9,699	9,096	8,622	8,632

China’s Energy Sector News Highlights

- **China coal importing companies and Russian coal exporters have expressed interest in working together.** However, there are still some details to work out, such as payments using CIPS in place of SWIFT, logistic bottlenecks, coal quality, etc. China coal imports from March to April are expected to decline YoY based on shipment data. High Indonesian coal export prices reduce China’s import interest. – *Source: CCTD, 17th March 2022.*
- **China’s January to February raw coal production rose by 10.3% YoY to 690Mt.** March’s coal transportation via rail remained high, with Daqing railway transporting 1.3Mt/day of coal. China’s average daily coal production will rise towards 12.6Mt/day. The end of winter heating season will loosen domestic coal supply conditions. – *Source: CCTD, 16th March 2022.*
- China’s NDRC told officials from major mining regions at a meeting that it wants to **boost domestic production capacity by about 300Mt. It also plans to build a 620Mt stockpile** of fuel split between government, miners, and users. The production increase would be split, with 150Mt of capacity coming from new, upgraded operations and another 150Mt from open-pit mines and some mines that had previously been shutdown. The daily output should average 12.6Mt/day. **The added 300Mt of capacity is equivalent to China’s typical annual imports.** The nation produced over 4Bt of coal last year. – *Source: Bloomberg, 14th March 2022.*

Table 1: China Thermal Coal Supply and Consumption Indicators

		Latest	MoM	YoY	Remarks
China Thermal Coal Price					
18/Mar	Qinhuangdao Thermal Coal, Shanxi Origin, CNY/t	940	-6%	42%	
Six Major Power Plants' Consumption and Inventory					
14/Mar	Average Daily Thermal Coal Consumption, Mt/Day	0.7	-7%	-2%	
14/Mar	Thermal Coal Inventory, Mt	11.5	-3%	-23%	
China Thermal Coal Delivery and Supply					
17/Mar	Daqin Railway 7D Cumulative Coal Delivery, Mt	8.8	16.0%	7%	*From Northern domestic coal mines*
18/Mar	Northern Ports 7D Cumulative Throughput, Mt	11.8	4.1%	-14%	*Mostly for delivery to the South*
11/Mar	China 55 Ports Inventory, Mt	37.6	-1.6%	-36%	*Downstream domestic and imported supplies*
15/Mar	25 Provinces Inventory, Mt	86.9	-10%	16%	*Downstream inventory*

Chart 1: China 7DMA Daqin Railway Domestic Coal Delivery, Mt/Day

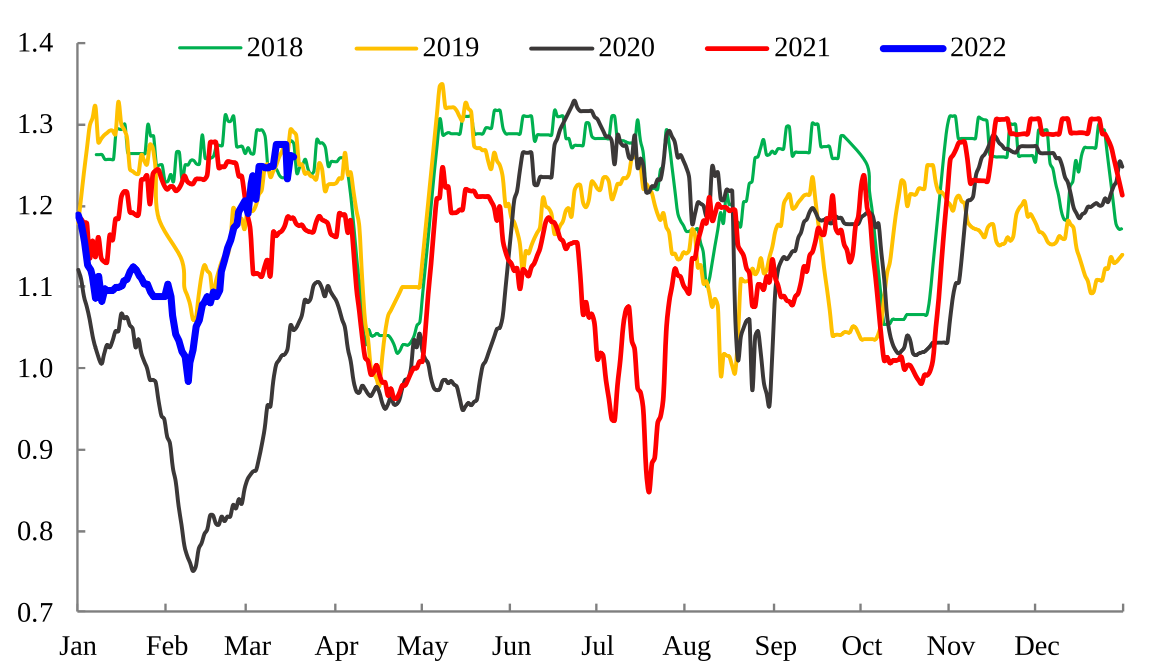


Chart 2: Number of Cars Unloading Thermal Coal at Qinhuangdao and Caofeidian

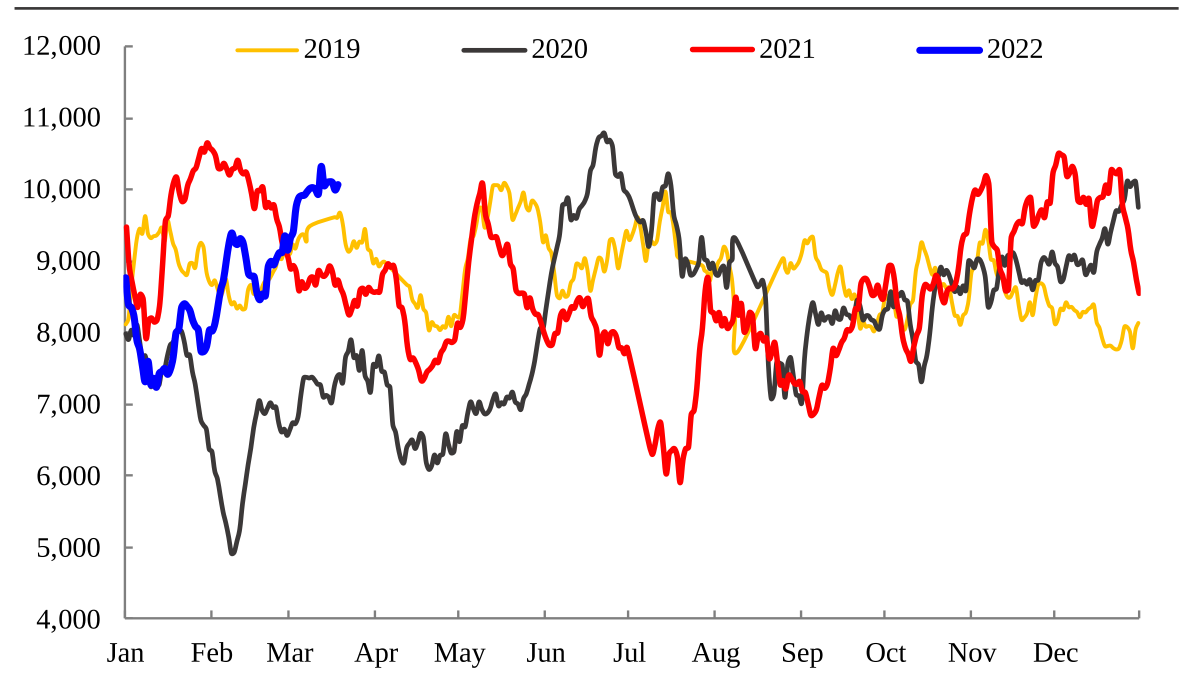


Chart 3: 25 Provinces Number of Days of Thermal Coal Inventory

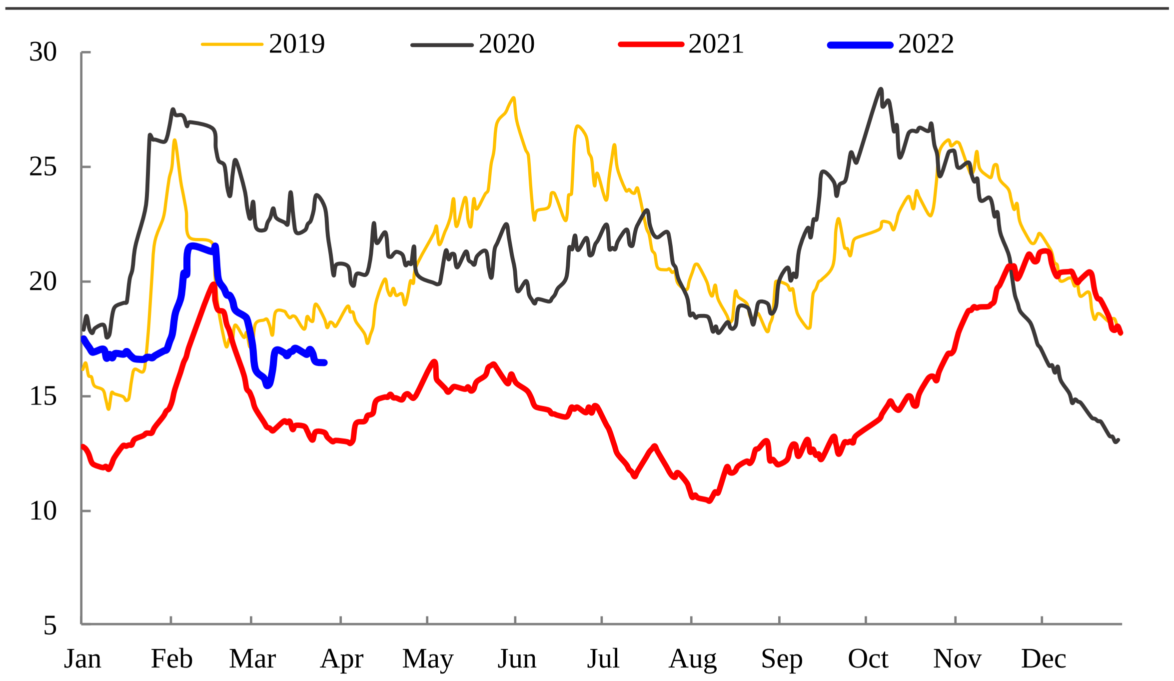
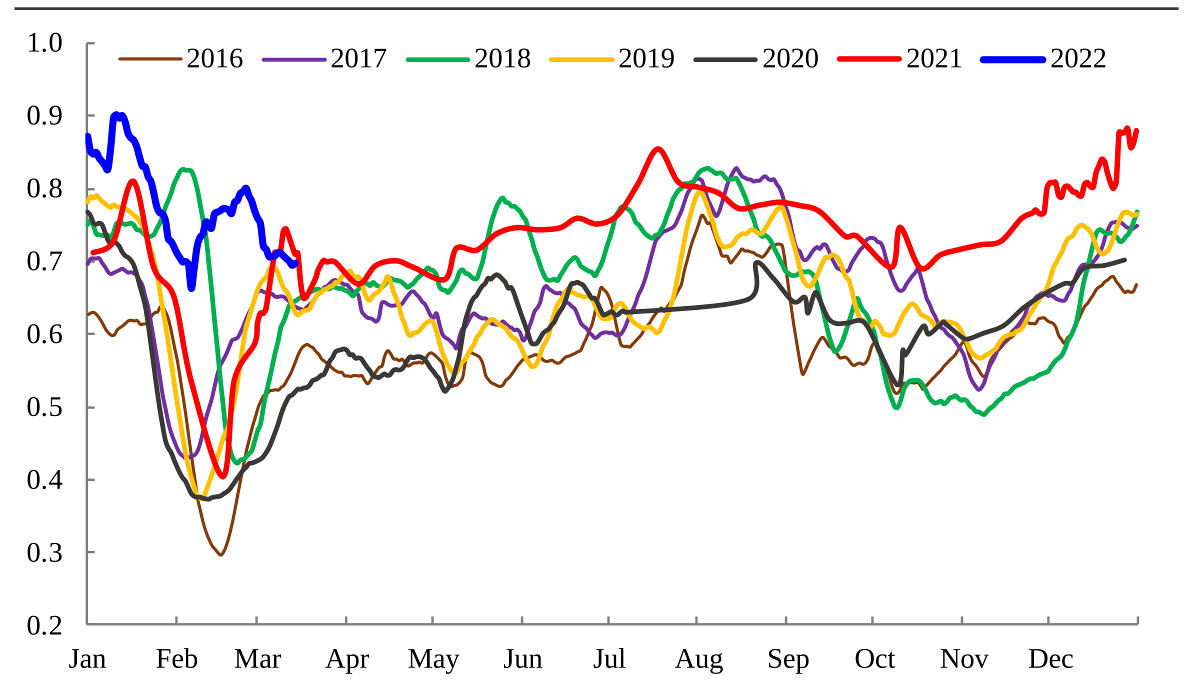


Chart 4: China Six Major Power Plants' Daily Thermal Coal Consumption, Mt



Financial assets' prices include a premium for the war that will be obliterated once there is a ceasefire.

- China's COVID-19 outbreak, and the Russia and Ukraine war are two events that have driven recent market prices. China's economy is bound to be affected in the short term due to its zero-COVID policy in which commodities prices are pricing into the potential fall in demand during the Q2 peak consumption season. However, like the post-COVID period in 2020, this demand will be made up for after the situation improves. At the same time, to stabilize economic growth, there will be stronger policy support.
- On the other hand, the prices of upstream commodities such as energy and agricultural products have included a 'premium' for possible supply disruptions due to the war and sanctions. Therefore, prices will fluctuate according to the war's development and sanctions. Supposing there is a ceasefire, commodities including crude oil could return to the pre-war period's $90/bbl.

Chart 5: Potential sanctions on Russian energy products have sent U.S. Expected Inflation up to 3%.

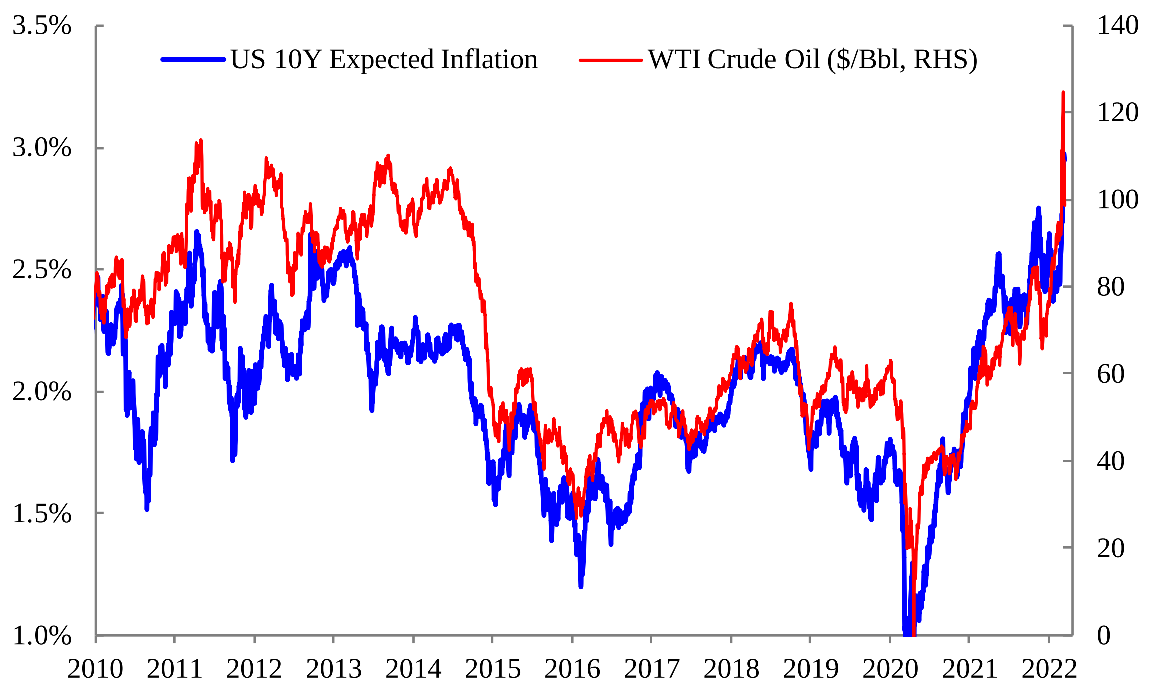
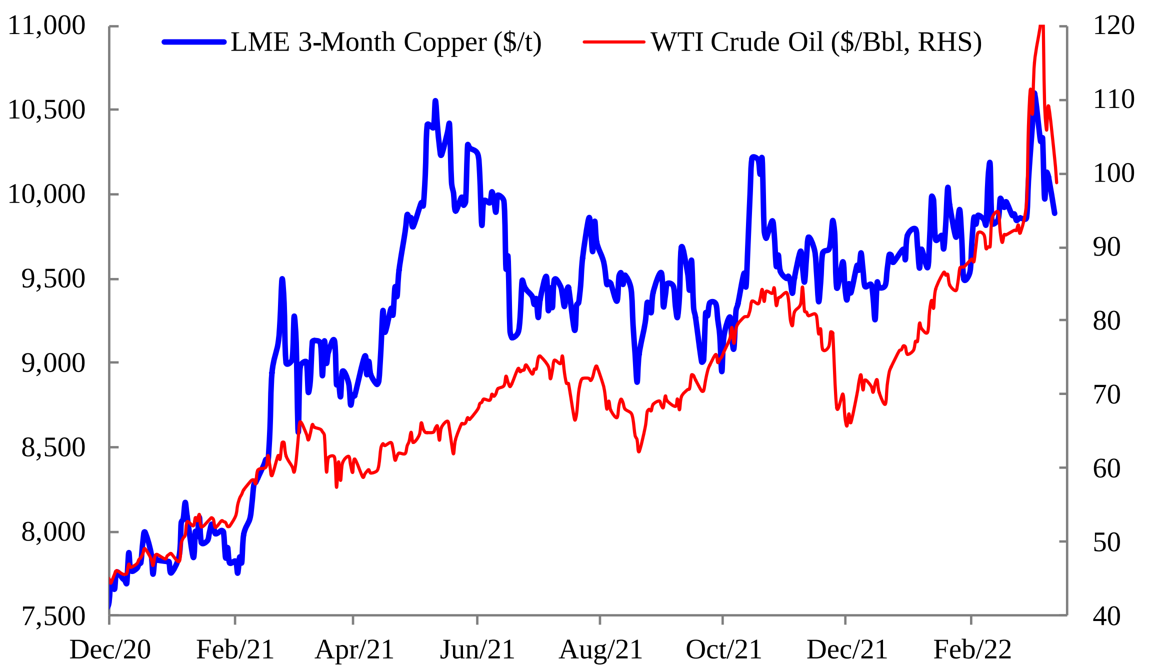


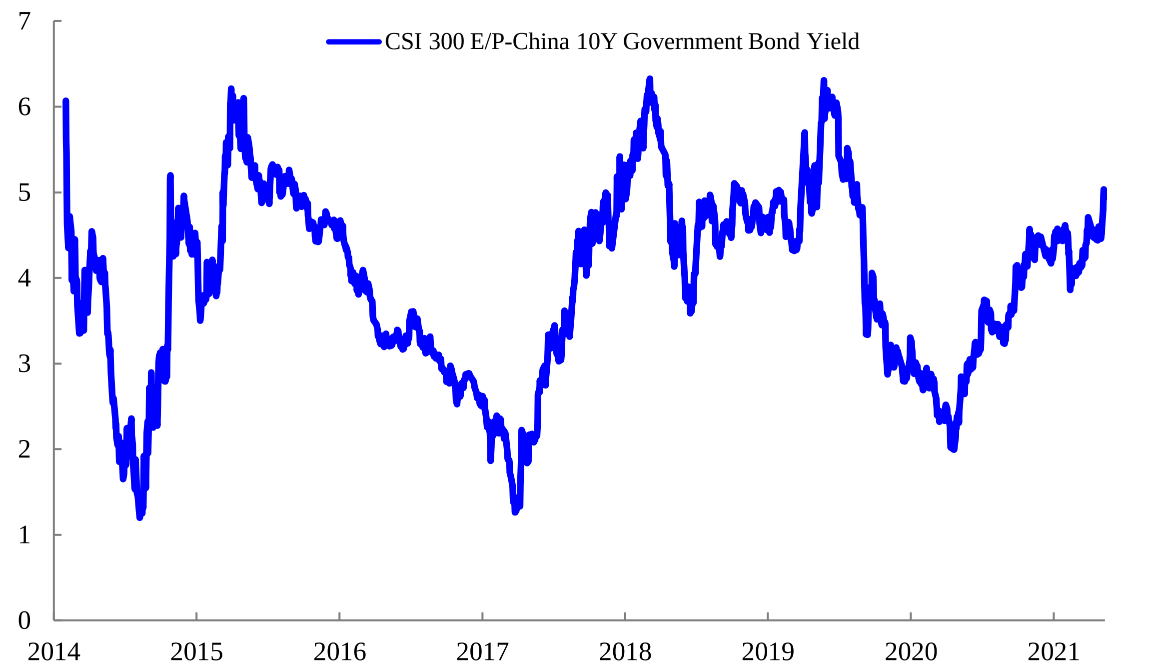
Chart 6: High Expected Inflation which prices in the possibility of supply disruptions have also driven up industrial metals' prices.



Investment interest will improve after prices ease to a level that increases the likelihood of good returns.

- With high volatility and uncertainties, investors may only invest when the prices of a particular asset are at an attractive point. For instance, for the CSI 300, its returns are still not attractive based on the Fed Model, a market-timing tool for determining whether the stock market is fairly valued by netting returns with long-term government bond yields.
- The relative returns of CSI 300 are still some distance away from the high seen in March 2020's COVID-19, January 2019, and January 2016 (Chart 7). We estimate that the CSI 300 will need to retreat to the lower-bound of CNY 4,000 to improve the odds of increased investment.

Chart 7: CSI 300 may need to retreat to the lower bound of CNY 4,000 to improve its investibility odds.



In February, China's social financing contracted with households' credit demand at its weakest.

- China's February social financing retreated more than -80% MoM and YoY to CNY 1.19 trillion, with household loans the weakest amongst all components. Household medium to long-term loans comprising mortgages had plunged by -CNY 46 billion, the lowest since 2007 when the data was first reported.
- The current credit cycle may turn out like 2014's; due to the regulators' unwillingness to relax the real estate sector at the early stage of loosening, credit growth has been stable and not expanded. The regulators may then loosen the real estate industry curbs only when the economic pressure becomes immense.
- Policies have restricted the lending of financial institutions' willingness to provide loans, while other banks with room to issue loans are wary of the underlying credit risks. There is a concentration of foreign debt maturing in 1H 2022 within the real estate sector, and it remains to be seen if developers will run into repayment problems (Chart 9).
- In the near term, China's government bond yields may fluctuate within 20bps to 30bps as the real estate sector and domestic consumption recovery both remain slow. High energy costs and overseas demand are providing the primary support for commodities' prices. Policy needs to loosen further to improve economic conditions and for financial institutions to have confidence to provide longer-term loans.

Chart 8: China Newly Issued Household Medium to Long-Term Loans, Billion CNY

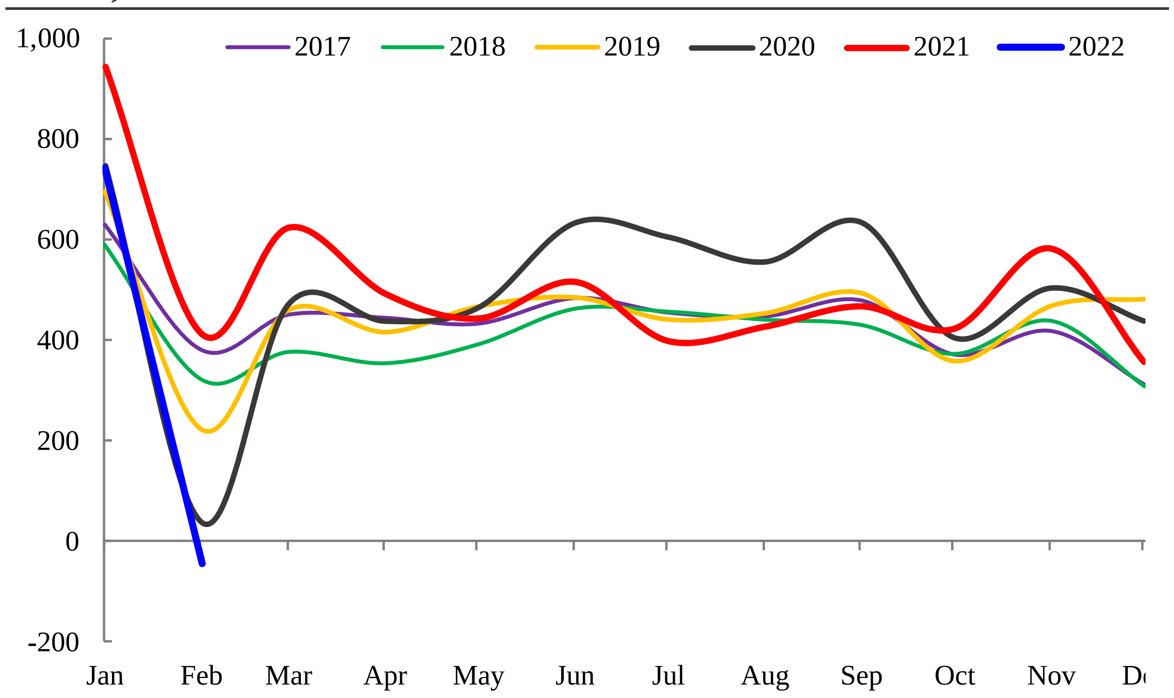
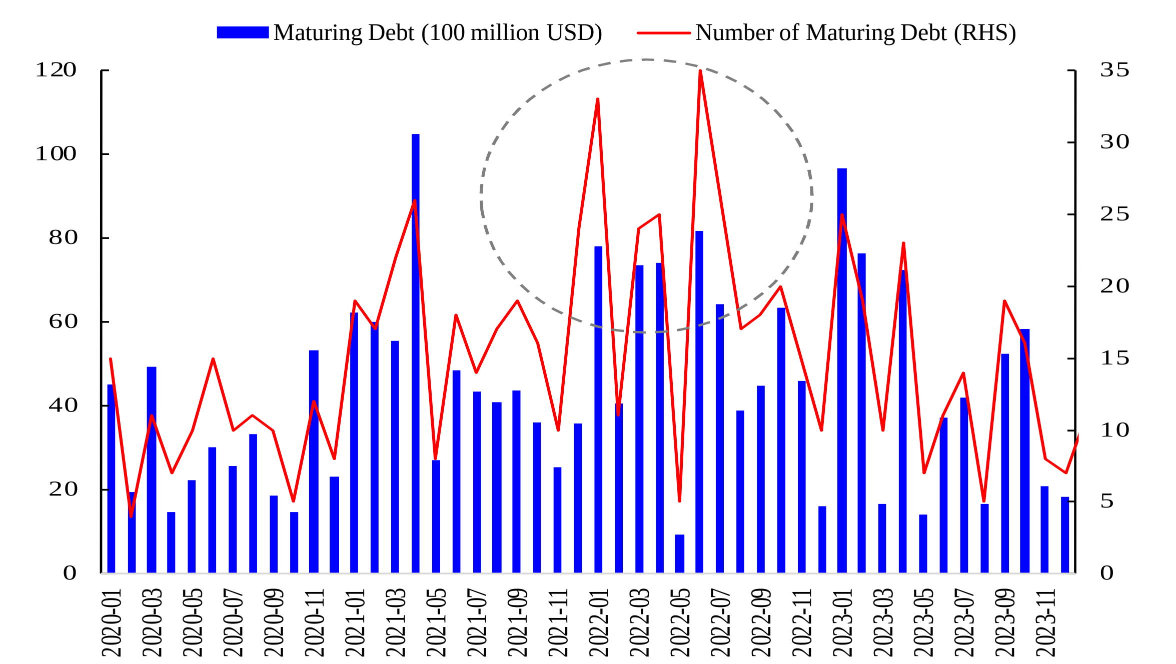


Chart 9: China Real Estate Sector Foreign Debt will be maturing in 1H 2022.



China's housing sales improvements could suggest better sales in the lower-tier cities.

- The contraction in China's floor space of buildings sold narrowed by 6% MoM to -9.6% YoY January and February. The results were better than expected despite a decline in housing sales in the 30 mid to large-sized cities, which is comprised mainly of the first and second-tier cities by -30% YoY and household medium to long-term bank loans by -50% YoY, during the same period (Chart 10). The smaller contraction in official data may imply that either the third and fourth-tier cities have improved quicker, or part of the sales in late-December 2021 was recorded within the period.
- Nevertheless, a sustained recovery in housing sales is required for the real estate industry outlook to improve and more confidence that China is on track to achieve its 5.5% GDP target. Compared to the official data, housing sales in the 30 cities have not shown signs of improvement. The March-to-date sales continued to soften by -50% YoY, which can be attributed to slower loosening of the cities' housing sector controls compared to the lower-tier cities (Chart 11).

Chart 10: Household medium to long-term loans remain in deep contraction compared to housing sales.

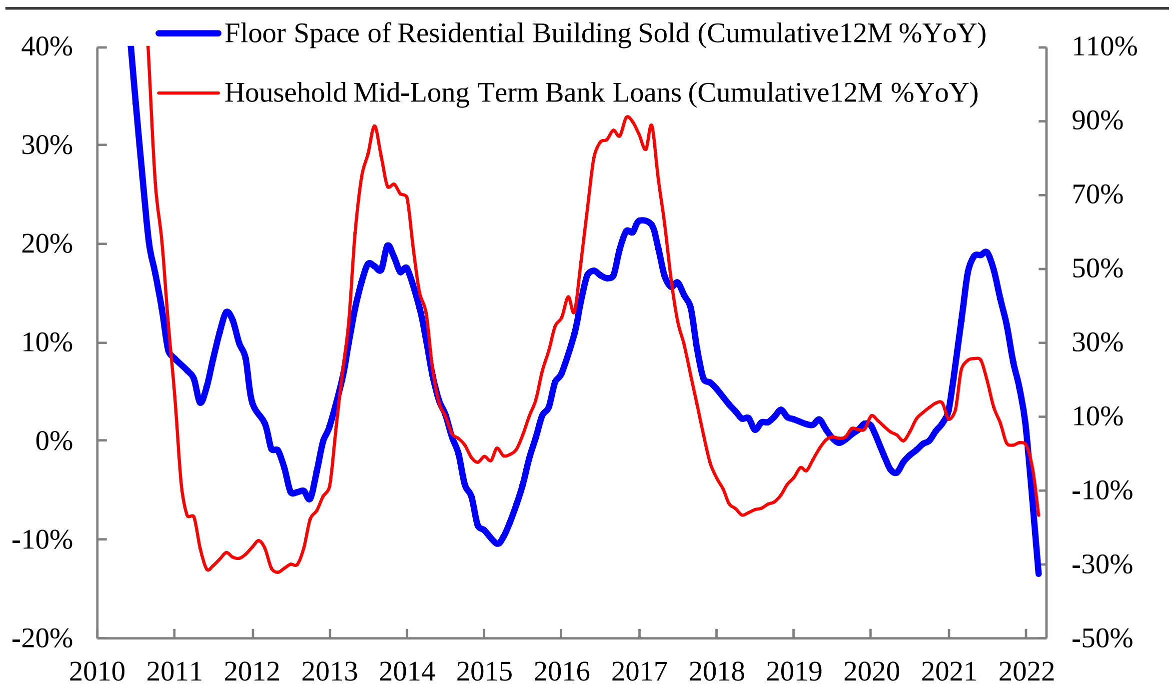
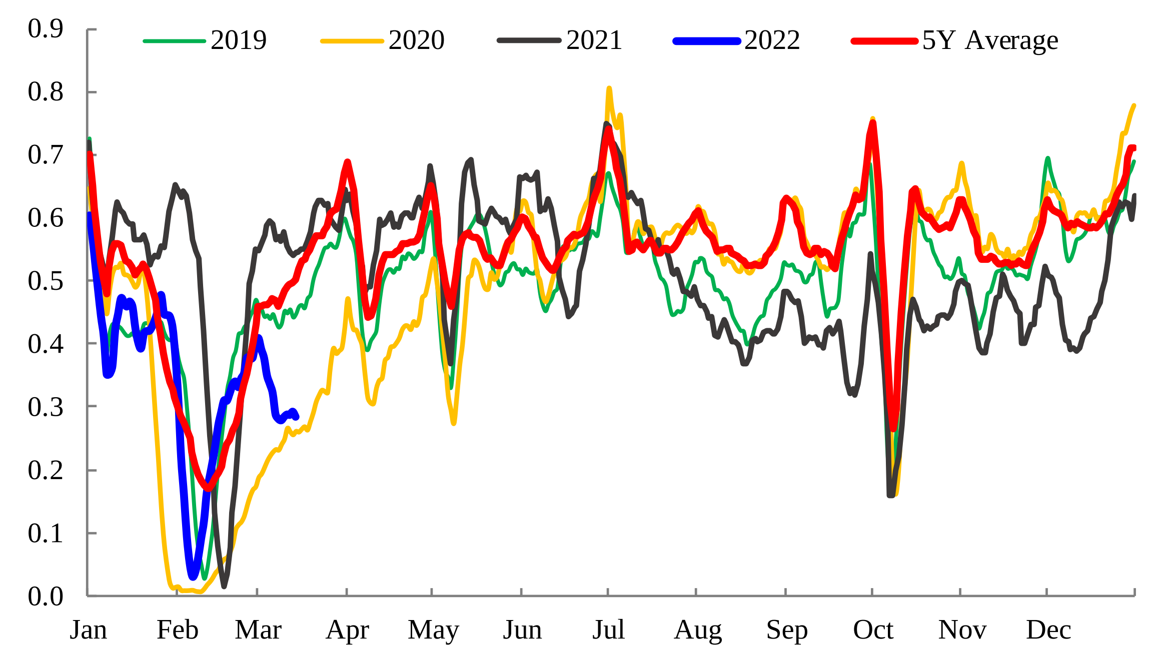


Chart 11: China 30 Mid to Large-Sized Cities Floor Space of Buildings Sold, Million Sqm



A sustained sales recovery and more policy support are needed to drive investments in the sector.

- China's real estate development investment growth also improved to 3.7% YoY from December 2021's low of -14% YoY. However, as sales remain in contraction, developers' cash flows are tight, with investment interest capped. The YTD land transactions have fallen steeply by -38% YoY (Chart 12). At the same time, construction and installation investments have eased as well (Chart 13).
- Supposing the policy support is not sufficient to drive recovery in housing sales and developers' funding, real estate development investments will enter into a deep contraction that has never historically been experienced. Even after excluding land purchases, construction and installation investments will at most record single-digit growth, putting a drag on the Chinese economy.

Chart 12: 100 Medium to Large-Sized Cities Floor Space of Land Transacted, Million Sqm

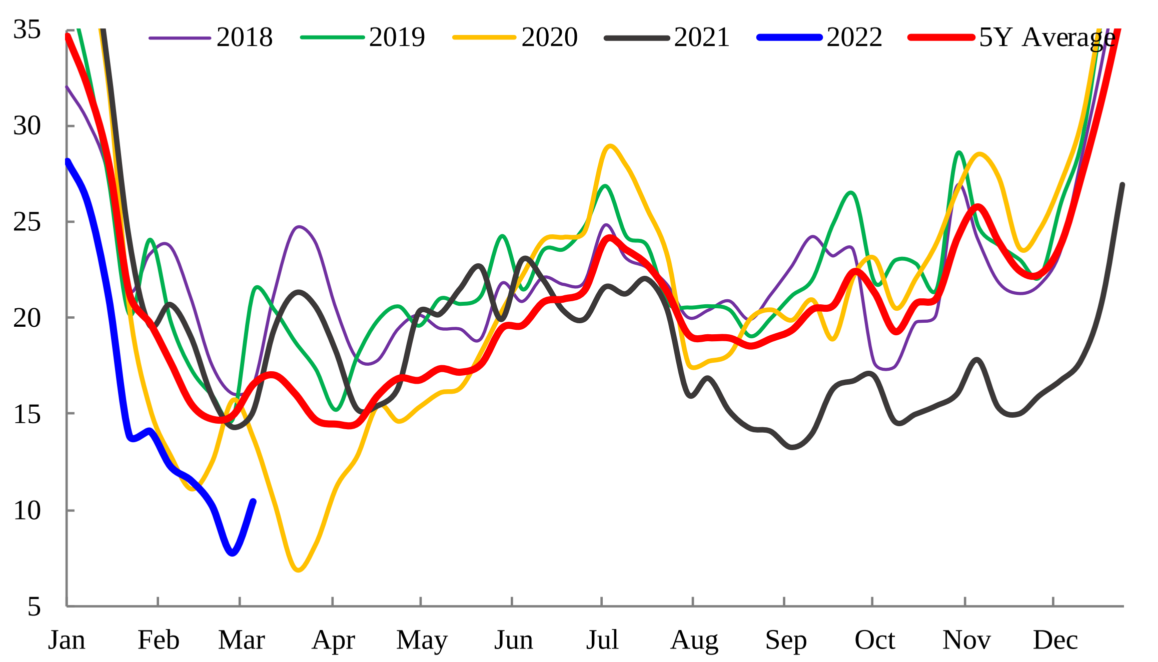


Chart 13: Construction and Installation Investments eased as developers slowed construction pace due to tight cash flows.

There is room for investments to recover given low industry inventory.

- Not considering developers' cash flow problems, China's real estate inventory structure is healthy, with sales outpacing investments after 2016. The ratio has retreated to a historic low, leaving room for investments to expand (Chart 14). At the same time, the real estate inventory pressure has also been stable (Chart 15).
- Therefore, if developers' cash flow improves, there is room for investments to recover. In particular, an increase in floor space moving to the under-construction stage as developers draw down floor space on hand will drive construction and installation investments.

Chart 14: China's housing sales have outpaced investments after 2016 which leaves room for the latter to expand.

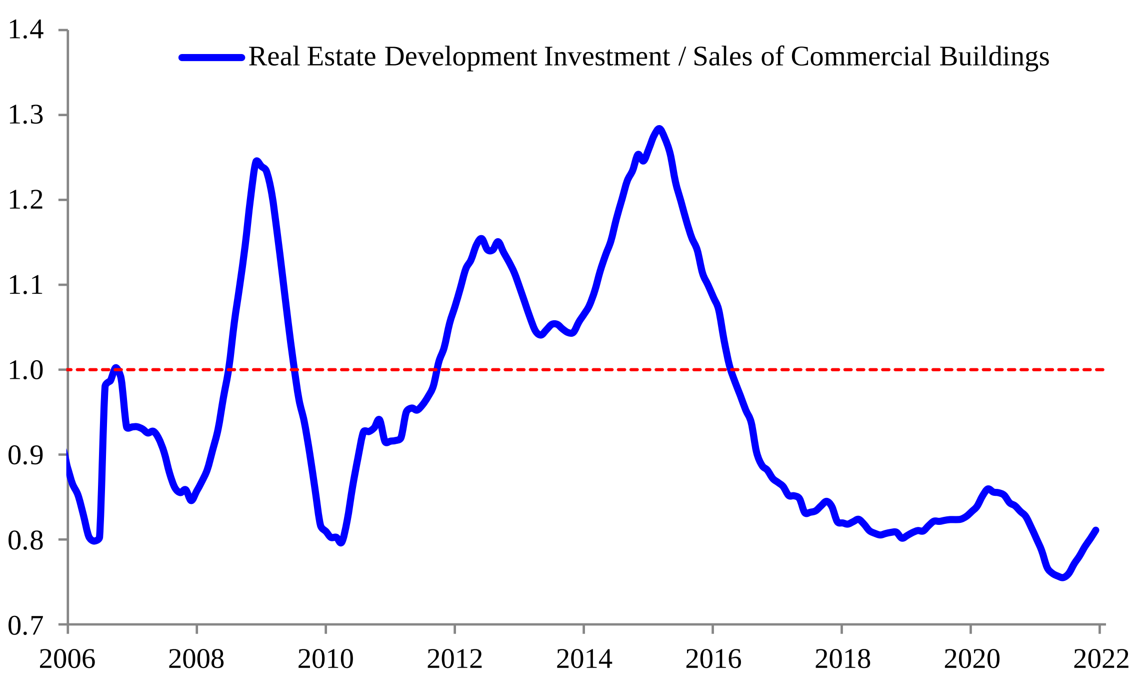
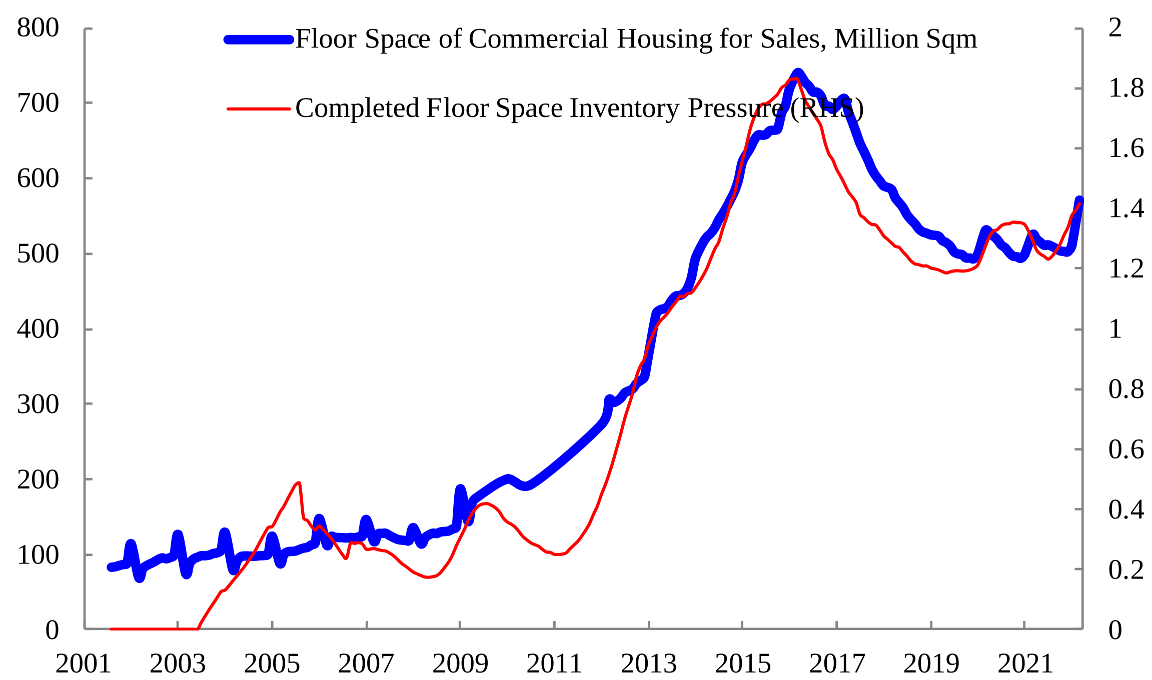


Chart 15: China Completed Floor Space Inventory Pressure is low despite an uptick due to weak sales since 2H 2021.



China may accelerate its policy supports after the Two Sessions.

- The Chinese government may accelerate its policy supports and relaxations after the Two Sessions as the country's economic pressure will expand as time passes (Charts 16 and 17).
- At the same time, we have noticed that compared to first and second-tier cities, the lower-tier cities have loosened their real estate sector quicker by lowering the percentage of initial down payments. On the other hand, first and second-tier cities have lowered their mortgage rates which have a smaller impact than reducing down payments.
- The stronger loosening in the lower-tier cities comes as their land sales are weaker than in first and second-tier cities. Uncertainties in the housing market often weaken investments and consumers' buying interest in lower-tier cities.
- On the other hand, if first and second-tier cities' housing sales remain weak after a decline in mortgage rates, the cities could loosen controls on mortgage quotas, restrictions on loans, and the number of home purchases. Developers' land purchasing demand affects local governments' land-transfer income, which is a critical funding source for infrastructure investments.

Chart 16: The real estate sector has a longer supply chain that affects more sectors' consumption. It is also more effective in driving longer-term loans which are essential for credit expansion.

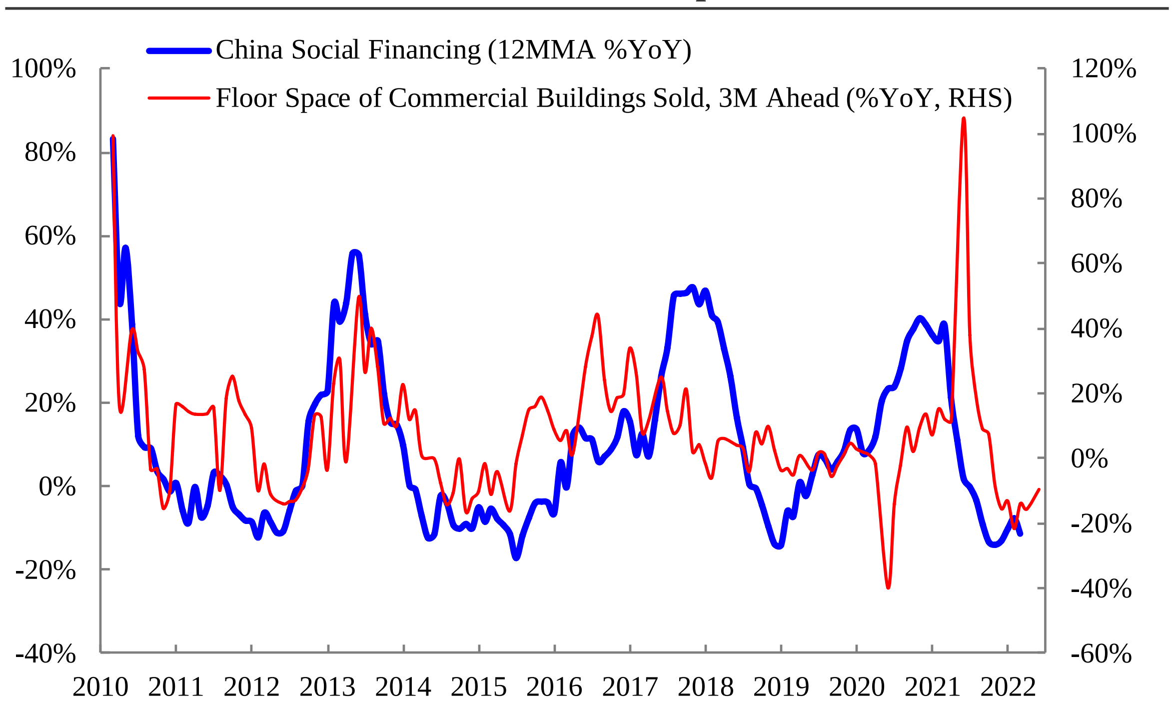
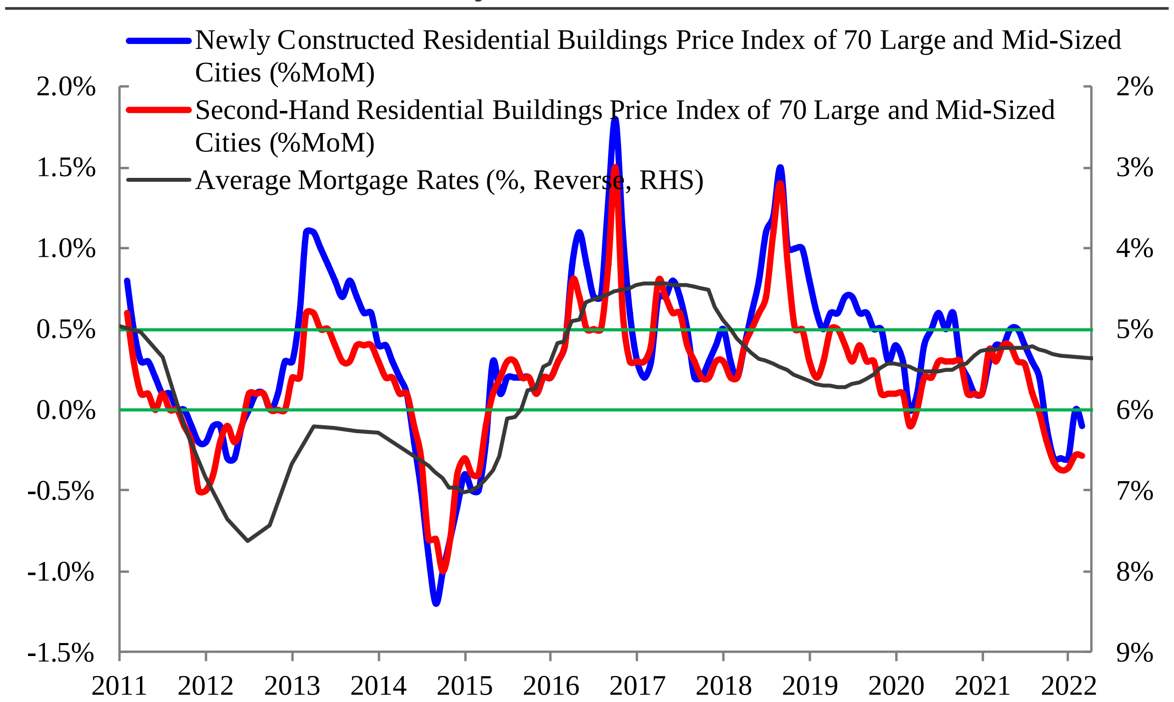


Chart 17: There is room to lower mortgage rates with housing prices maintaining a steady decline despite a brief recovery for newly constructed homes in January.



Sales are bound to improve as long as China is consistent with its efforts.

- As long as the Chinese government continues to loosen its curbs on the sector, housing sales are bound to improve as the current conditions and buying sentiments are not worse off than post-COVID-19.
- Post-COVID-19 in 2020, apart from the high economic uncertainty, a rise in unemployment to 6% has also affected household income. However, after a series of supportive measures to drive the sector, housing sales recovered quickly and even rose to a historic high.
- From past cycles, mortgage rate movements, representing the real estate sector's financial conditions, directly correlate to housing sales (Charts 18 and 19). Therefore, housing sales will improve depending upon when the regulators start to loosen industry restrictions.

Chart 18: China has only cut 5-year LPR by 5bps compared to a total 15bps cut in 2020.

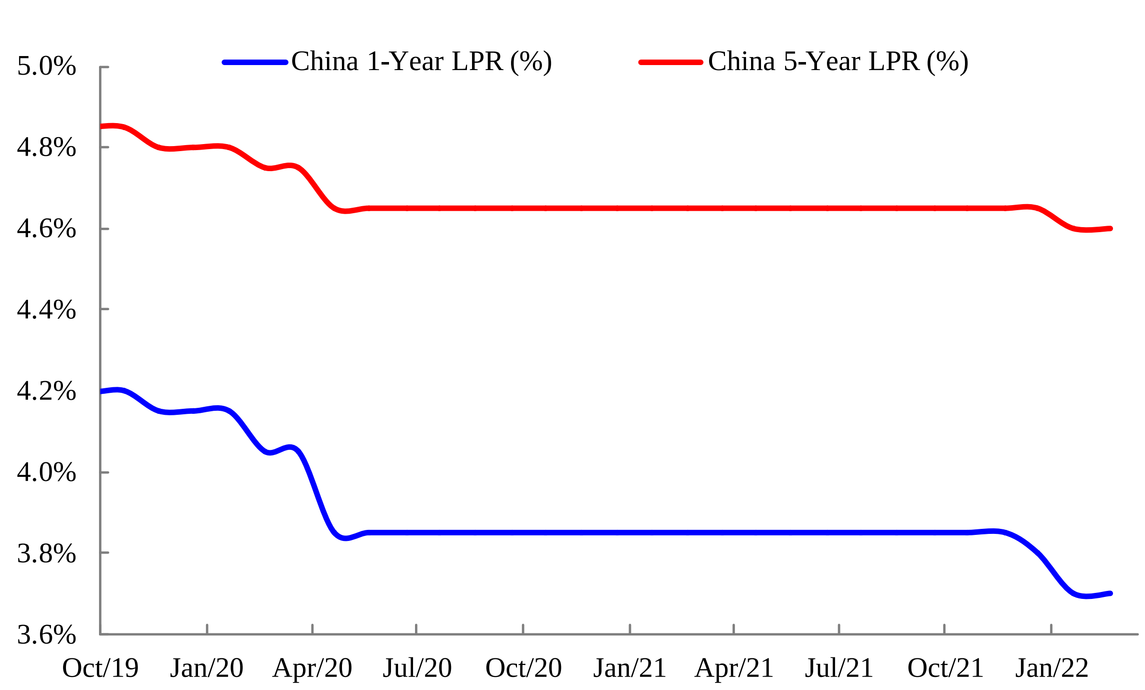
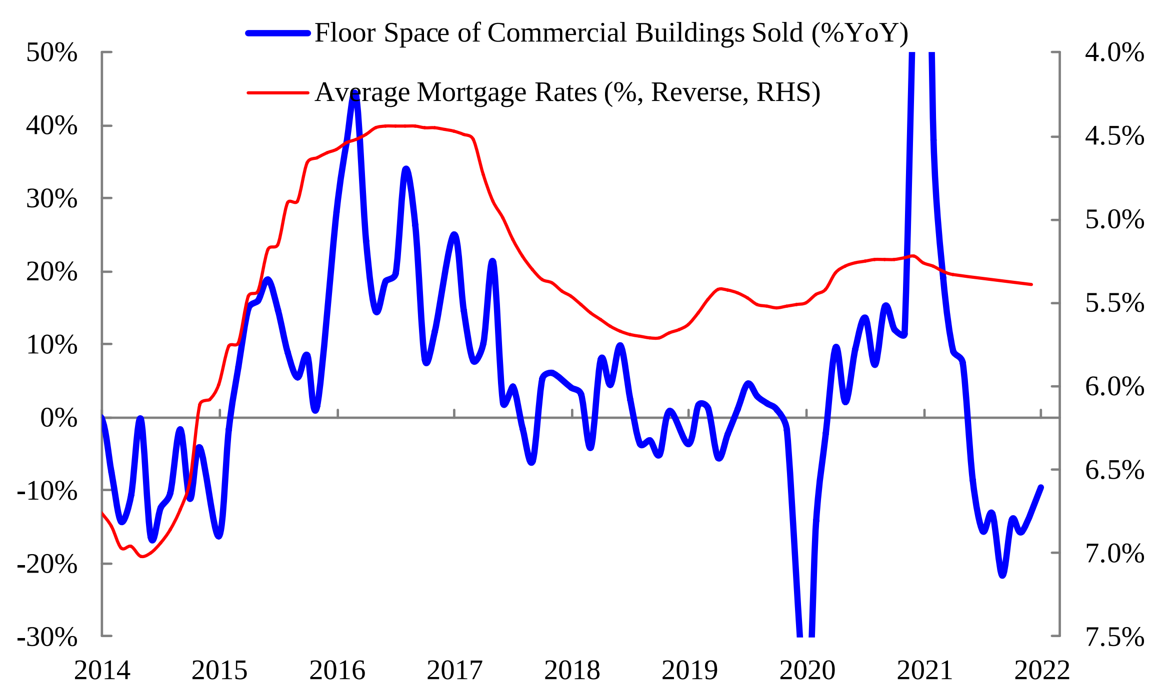


Chart 19: Sales recovery will depend on when China increases its effort to relax controls over the real estate sector.



Land investments will be weak without relaxation in leverage controls. Sales recovery will support under-construction and completed floor space.

- Real estate developers' cash flows will improve following housing sales recovery as it forms more than 50% of their funding sources (Chart 20). An improvement in cash flows will aid in ensuring the continuity of developers' under construction work, supporting floor space completions, and developers' turnover (Chart 21). The increase in under construction and completed floor space will support construction and installation investments in 2H 2022.
- On the other hand, land investments will remain weak if there is no relaxation of leverage controls for banks and developers.

Chart 20: Developers Funding Sources Composite, %: The Three Red Lines policy has increased developers' reliance on sales.

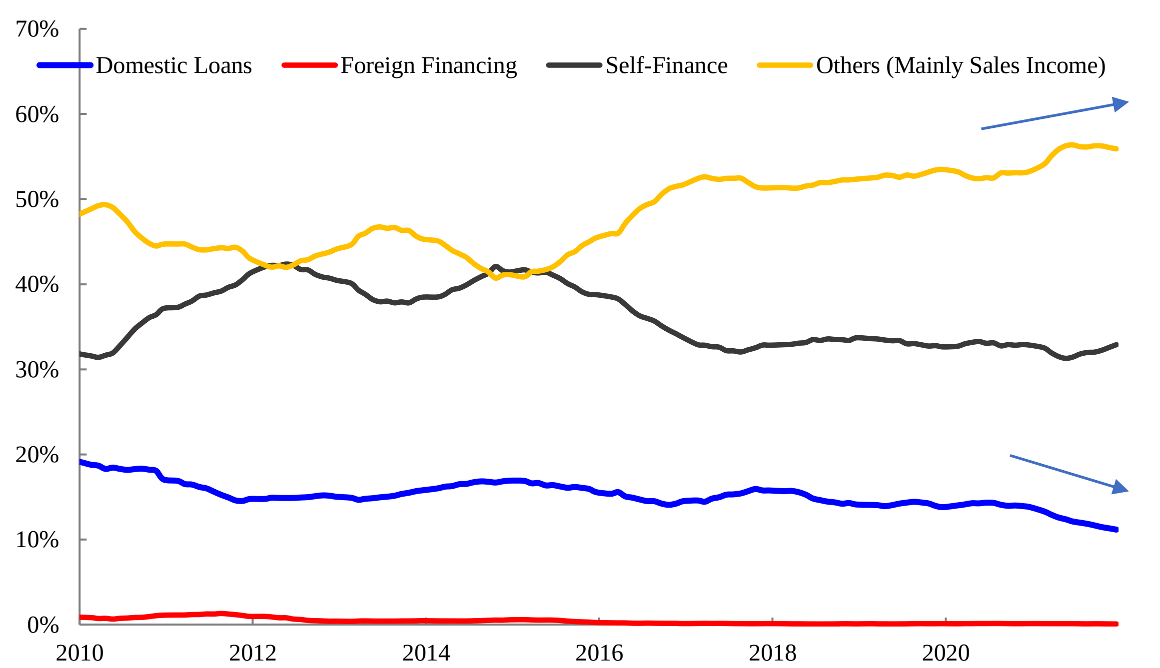
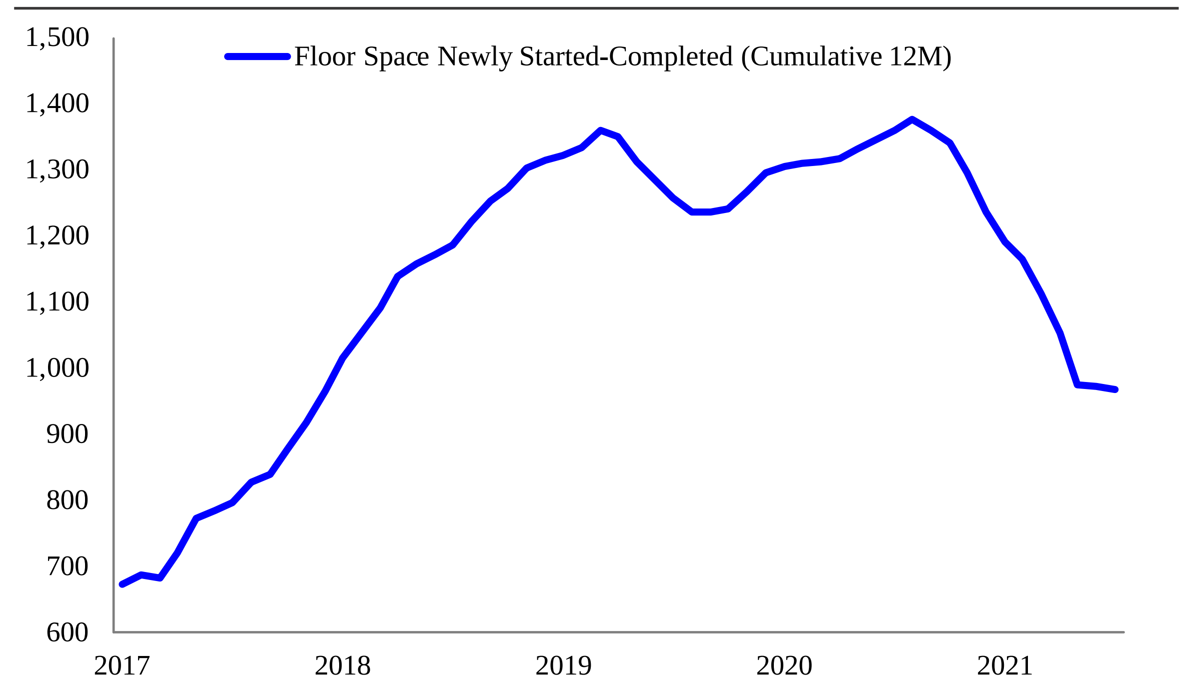


Chart 21: Developers have been working on their floor space inventory to accelerate completions and turnover.



China's real estate sector's construction steel demand will be weak in Q2 2022 before improving in 2H 2022.

- For construction steel demand, even if housing sales recover in April, it will not immediately translate into better real estate sector consumption. At the same time, with land investments capped by the existing leverage controls, newly started floor space, which drives construction steel demand, will continue to ease in 1H 2022. Therefore, there is a high likelihood that the peak consumption season's steel demand in Q2 2022 will be slower than the previous year.
- However, moving into 2H 2022, an increase in floor space under construction and infrastructure buildings will support construction steel demand.

Chart 22: Floor Space of Buildings Newly Started which are driven by land transactions will remain weak in 1H 2022.

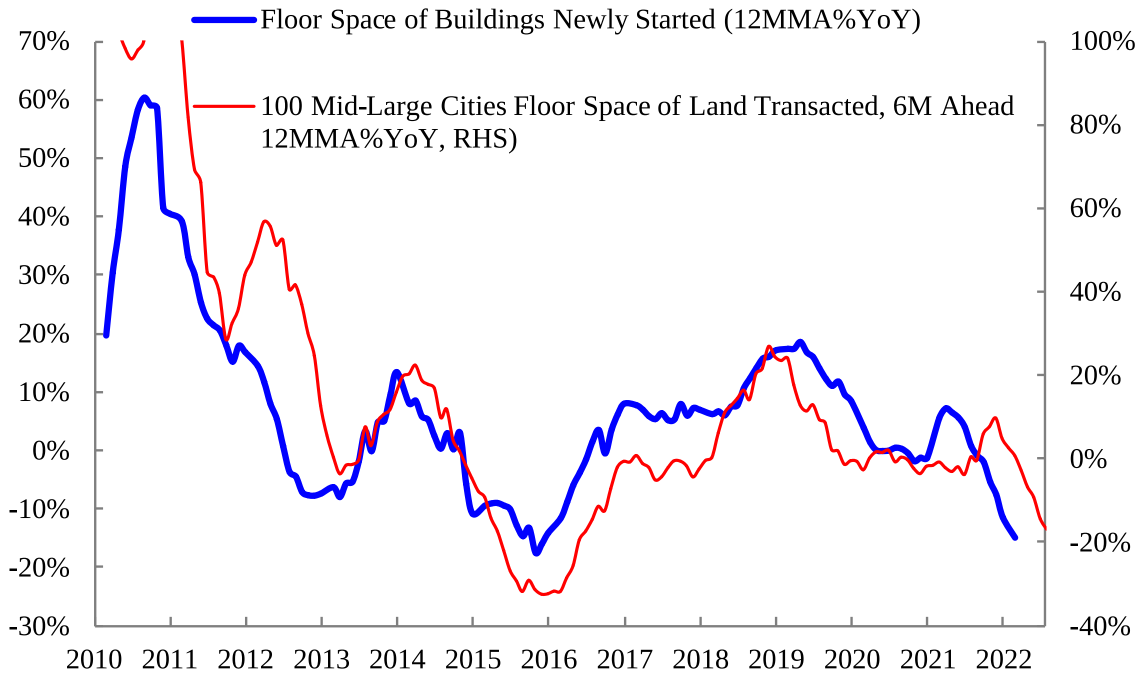
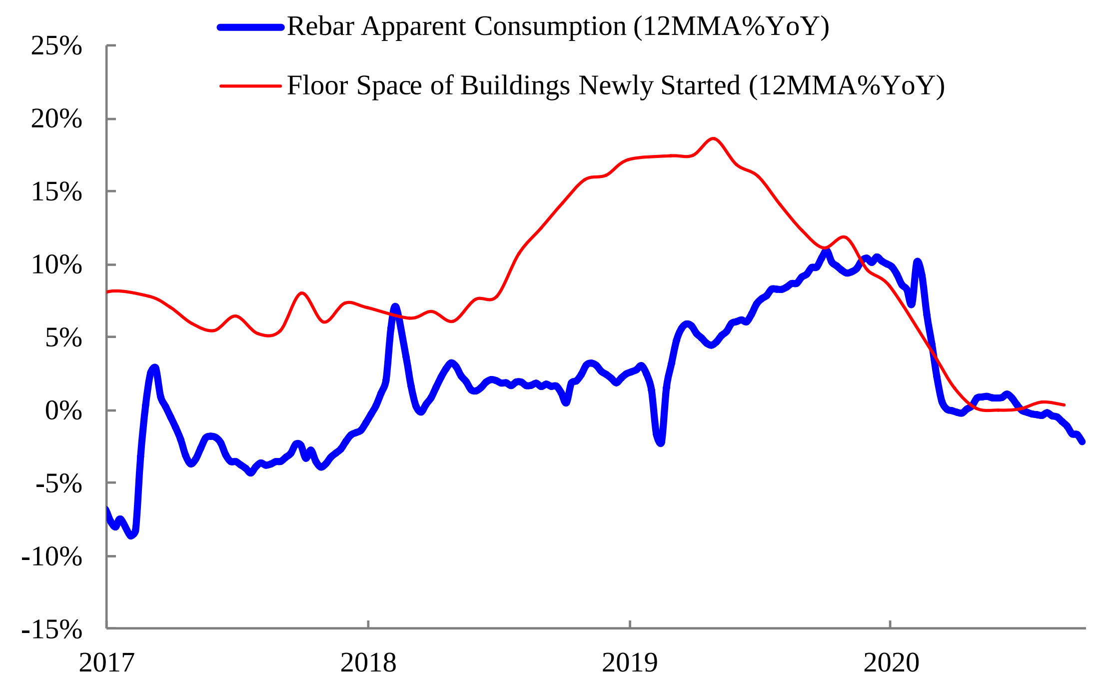


Chart 23: Rebar Consumption may only improve in 2H 2022 after under-construction activities pick-up.



In 1H 2021, flat glass demand and prices were driven by developers' focus on bringing floor space into completion.

- Historically, flat glass active futures tend to strengthen against rebar when the completed floor space growth outpaces newly started floor space (Chart 24). Rebar is used more intensively at the initial stage of construction (newly started), while flat glass is consumed when floor space is nearing completion.
- In 1H 2021, following an increase in under-construction floor space, flat glass demand was lifted, driving the already low inventory down, and spot prices up quickly.
- Many flat glass processors have restarted production following profits recovery and strong demand. However, as the real estate sector weakened in 2H 2021, flat glass and its upstream soda ash demand also softened (Chart 25).

Chart 24: Flat Glass Prices tends to strengthen against rebar when there is an acceleration in floor space being drawdown to completion.

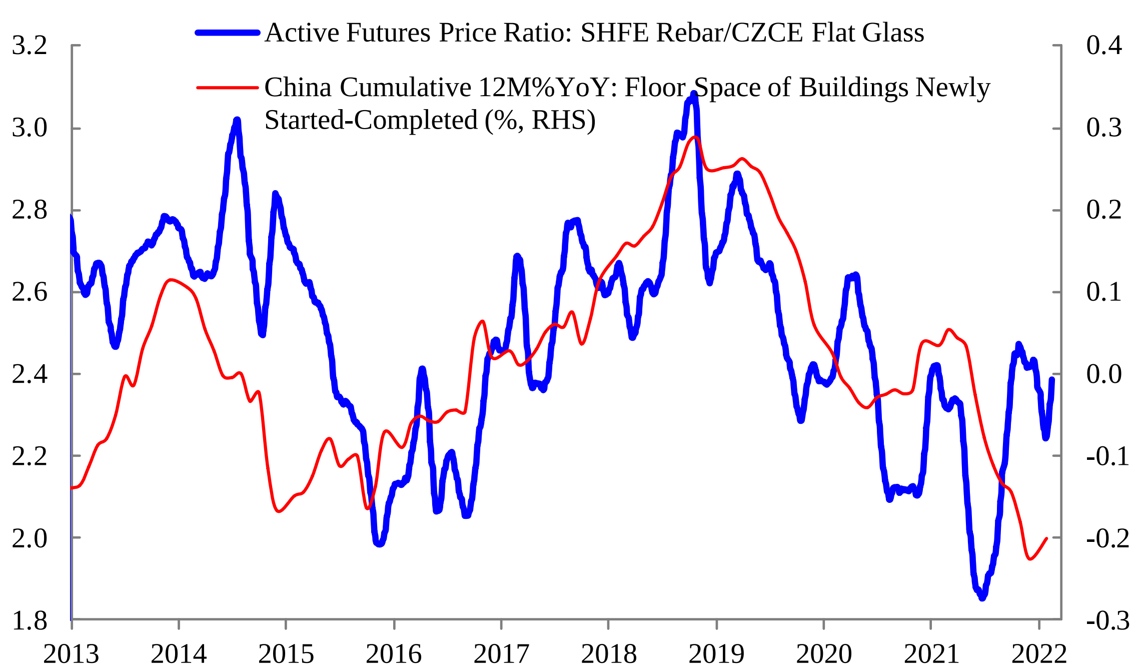
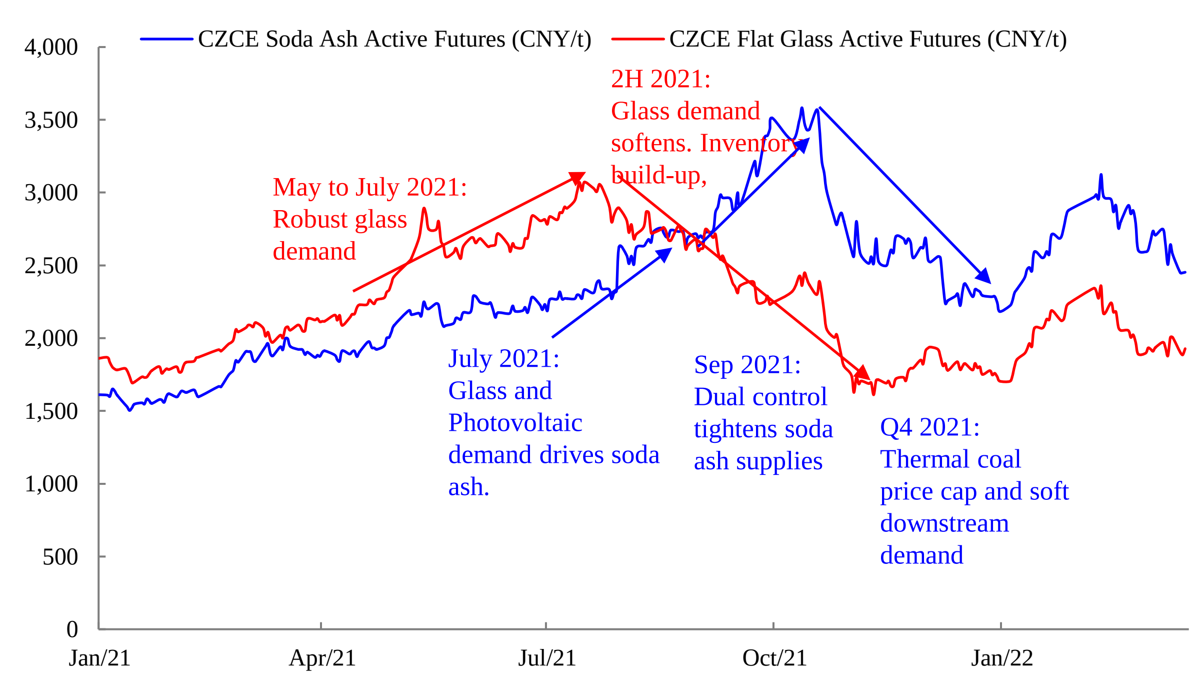


Chart 25: China 2021 Flat Glass and Soda Ash Price Recap: Prices and demand were firm in 1H 2021.



A pick-up in flat glass consumption in Q4 2021 was driven by midstream traders' pre-stocking instead of actual downstream demand.

- In late-Q4 2021, against the weakness in the real estate sector and seasonal patterns, China's apparent flat glass consumption rose by 3% YoY (Charts 26 and 27).

Chart 26: Flat Glass Apparent Consumption rose in late-2021 against the real estate industry's weakness.

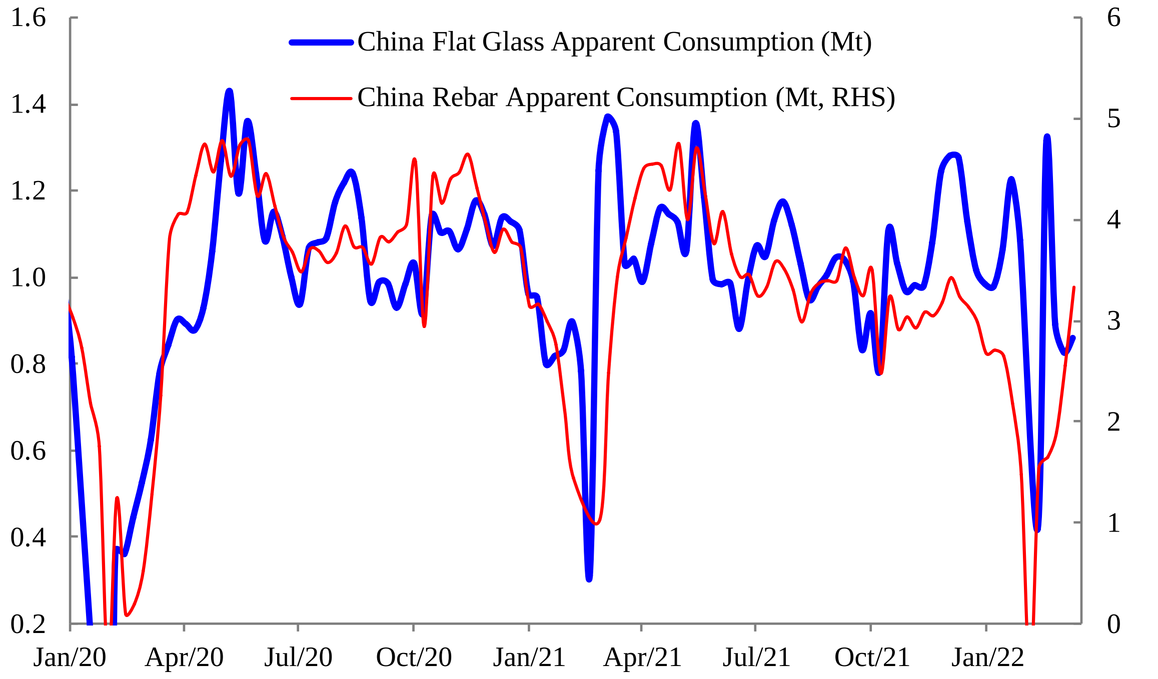
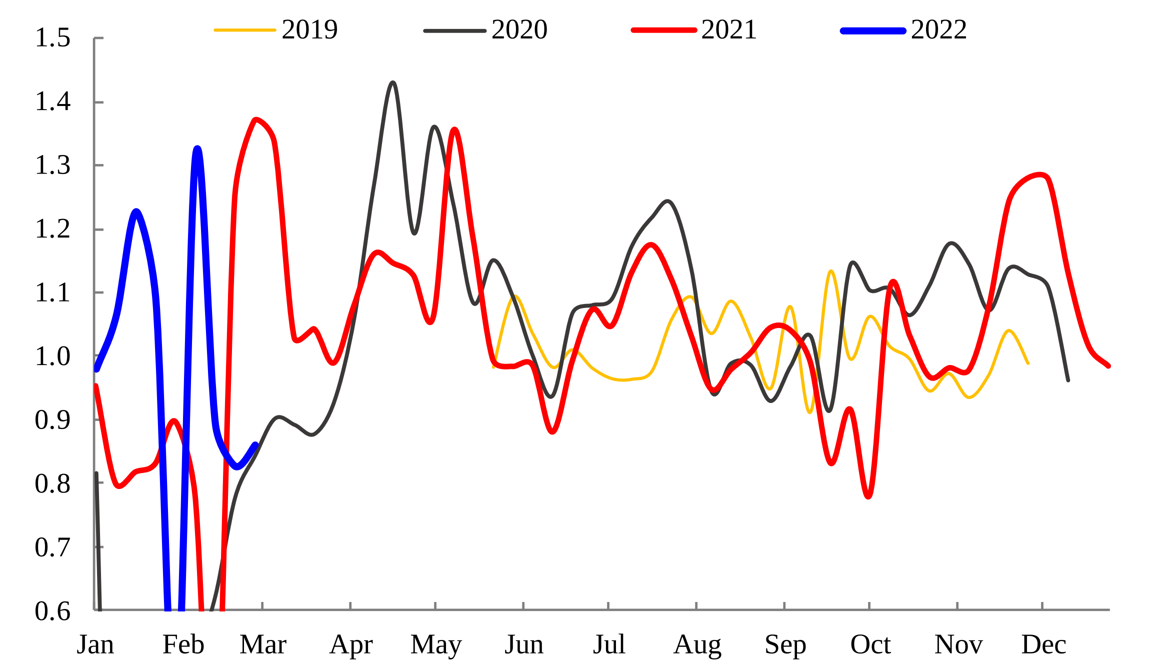


Chart 27: China Flat Glass Apparent Consumption, Mt: Risen by 3% YoY from November to December 2021, against seasonal patterns.



- Traders' pre-stocking demand has driven the increase as after excluding traders' inventory changes, the actual industry's consumption eased, following the seasonal patterns (Chart 28).
- Actual flat glass consumption has been easing since 2H 2021, falling by -4% in late-Q4 2021 (Chart 29). After removing the traders ' inventory changes, China's apparent flat glass consumption closely matches housing sales and factories' orders (Charts 30 and 31).

Chart 28: After removing traders' inventory changes, Flat Glass Apparent Consumption matches the real estate sector's demand.

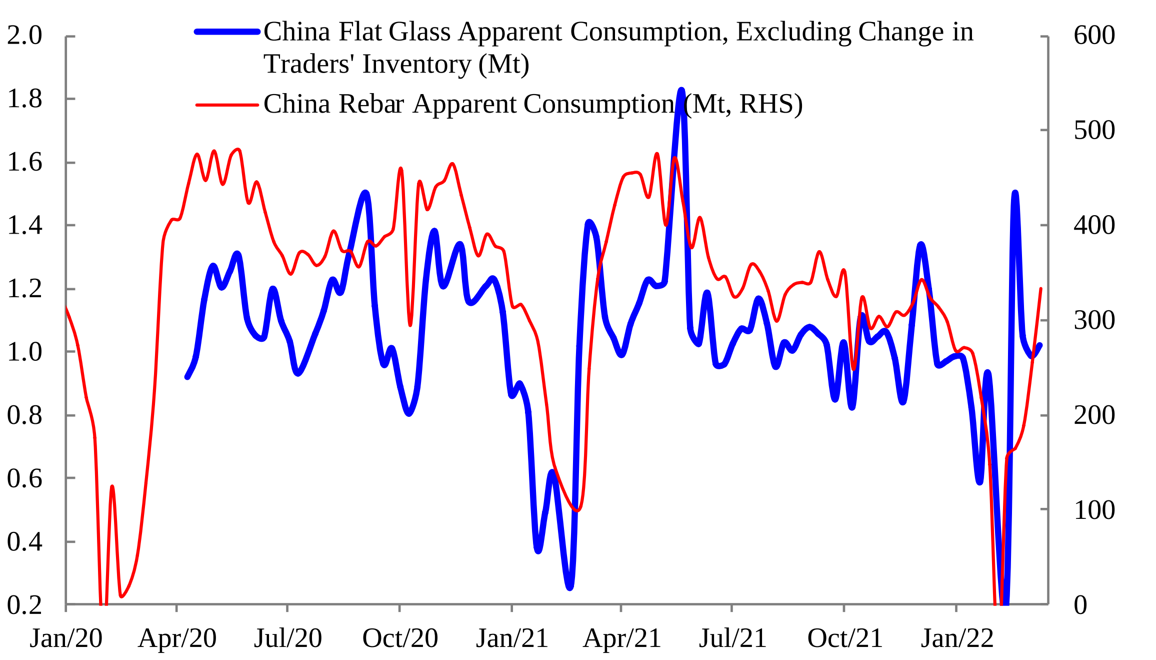


Chart 29: China Flat Glass Apparent Consumption, Excluding Change in Traders' Inventory, Mt: Fell by -4% YoY from Nov-Dec 2021.

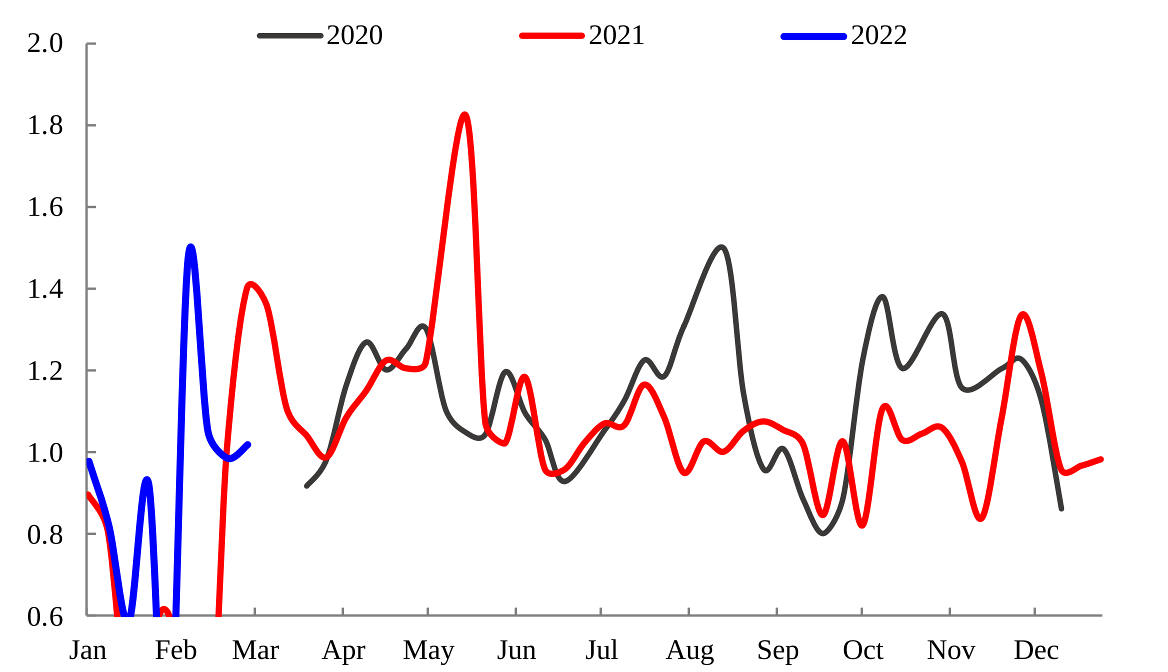


Chart 30: After adjusting for Flat Glass apparent consumption, it matches with industry conditions.

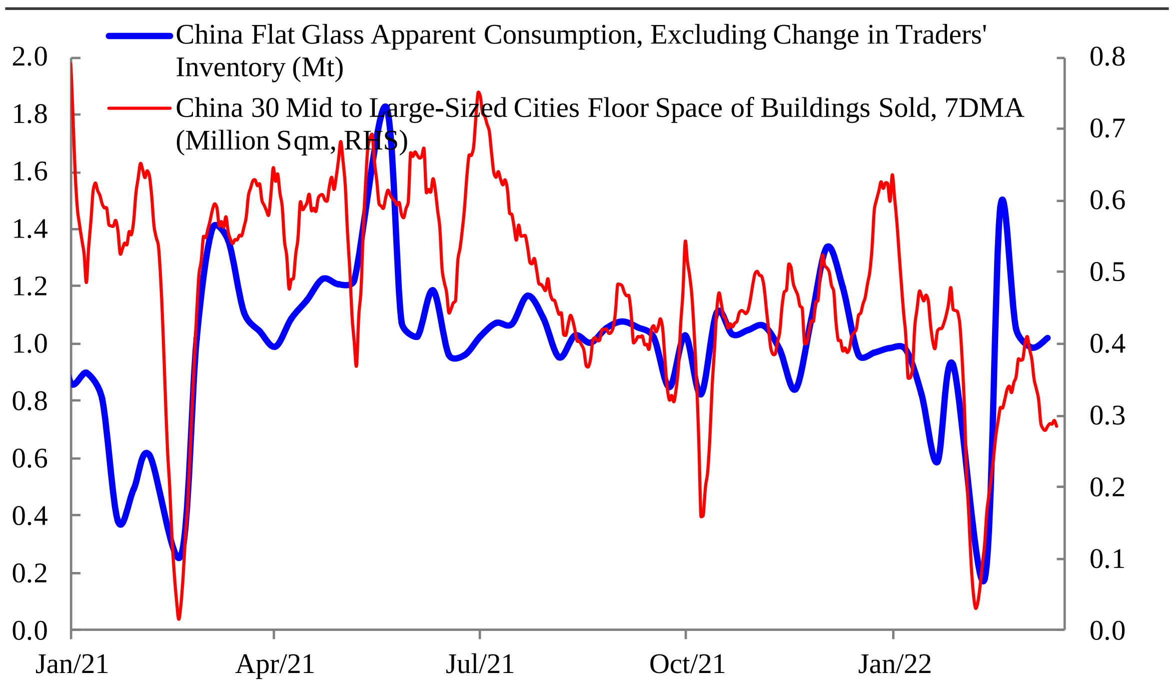
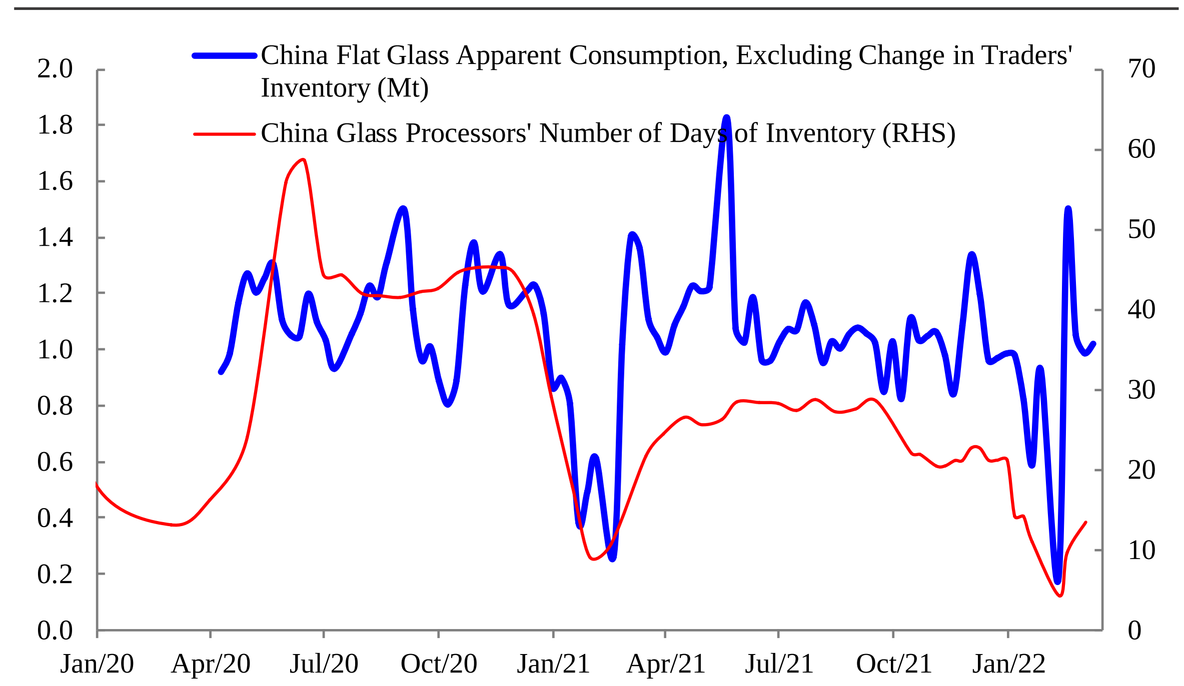


Chart 31: Glass Processors' Orders have been declining quickly since Q4 2021. From 29 days in October to 21 days at end-December 2021.



Flat glass traders’ pre-stocking demand was driven by the rebound in Q4 2021 social financing .

- Due to a rebound in China's October social financing by 16% YoY, spurred by the regulators' orders to accelerate mortgage issuance, flat glass traders' have built up inventory (Chart 32). However, the expansion has slowed down since the start of 2022, falling by -31% YoY in February.
- The rebound in social financing has not led to a recovery in actual downstream consumption. The correlation between social financing and flat glass apparent consumption weakens when we remove changes in traders' inventory from the equation (Chart 33).

Chart 32: Traders’ Q4 2021 pre-stocking was driven by optimism over continuous policy support and social financing expansion.

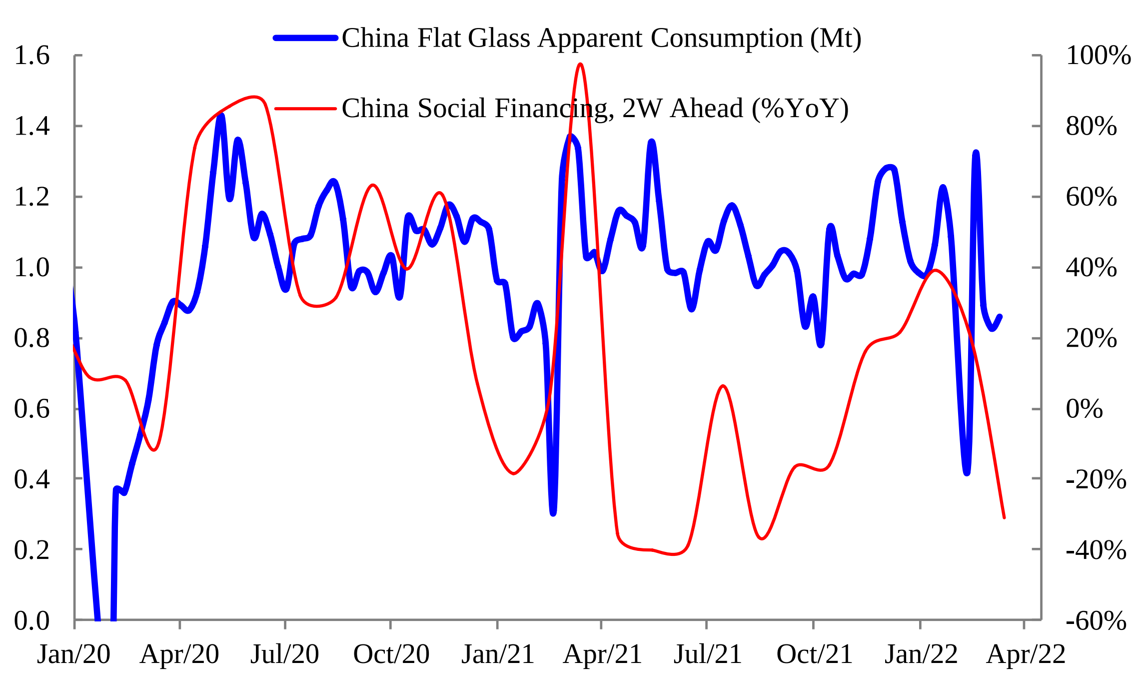
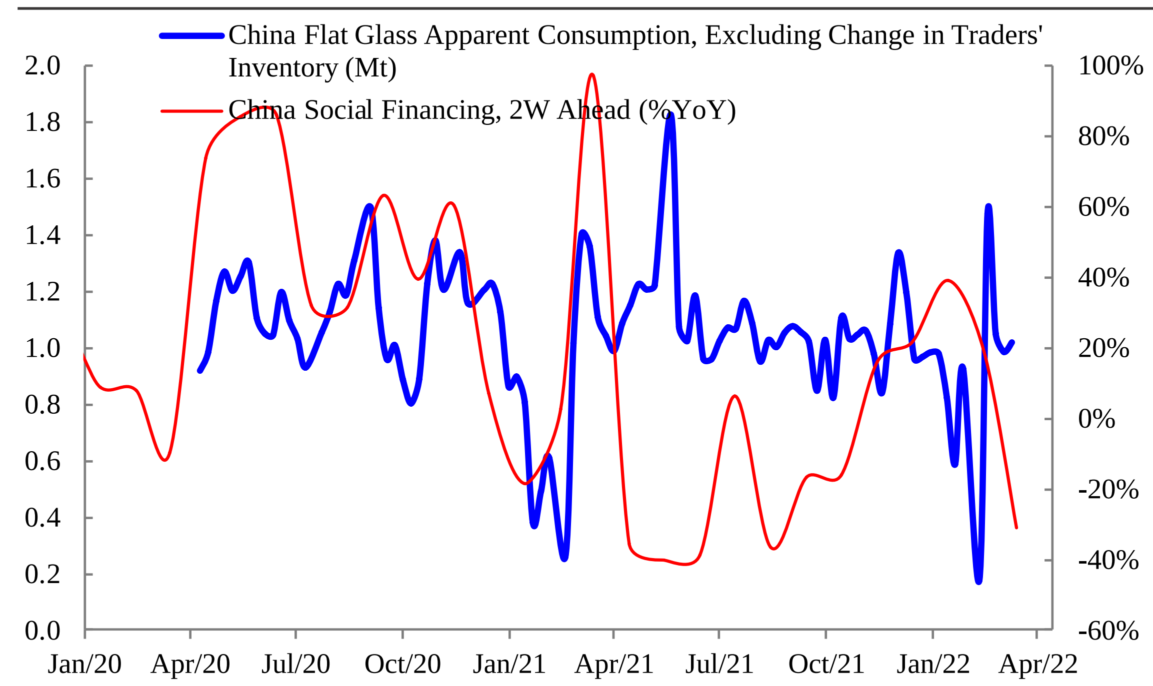


Chart 33: However, the rebound in social financing did not improve actual flat glass consumption.



Flat glass production and consumption rise before floor space gets completed.

- The real estate sector accounts for 80% of flat glass demand, while the automobile industry accounts for the remaining share. Historically, an increase in the construction of newly started floor space will lead to the same for completed floor space in three years and vice versa. This suggests that in 1H 2022, the floor space of real estate completed is looking at an average of more than 10% YoY growth per month (Chart 34).
- There is a misconception that flat glass demand will be robust with an expected increase in completed floor space this year.
- If we look at the correlation between flat glass production and completed floor space, flat glass production increases eight months before the floor space gets completed (Chart 35). The reasons behind that are 1) Door and window glass installations are completed long before the floor space is ready for delivery. 2) Real estate developers’ report of their completed floor space comes after consumption. From industry feedback, glass is often consumed more than 6-months before the floor space gets completed.
- Flat glass production is driven by downstream demand, production profits, and inventory changes. Therefore, actual glass consumption precedes floor space of real estate completed by more than eight months.

Chart 34: China’s floor space completion looks to record more than 10% growth, supported by an elevation of new starts in recent years.

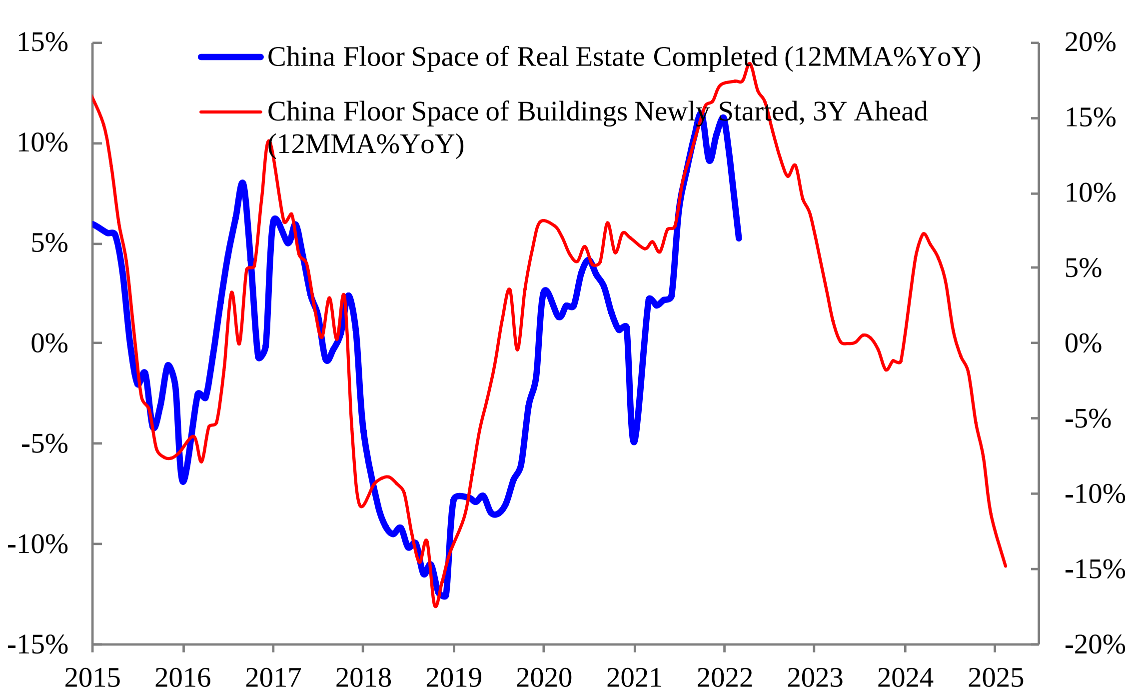
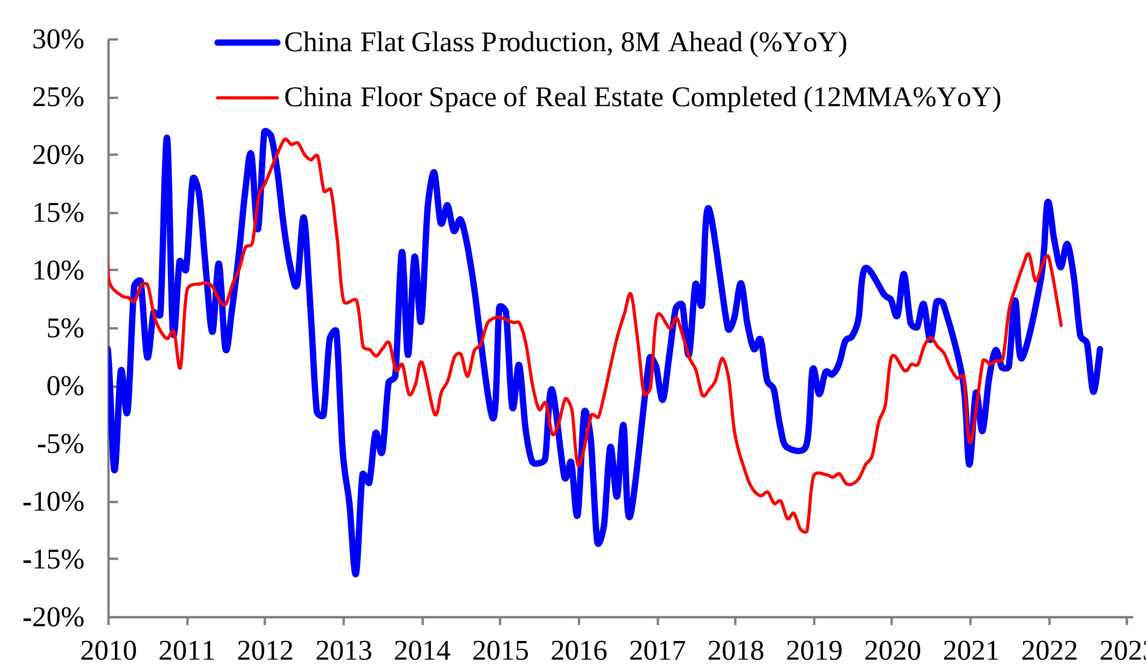


Chart 35: However, flat glass production, which increases after demand, picks up before a rise in completions.



If newly started floor space precedes glass consumption by 28 months, demand will grow by 5% YoY in 2022.

- If we replace completed floor space with newly started floor space, it provides a 28-month leading indication for flat glass production and demand. Under this relationship, China's 2022 flat glass demand could increase by 5% YoY under the bullish scenario
- Similar to the real estate sector, 2H 2022 consumption may be better than 1H 2022.

Chart 36: Compared to completed floor space, Changes in Newly Started Floor Space precedes glass production.

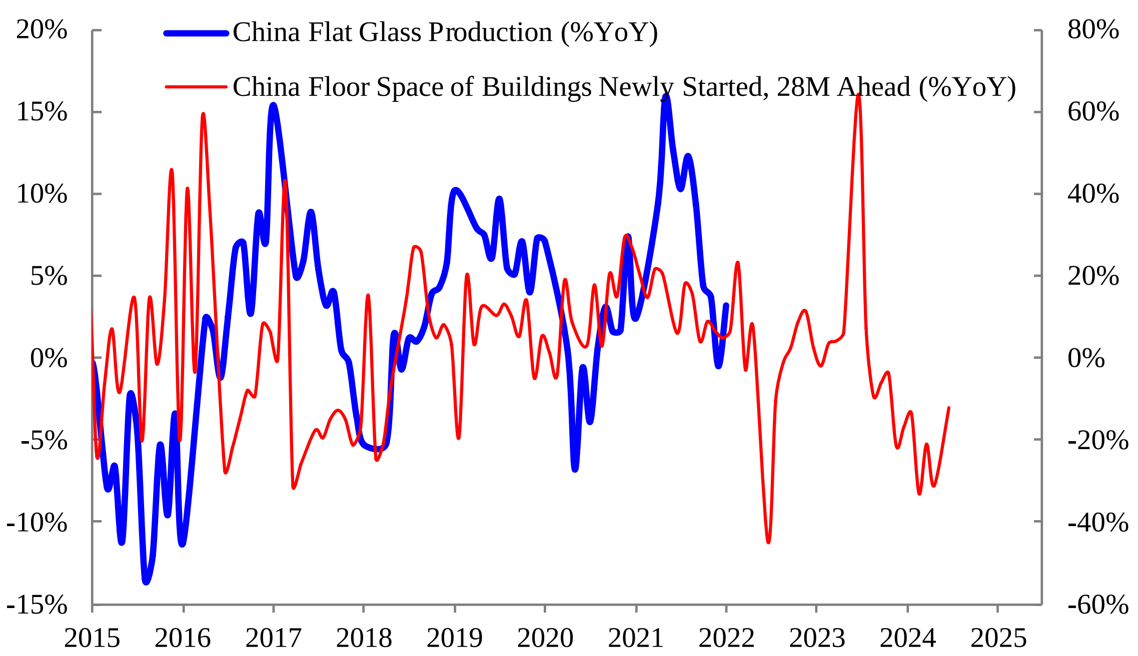
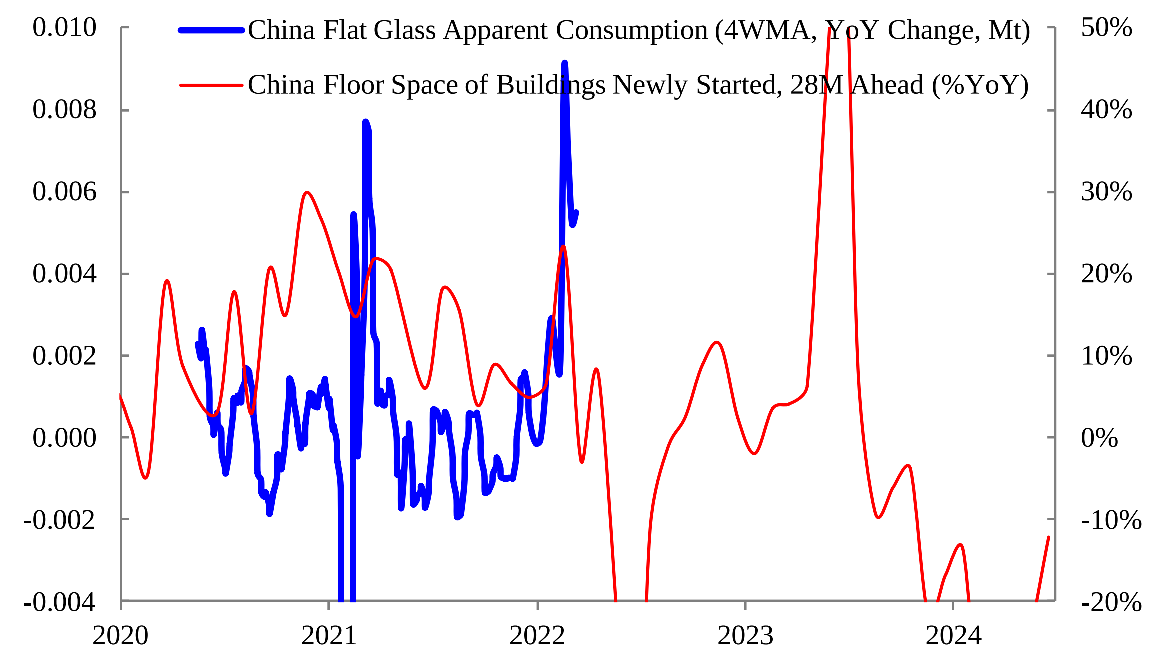


Chart 37: Bull Case: Under a 28-month leading relationship, flat glass consumption will increase by 5% YoY.



Our base case suggests that China's 2022 flat glass consumption will be flat YoY.

- However, demand usually picks up before output, meaning the newly started floor space may precede flat glass consumption by a shorter timeframe.
- If the correlation between the two is shortened to 20 months, 2022's flat glass demand will be flat YoY. However, if we adjust the correlation to a shorter timeframe of 12 months, it will be bearish for 2022's flat glass consumption, which is estimated to decline by -10% YoY. The shorter the lead time for newly started to drive flat glass consumption, the more unfavorable it is for the commodity as newly started floor space fell into contraction in 2H 2021.
- Our industry survey, which targets first and second-tier cities, suggests that there is a good chance that newly started floor space precedes flat glass consumption by 12 months or less. That said, these advanced cities may not be representative of China as their construction efficiency may be higher than average. Therefore, a -10% YoY fall in flat glass consumption is unlikely.

Chart 38: Base Case: Under 20 months leading relationship, flat glass consumption will be flat YoY.

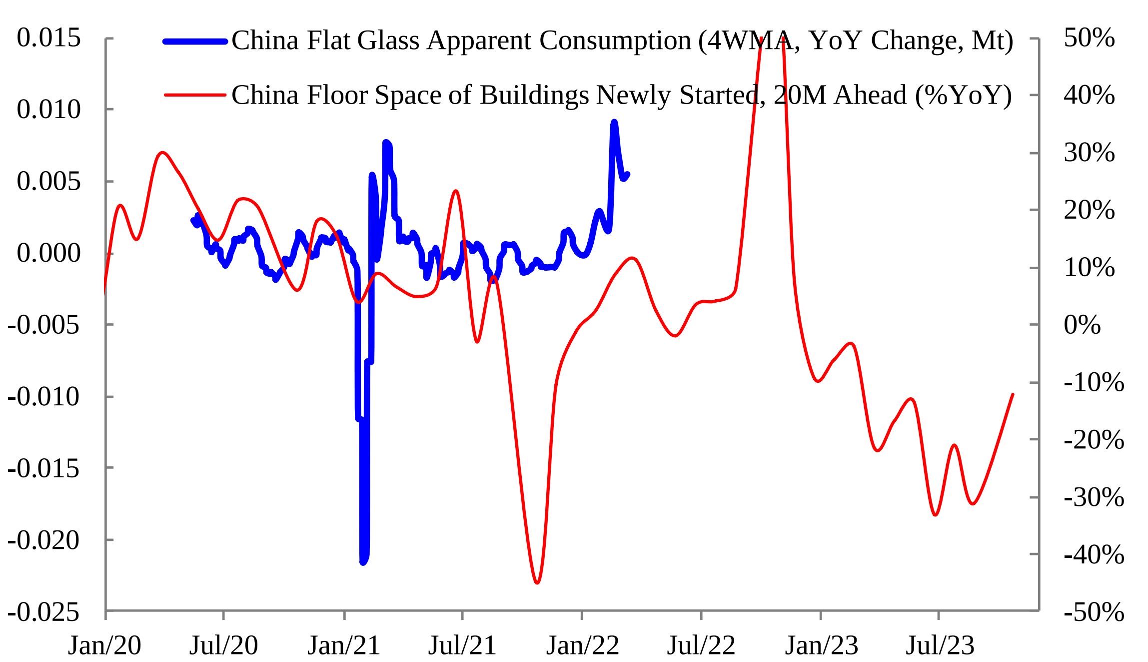
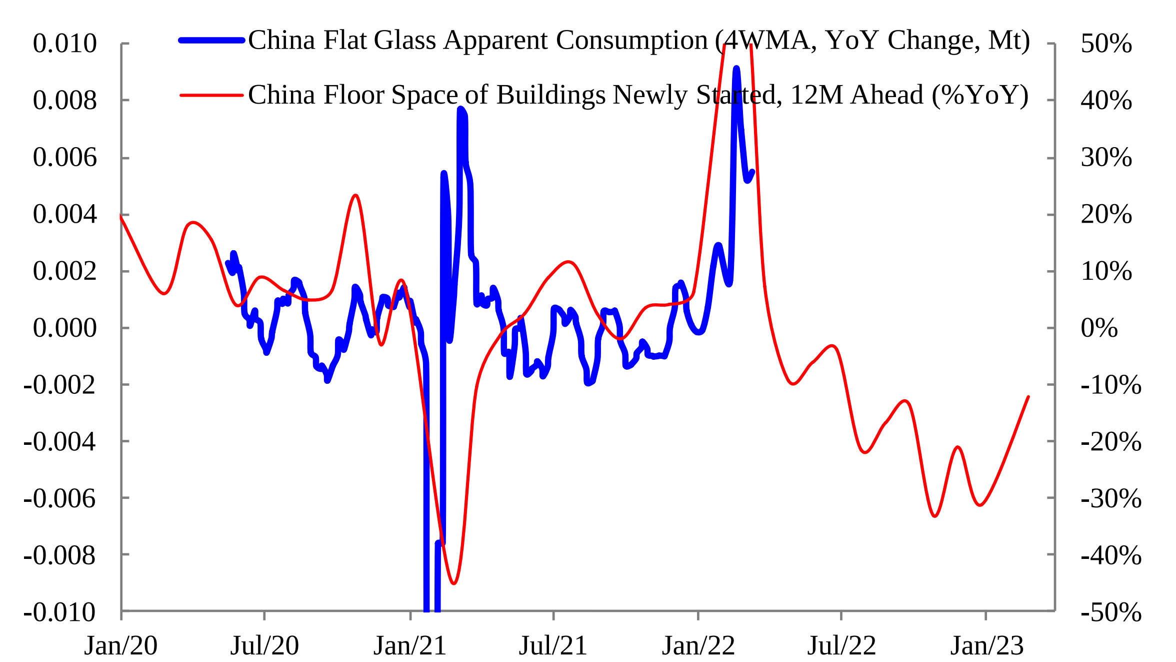


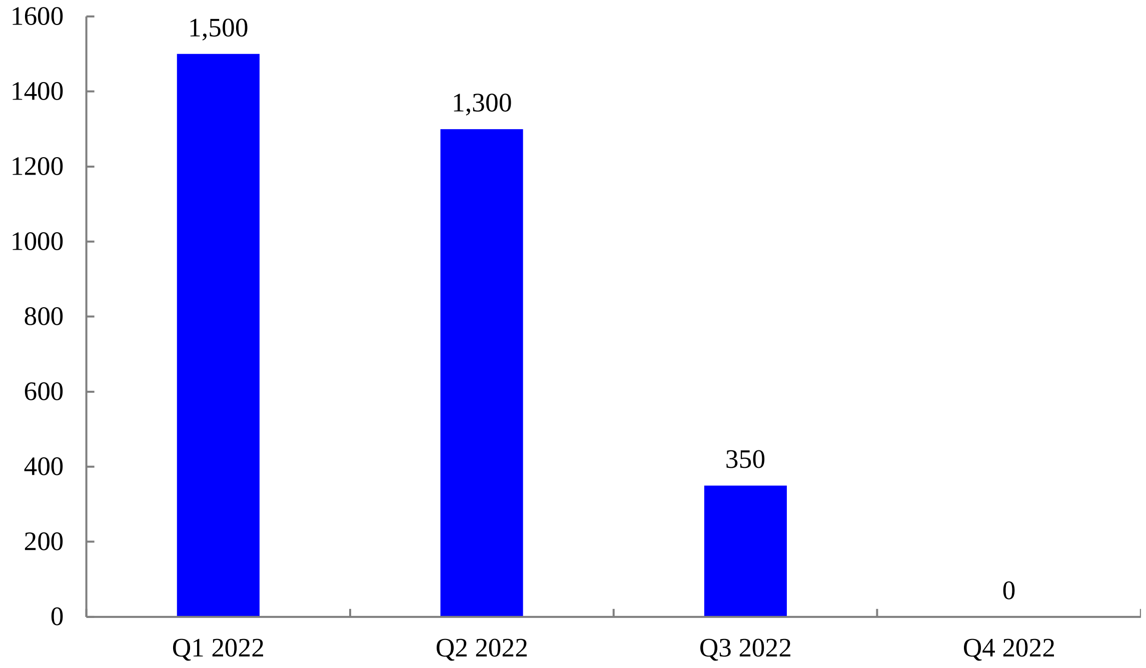
Chart 39: Bear Case: Under 12 months leading relationship (in first and second-tier cities), flat glass consumption will fall by -10% YoY.



China's flat glass supply may increase by 3,150 tons with most of the increase concentrated in 1H 2022.

- In 2022, China's flat glass supply may increase by 3,150 tons, with most of the increase concentrated in 1H 2022. The industry's supply will be in excess under the base case scenario of no growth in flat glass demand. Inventory build-up pressure will be high in 2H 2022 unless there is a change in seasonal patterns.

Chart 40: China 2022 Flat Glass Supply Increase*, Tons: New capacity in 1H 2022 will gradually ramp up in 2H 2022.



**New + Restarting Capacities – Maintenance*

Chart 41: China Flat Glass Factory Inventory, Mt: Bull Case Scenario: Assume 5% Growth

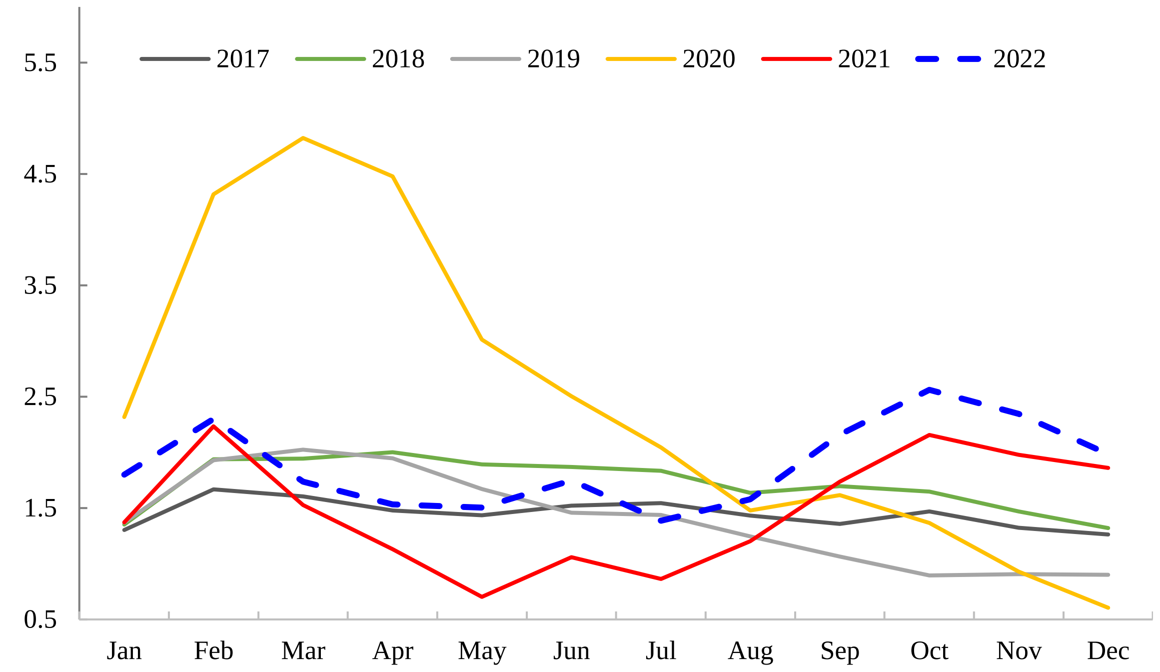


Chart 42: China Flat Glass Factory Inventory, Mt: Base Case Scenario: Assume 0% Growth

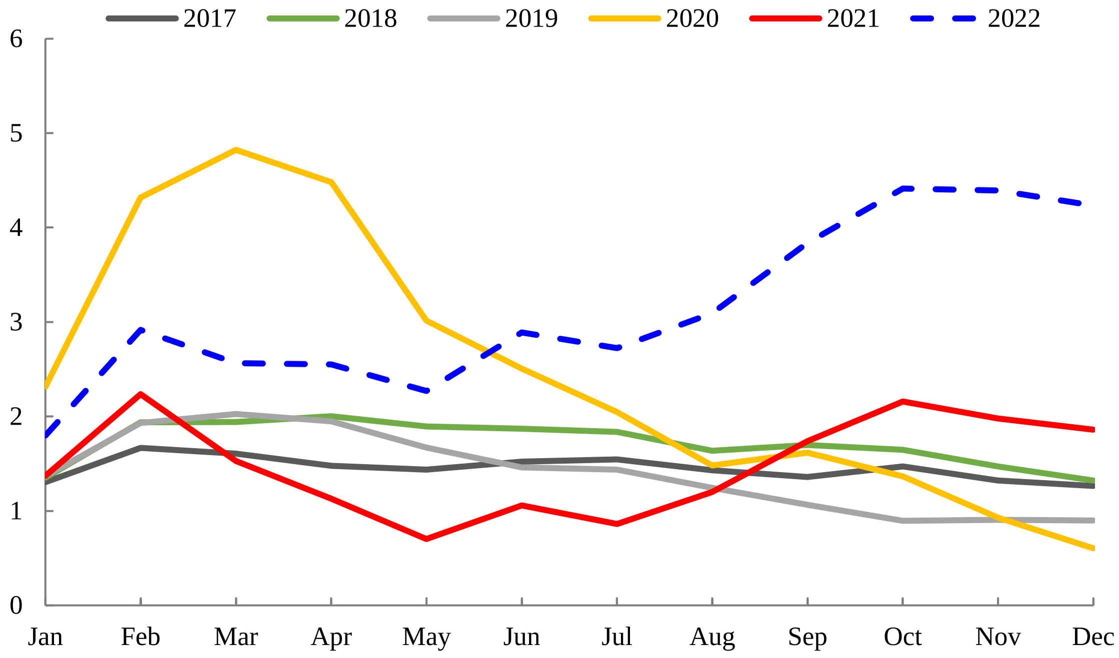
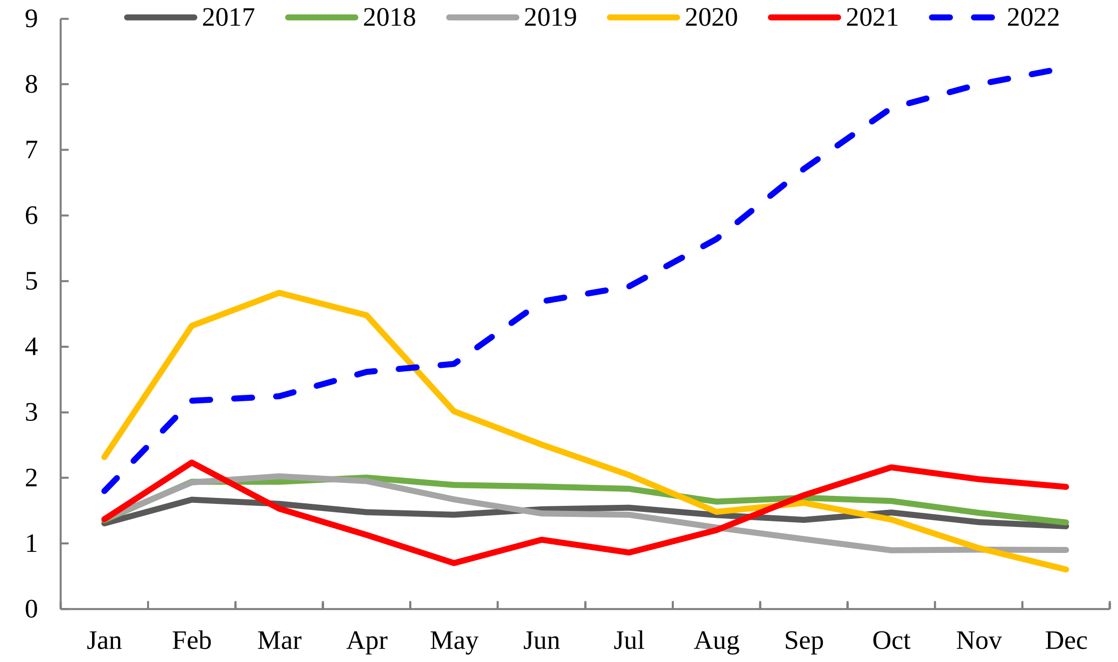


Chart 43: China Flat Glass Factory Inventory, Mt: Bear Case Scenario: Assume -10% Decline



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