

## METALS & MINING

18 October 2023

### Steel demand resilience lowers downside risk to margins

- **WSA outlook points to resilient steel demand with stabilisation in China, lowering the downside risk to steel margins**
- **Continuing tightness in coking coal into Q3 shifts likelihood of margin stabilisation to late-H2FY24**
- **We remain constructive on Indian ferrous players given benefits from upcoming brownfield expansion; prefer TATA**

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**Ferrous wrap:** In this report, we cover the WSA's global steel demand outlook, China's Sep'23 production data, and the quarterly production releases of global iron ore majors – BHP, Rio Tinto (RIO) and Vale.

**Resilient steel demand lowers risk to margins:** The WSA's Oct'23 steel demand outlook points to resilient growth in CY23 despite a lower forecast of 1.8%. More importantly, WSA expects China's property market to stabilise in the later part of the year and sees demand growth supported by government measures.

**China's production trending down but more cuts needed:** While China's steel production has dropped to 82mt or 1bnt annualised in Sep'23, demand is likely to soften in winter months, with early signs already visible in October. Exports also remain high at 8mt in September. We believe China needs further production cuts to balance the domestic market in winter months.

**Iron ore to be range-bound:** Though collective iron ore production increased seasonally for the three iron ore majors, it is likely to be somewhat down-to-flat QoQ over Oct-Dec'23. With potential steel production cuts in China, the iron ore market balance is likely to loosen, keeping prices softer in the range of US\$ 100-110/t.

**Coking coal tightness to continue through December:** BHP's release confirms weakness in Australian coking coal supply over Jul-Sep'23, which we believe has driven up prices from US\$ 230/t to over US\$ 350/t. Further, BHP's guidance suggests supply weakness is likely to continue till December.

**Margin stabilisation to shift to Q4FY24:** With tightness in coking coal continuing in Q3FY24, we expect margin stabilisation to move to Q4 – still within our current timeframe of H2FY24 (see our [metals quarterly preview](#) of 11 October).

**Constructive on Indian ferrous sector:** Earnings prospects from ongoing expansion keeps us positive even at mid-cycle margins. Maintain BUY on TATA (TP Rs 155) and JSP (TP Rs 810).

### Recommendation snapshot

Ticker	Price	Target	Rating
JSP IN	683	810	BUY
JSTL IN	784	845	HOLD
SAIL IN	88	90	HOLD
TATA IN	127	155	BUY

Price & Target in Rupees | Price as of 18 Oct 2023



## Steel demand outlook

Despite paring its forecast, the World Steel Association (WSA) continues to expect resilient global steel demand growth during CY23 in its Oct'23 Short Range Outlook. More importantly, WSA expects China's property market to stabilise in the later part of the year and return to positive demand growth supported by government measures. This optimistic commentary lowers the downside risk to steel margins. For India as well, WSA has raised demand forecasts.

- **World steel demand growth – resilient in CY23 even after downward revision.** WSA lowered its CY23 growth forecast to 1.8% from 2.3%. This factors in slower growth in the developed world (-12mt from the last forecast in Apr'23), partially offset by stronger demand growth in Russia (+4.2mt), Turkey (+3.3mt) and India (+2.6mt). WSA highlights that Infrastructure investment momentum has been cushioning weakness in construction to some extent across regions.

**Fig 1 – World steel demand growth forecast by WSA**

Region	Steel demand forecasts (mt) (Oct'23 assessment)			Demand growth forecast (%) (Oct'23 assessment)			Apr'23 assessment	
	2022	2023F	2024F	2022	2023F	2024F	2023F	2024F
Europe	191	189	200	(6.8)	(1.0)	5.7	1.3	5.7
USMCA	133	134	136	(3.0)	0.9	1.5	1.6	2.3
Asia ex-China	344	359	376	(0.5)	4.2	4.6	5.3	4.3
Others	193	193	198	(4.2)	(0.2)	2.7	(0.1)	1.1
World ex-China	862	875	910	(3.2)	1.6	4.0	2.6	3.6
China	921	939	939	(3.5)	2.0	0.0	2.0	0.0
<b>World</b>	<b>1,783</b>	<b>1,815</b>	<b>1,849</b>	<b>(3.3)</b>	<b>1.8</b>	<b>1.9</b>	<b>2.3</b>	<b>1.7</b>

Source: World Steel Association, BOBCAPS Research

- **China steel demand growth forecast to be positive in CY23.** RIO's assessment indicates that steel demand in China increased 1% YoY over January-August. WSA has also maintained its China steel demand growth forecast at 2% for the year on the back of support from infrastructure investments, moderate growth in manufacturing (particularly auto and appliances) and expected stabilisation in the property sector with additional government measures in Jul'23.

For CY24, WSA expects steel demand to sustain at the level of CY23 assuming the Chinese government introduces additional measures to support the economy. It also expects infrastructure investments to remain moderately positive through the year as the central government kicks off additional projects.

- **World steel demand growth to come back on track in CY24.** WSA largely maintains world steel demand growth at ~1.85bnt in CY24, raising its growth forecast to 1.9% (from 1.7%). It expects slower demand growth in developed economies to be offset by faster growth in emerging economies.
- **Developed economies are forecast to contract 1.8% in CY23** after a fall of 6.4% in CY22 with Europe suffering from monetary tightening and high energy costs. In CY24, WSA expects a technical rebound to drive 2.8% growth in steel demand.
- **Emerging/developing economies are forecast to rebound** from a decline of 0.6% in CY22 to growth of 4.4% in CY23 and 4.8% in CY24. While WSA highlights

Developing Asia ex-China as the most resilient region within the emerging economies, it emphasises the impact of tighter monetary conditions on Latin America.

- **US steel demand to decline in CY23 despite resilient economy.** WSA expects a demand decline of 1.3% from steel-using sectors in the US in CY23 as a slowdown in residential construction is only partly offset by higher infrastructure investment and momentum in commercial construction. RIO has also noted a slowing pace of economic activity from tighter monetary policies and the possibility of recession by the year-end.
- **India steel demand growth stands revised up** to 8.6% (from 7.3%) in CY23 and 7.7% (from 6.2%) in CY24 by WSA, recognising stability of the economy despite the high interest rate environment, and government spending on infrastructure and private investment recovery as growth drivers.

### Readthrough from China's September production data

- **China showing clearer signs of stabilisation.** China reported Q3CY23 GDP at 4.9%, ahead of consensus of 4.4% and up 1.3% QoQ in seasonally adjusted terms. With CY23 YTD GDP at 5.2%, China needs to deliver 4.4% YoY growth in Q4CY23 to meet its 5% target. While 83% of CY23 YTD GDP growth has been supported by consumption, 30% was driven by capital formation partially offset by a 13% decline in net exports.
- **Other indicators also show positive momentum.** (a) September industrial production grew 4.5% (vs. consensus 4.4%, Aug 4.5%), (b) September retail sales grew 5.5% YoY, the highest since May (vs. consensus 4.9%, Aug 12.7%), and (c) power generation was up 7.7% YoY for the month and 4.2% in CY23 YTD.
- **Steel production falls in Sep but more needed through Q4.** China's crude steel output stood at 82.1mt in September, declining 5% MoM and 5.6% YoY. The production run-rate has come down to 1bnt annualised, indicating a more balanced market, but early signs show a further slowdown in steel demand in October. Also, steel exports have remained high at 8.1mt even in September, totalling 66.8mt since January.

While it may be difficult for China to now maintain CY23 production at CY22 levels, added cuts would help improve the market balance when demand retreats further during winter months. To push CY23 production below CY22, China needs another 10mt cut below the September level to ~72mt per month during Q4CY23.

- **Real estate weakness continues; measures will take time to flow through.** January-September property investment declined 9.1% YoY (vs. -8.8% in Jan-Aug), sales fell 7.5% YoY (vs. -7.1%), starts were down 23.4% YoY (vs. -24.4%), and developers' funding contracted 13.5% YoY (vs. -12.9%). Implied September investment dropped 18.7% YoY (vs. -19.1% in Aug) and sales fell 19.8% YoY (vs. -24.0%).

## Iron ore outlook

Though collective iron ore production increased seasonally for the three iron ore majors, it is likely to be somewhat down-to-flat QoQ over Oct-Dec'23. With potential steel production cuts in China, the iron ore market balance is likely to loosen, keeping prices softer in the range of US\$ 100-110/t.

- **Iron ore supported by resilient China steel production.** RIO highlights that iron ore is finding support from resilient demand in China, backed by stable domestic steel demand and higher steel exports. RIO also highlights that portside iron ore inventory at China remains at a three-year low.
- **Seasonal uptick in iron ore supply over Jul-Sep quarter...** Production releases across the three global iron ore majors indicate a seasonal supply uptick of 4% QoQ over the July-September quarter. Though BHP's iron ore production was down 4% QoQ on planned maintenance and tie-in activities at its main hub, Western Australia Iron Ore (WAIO), Vale's shipments grew 10% QoQ supported by inventory release and RIO's shipments increased 6% QoQ.
- **...but flat-to-lower QoQ supply likely over Oct-Dec quarter.** All three majors have maintained production guidance for the current financial year. Implied Q4CY23 shipment guidance for both RIO and Vale points to stable supply for the quarter.
  - RIO: Implied Q4 shipment guidance works out to 82.0-89.5mt, which shows the possibility of an increase in supply to over 83.9mt in Q3CY23.
  - Vale: Implied Q4 production guidance works out to 78-88mt, which could mean somewhat down-to-stable Q3 production of 86mt.
  - BHP: While we don't have implied guidance for Q4CY23 owing to a different financial year, BHP's guidance implies stable supply over Oct-Dec'23 with the company indicating that its production outlook is weighted toward Jan-Jun'24, while maintaining annual guidance at 282-294mt for Jul-Jun'24.

**Fig 2 – The latest guidance from three global majors point to somewhat down-to-flat QoQ supply over Oct-Dec'23**

(mt)	Q1CY23	Q2CY23	Q3CY23	Q4CY23	Guidance
<b>Production</b>					
BHP	66	73	69	-	Jul-Jun'24: 282-294, Medium-term 305
RIO	79	81	84	-	-
Vale	67	79	86	78-88	CY23: 310-320
<b>Subtotal</b>	<b>212</b>	<b>233</b>	<b>239</b>	<b>-</b>	<b>-</b>
<b>Shipments</b>					
BHP	67	71	72	-	-
RIO	83	79	84	82-89.5	CY23: Upper half of 320-335, CY24: 323-338
Vale	46	63	70	-	-
<b>Subtotal</b>	<b>195</b>	<b>214</b>	<b>225</b>	<b>-</b>	<b>-</b>

Source: Company, BOBCAPS Research

### Other highlights

- Though RIO maintains its CY23 guidance at the upper half of the original 320-335mt range, it anticipates a marginal uptick to 323-338mt for CY24. In a somewhat negative development, RIO's supply mix now contains a higher proportion (17%) of lower grade iron ore (SP10) with Fe content at 59%. RIO expects SP10 share to remain high at 13-15% for CY23.
- BHP highlights medium-term production potential at 305mt at WAIO.
- Vale's Q3CY23 production decline (-4% YoY) underscores continuing production issues. The company attributed the decline to lower run-of-mine production from the Paraopeba complex and lower output from Serra Norte.
- Vale's pellet production was up 20% YoY to 9.2mt in Q3CY23 with improved availability of pellet feed from the Brucutu and Itabira mines after partial resolution of legacy issues. The company is an important supplier in the small global third-party pellet market. Even in Q4, pellet production is likely to rise to 9.4-13.4mt based on unchanged annual guidance of 36-40mt for CY23.

### Coking coal outlook

BHP's September quarter production release confirms weakness in Australian coking coal supply over Jul-Sep'23, which we believe has driven up prices from US\$ 230/t in June-July to over US\$ 350/t. The company's guidance suggests that coking coal supply weakness will continue over Oct-Dec'23 and production will improve only over January-July. With November through March being the wet season in Australia, coking coal supply improvement is likely to be weather dependent as well, although the current expectation is for lower disruptions this monsoon with a transition from La-Nina to El-Nino.

- **BHP's coking coal production was down 34% QoQ over Jul-Sep'23.** BHP saw a drop in production due to maintenance, an extended longwall move and low inventory at its main coking coal hub, BMA.
- **Supply likely to remain weak over Oct-Dec'23.** BHP has guided for planned wash plant maintenance at Peak Downs and Caval Ridge and for continuing ramp up of Broadmeadow from the longwall move into Oct-Dec'23.
- **Coking coal production increase targeted only over Jan-Jun'24.** Despite a weaker production outlook for Jul-Dec'23, BHP has maintained annual guidance at 56-62mt over Jul-Jun'24. The company currently guides for a production increase over Jan-Jun'24 after completion of the above planned activities.

## Aluminium outlook

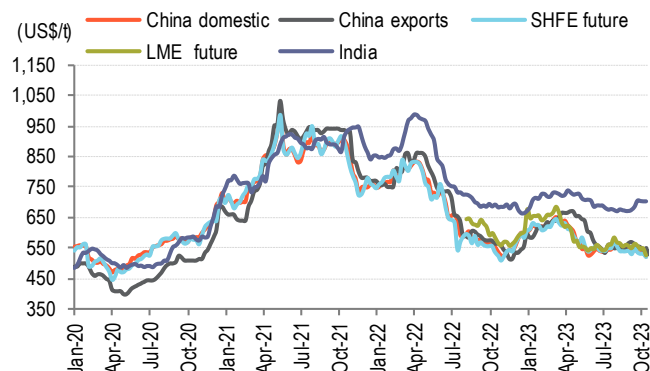
RIO's commentary in its Q3CY23 production result points to a sideways move for aluminium prices near-term but a resilient margin QoQ due to the decline in raw materials prices.

- **LME cash aluminium price rose by 10% QoQ**, although the average price for Jul-Sep'23 at US\$ 2,154/t was 5% lower QoQ. RIO notes that the decline in raw material prices is eroding cost support for aluminium.
- **China aluminium supply is ramping up** with the completion of smelter restarts in Yunnan. September aluminium output was at an all-time high of 3.6mt, translating to annualised production of 43.6mt. On the positive side, RIO highlights that reported inventories remain low in China with strong demand for aluminium from solar module construction.
- **Weak aluminium demand in developed economies.** RIO highlights weak aluminium shipments and orders in the US, Europe and Japan, except for the transport sector.

## Ferrous Chartbook

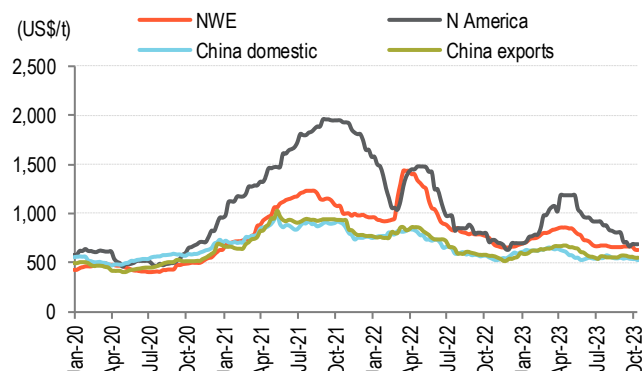
### Prices

**Fig 3 – HRC steel prices (China and India)**



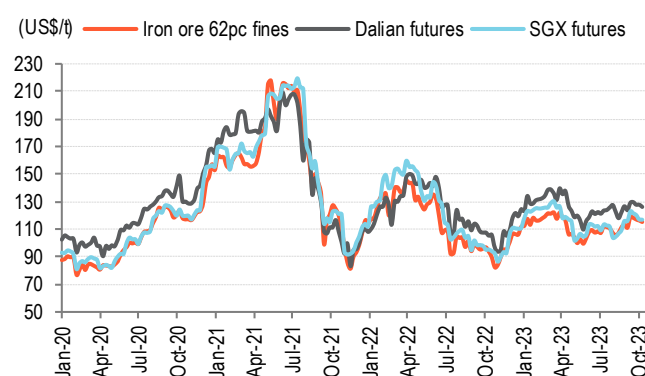
Source: Bloomberg, BOBCAPS Research | HRC: Hot Rolled Coil

**Fig 4 – Regional HRC steel prices**



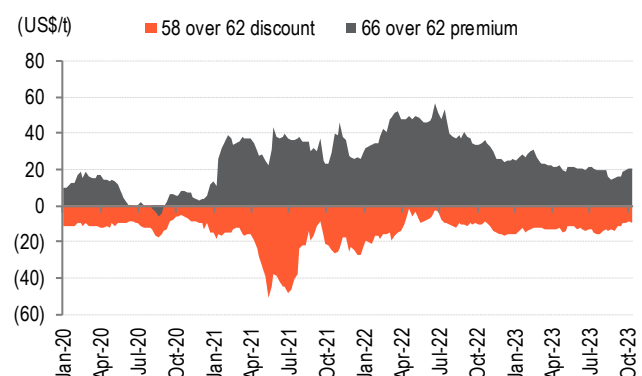
Source: Bloomberg, BOBCAPS Research

**Fig 5 – Iron ore prices**



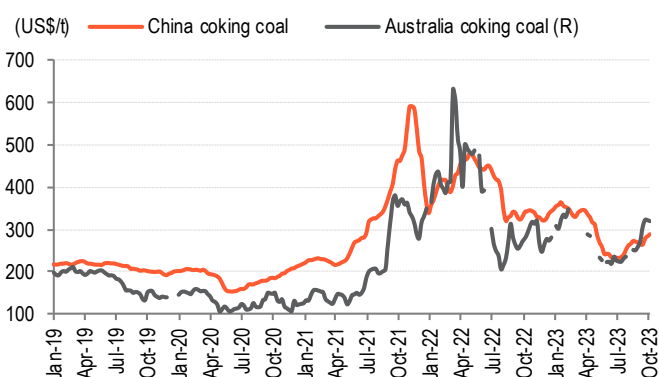
Source: Bloomberg, BOBCAPS Research

**Fig 6 – Iron ore grade premium/discount**



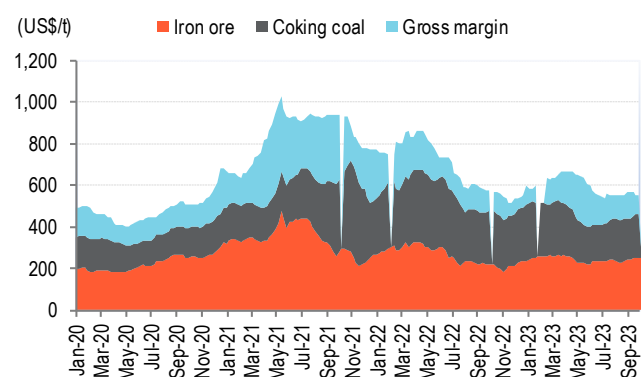
Source: Bloomberg, BOBCAPS Research

**Fig 7 – Coking coal prices**



Source: Bloomberg, BOBCAPS Research

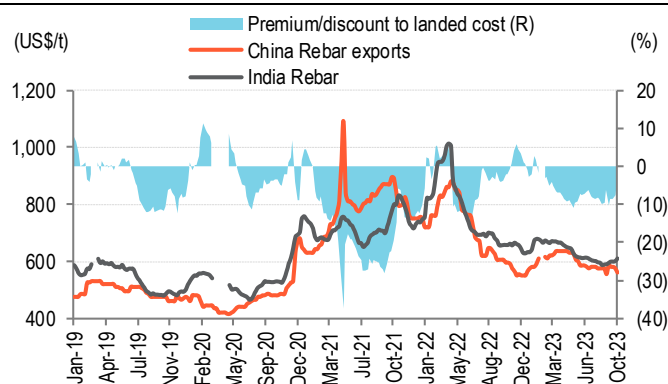
**Fig 8 – China HRC gross margin proxy (on export price)**



Source: Bloomberg, BOBCAPS Research

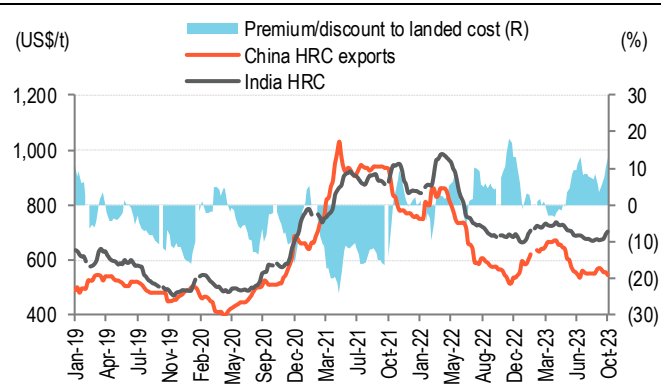
## India steel prices

**Fig 9 – India rebar premium/discount**



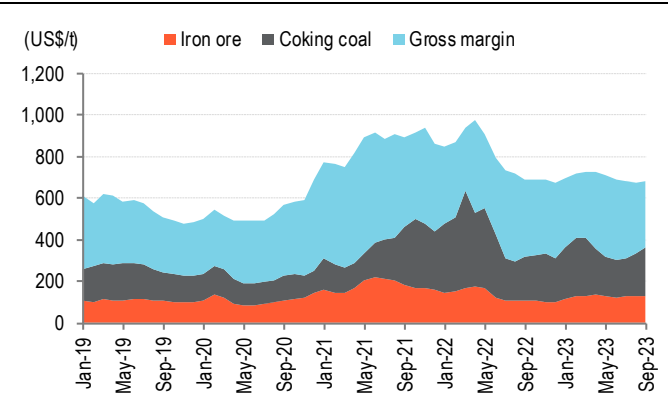
Source: : Bloomberg, Steelmint, BOBCAPS Research

**Fig 10 – India HRC premium/discount**



Source: Bloomberg, CMIE, BOBCAPS Research

**Fig 11 – India HRC gross margin proxy (monthly)**

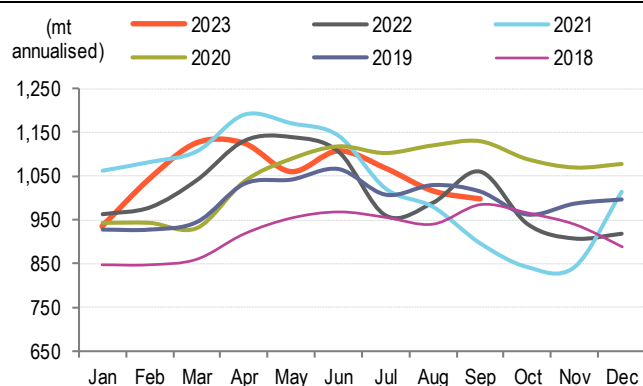


Source: : Bloomberg, Steelmint, BOBCAPS Research



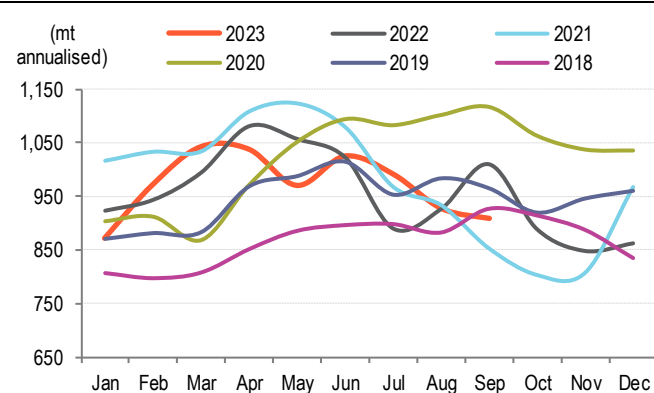
## China steel production and consumption

**Fig 12 – China steel production**



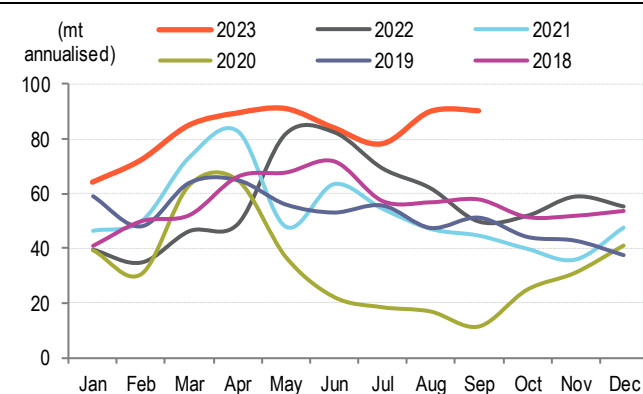
Source: Bloomberg, China National Bureau of Statistics, BOBCAPS Research

**Fig 13 – China apparent steel consumption**



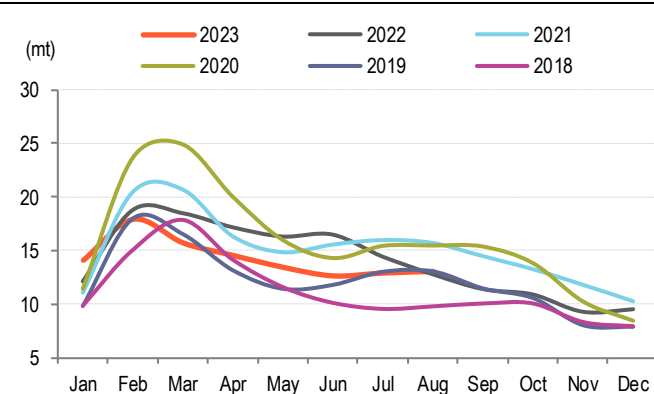
Source: Bloomberg, China Customs, China National Bureau of Statistics, BOBCAPS Research

**Fig 14 – China net steel exports**



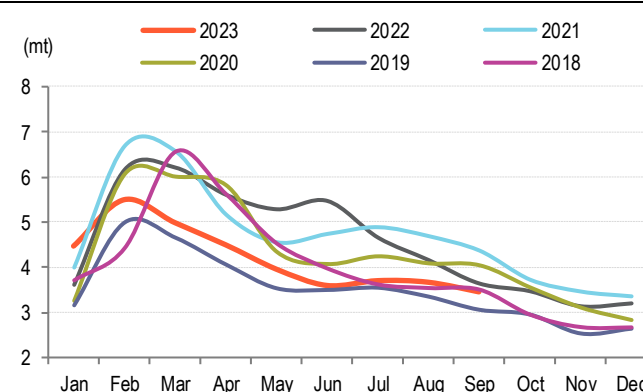
Source: Bloomberg, China Customs, BOBCAPS Research

**Fig 15 – China steel inventory for marketplace**



Source: Antaike, Bloomberg, BOBCAPS Research

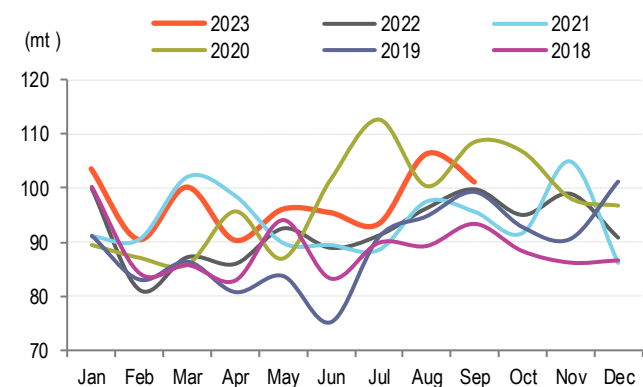
**Fig 16 – China steel inventory of traders**



Source: Bloomberg, Steelhome, BOBCAPS Research

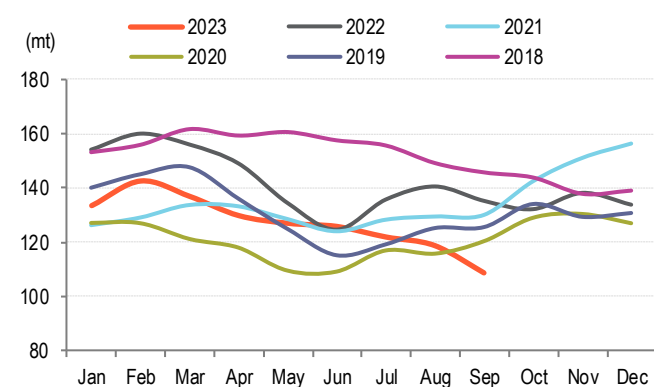
## Iron ore imports/exports

**Fig 17 – China iron ore imports**



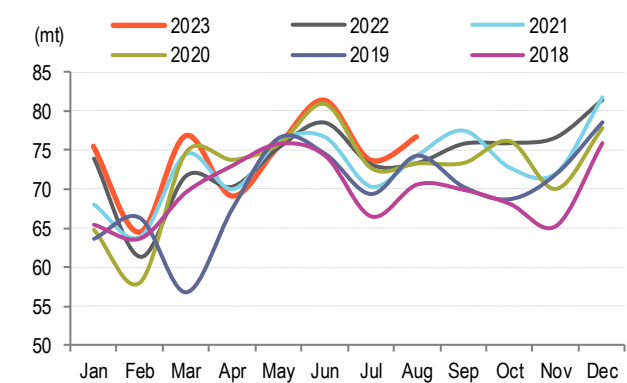
Source: Bloomberg, China Customs, BOBCAPS Research

**Fig 18 – China iron ore port inventory**



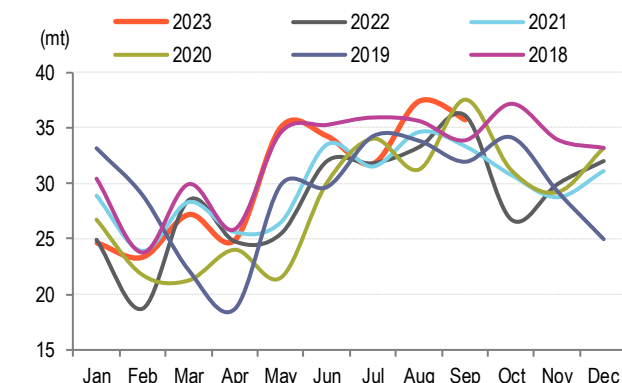
Source: Bloomberg, Steelhome, BOBCAPS Research

**Fig 19 – Australia iron ore exports (monthly)**



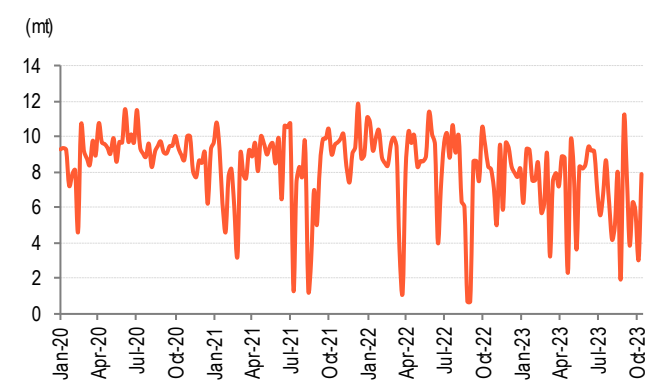
Source: Bloomberg, Australian Bureau of Statistics, BOBCAPS Research

**Fig 20 – Brazil iron ore exports (monthly)**



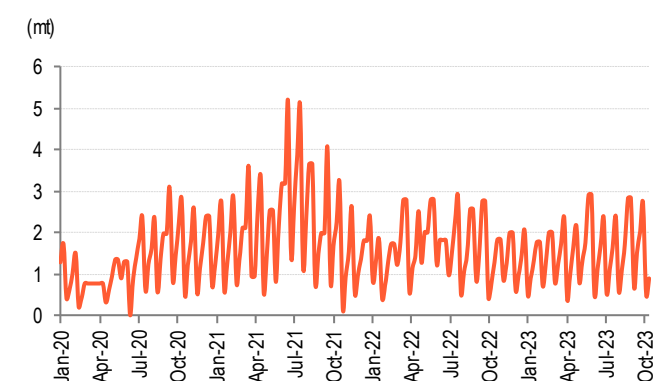
Source: Bloomberg, Brazil Ministry of Commerce, BOBCAPS Research

**Fig 21 – Australia Port Headland iron ore exports (weekly)**



Source: Bloomberg, Global Ports, BOBCAPS Research

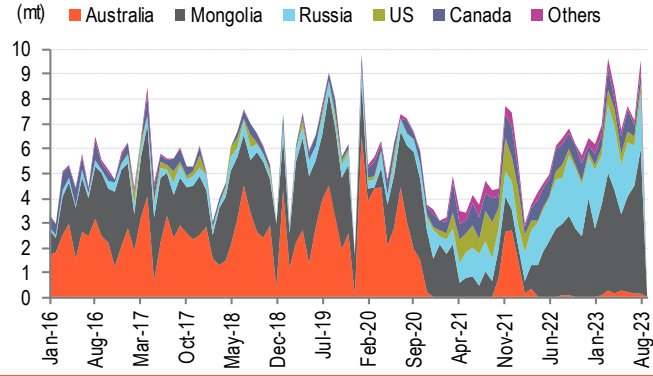
**Fig 22 – Brazil iron ore exports (weekly)**



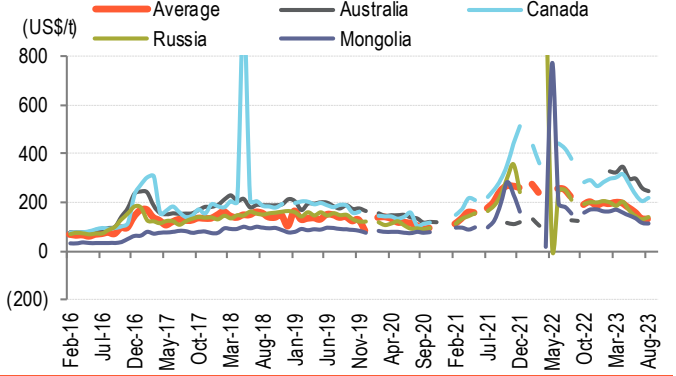
Source: Bloomberg, Brazil Ministry of Commerce, BOBCAPS Research

## Coking coal

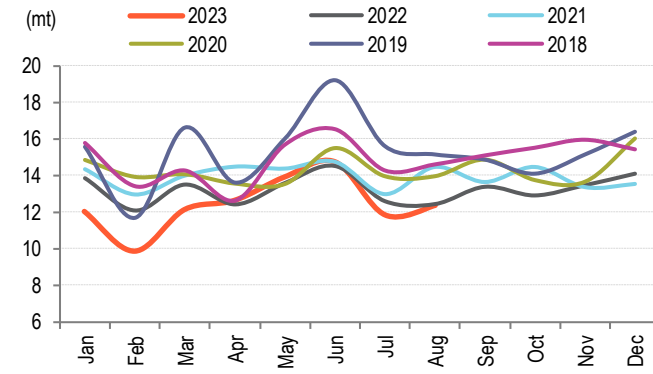
**Fig 23 – China coking coal imports**



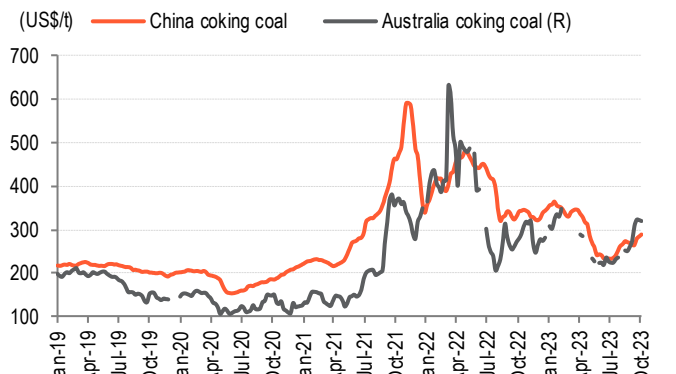
**Fig 24 – China coking coal import price**



**Fig 25 – Australia coking coal exports**

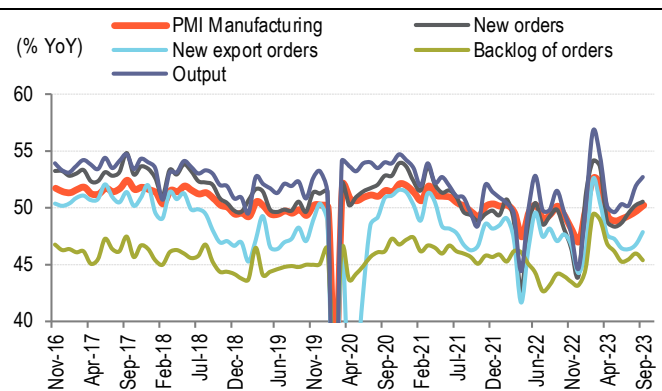


**Fig 26 – Coking coal price**



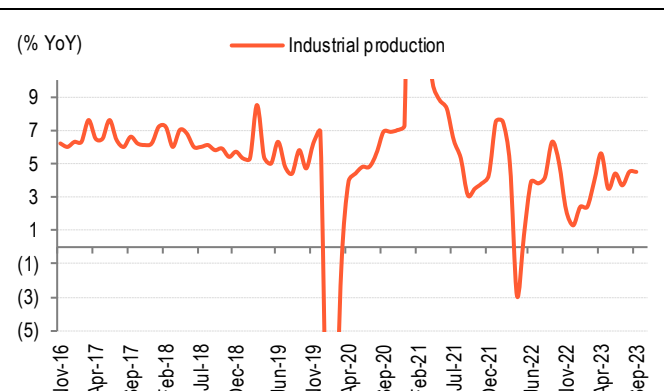
## China demand indicators

**Fig 27 – China manufacturing PMI**



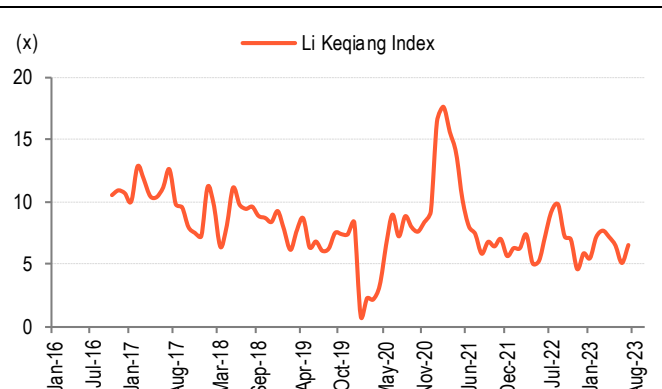
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 28 – China industrial production growth**



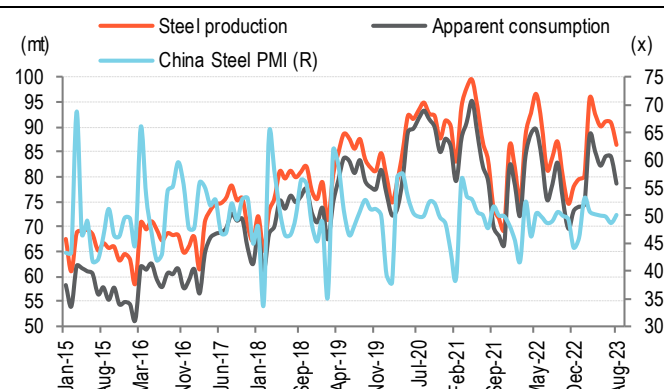
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 29 – China Li Keqiang Index (economy proxy)**



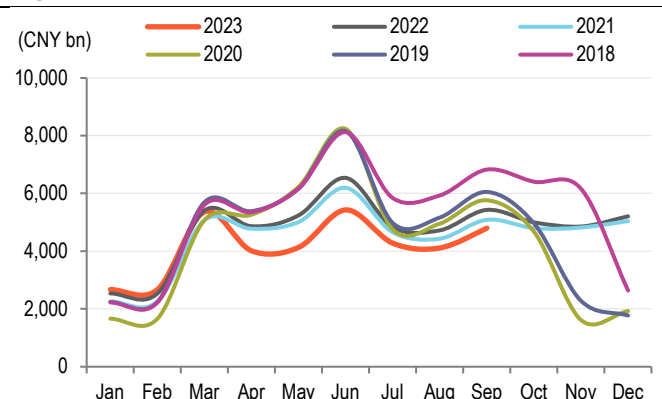
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research | FAI – Fixed Asset Investment

**Fig 30 – China steel PMI**



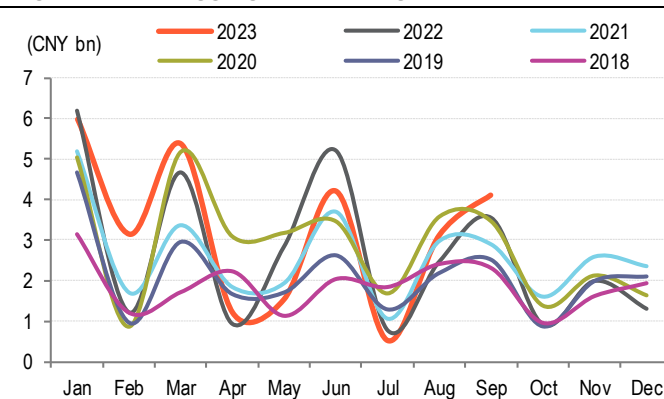
Source: Bloomberg, Steelhome, BOBCAPS Research

**Fig 31 – China FAI ex-rural households**



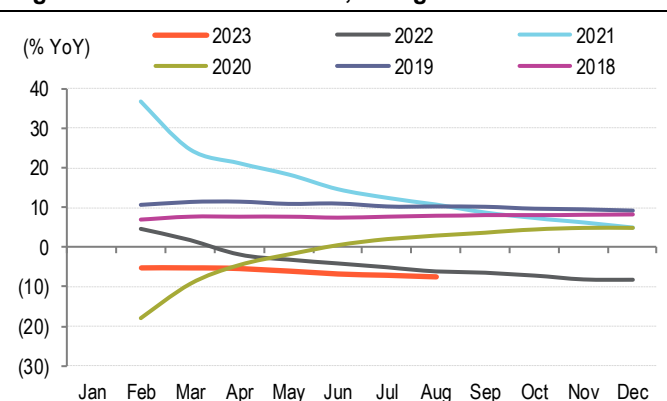
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research | FAI – Fixed Asset Investment

**Fig 32 – China aggregate financing**



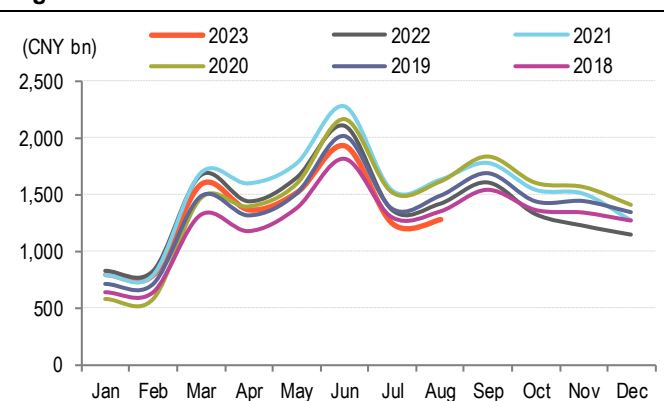
Source: Bloomberg, BOBCAPS Research

**Fig 33 – China real estate FAI, YTD growth**



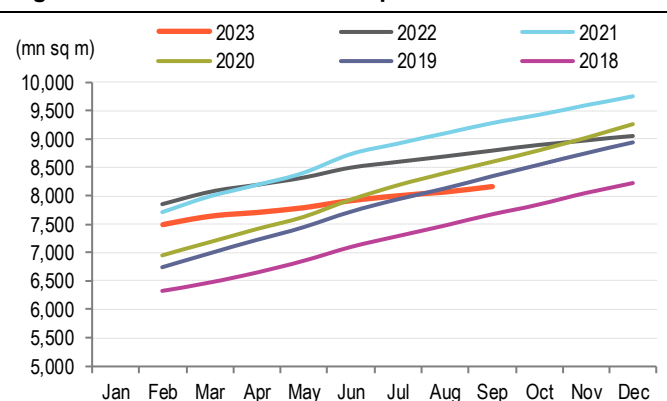
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 34 – China real estate FAI**



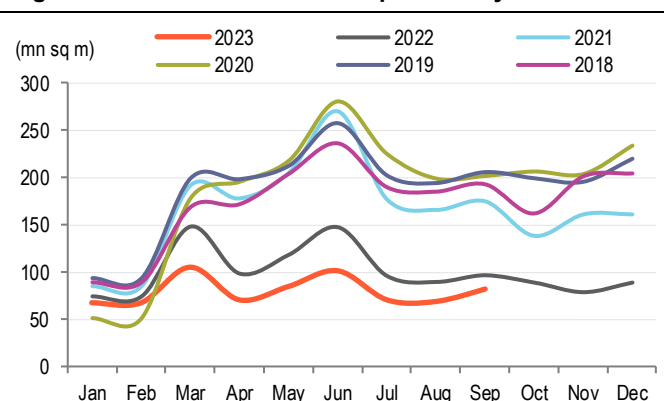
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 35 – China real estate floor space under construction**



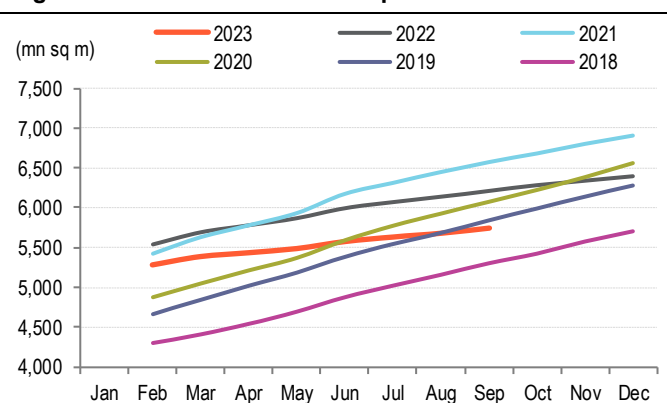
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 36 – China real estate floor space newly started**



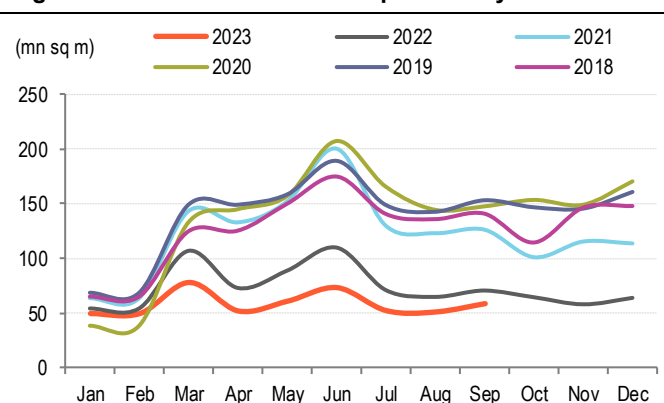
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 37 – China residential floor space under construction**



Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

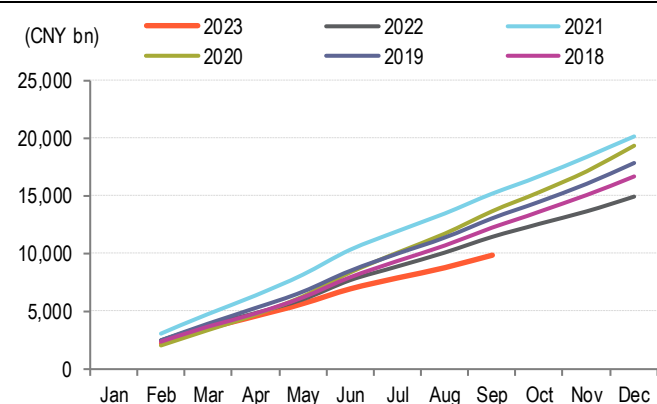
**Fig 38 – China residential floor space newly started**



Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

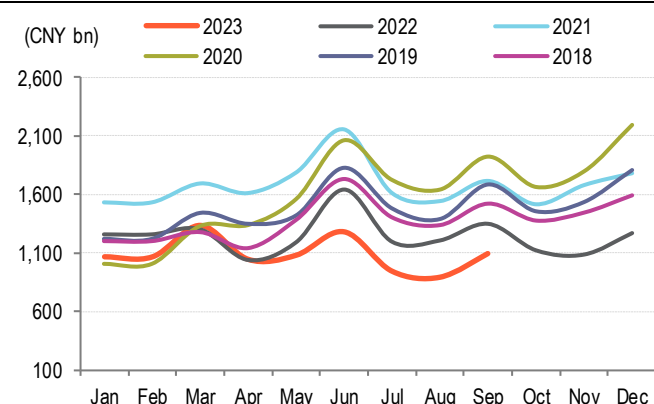
## China property sector indicators

**Fig 39 – China real estate – total funds cumulative**



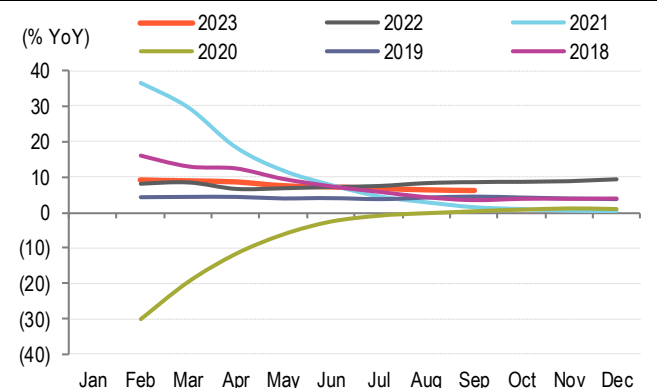
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 40 – China real estate – total funds monthly**



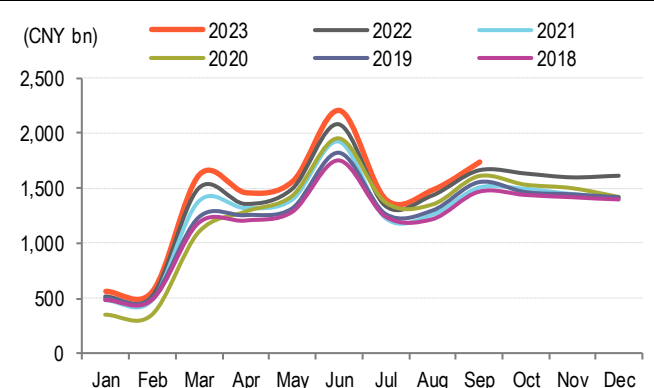
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 41 – China infrastructure FAI excluding electric power, heat power, gas and water, YTD growth**



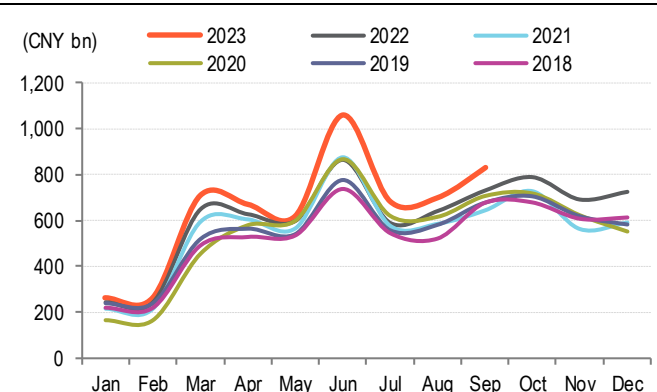
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 42 – China infrastructure FAI excluding electric power, heat power, gas and water**



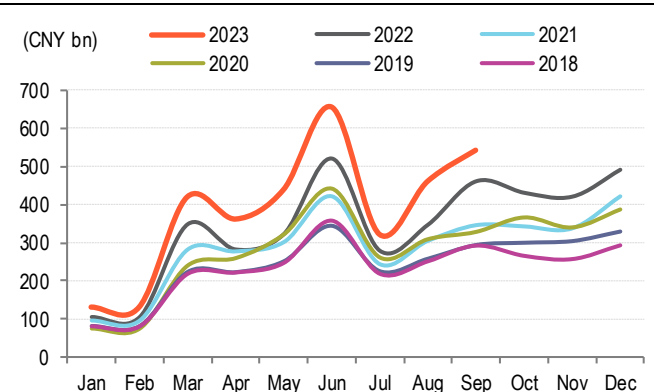
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

**Fig 43 – China transport, storage, posts FAI**



Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

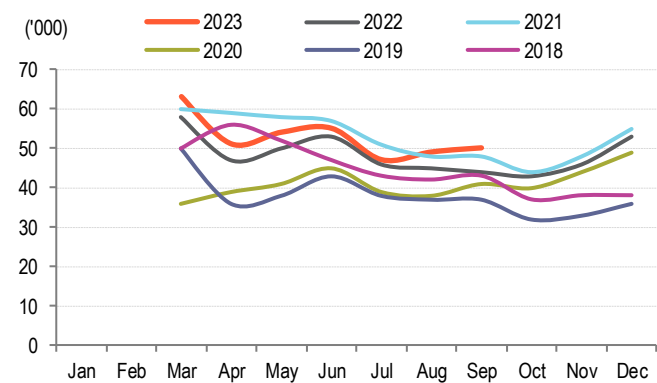
**Fig 44 – China power, gas and water FAI**



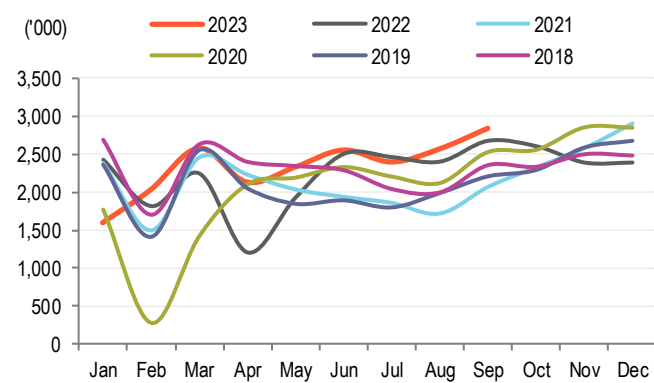
Source: Bloomberg, National Bureau of Statistics, BOBCAPS Research

## China downstream demand indicators

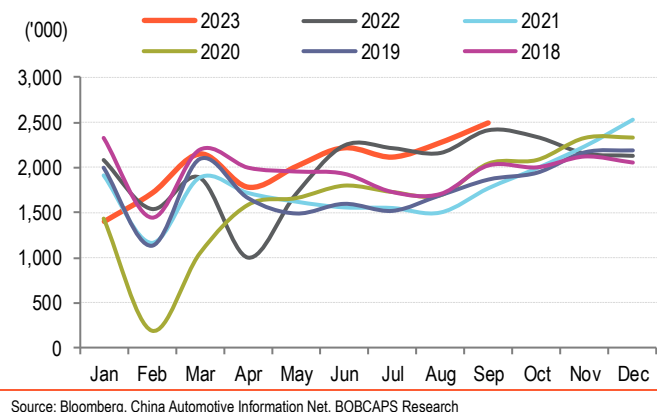
**Fig 45 – China machinery: Metal cutting machine production**



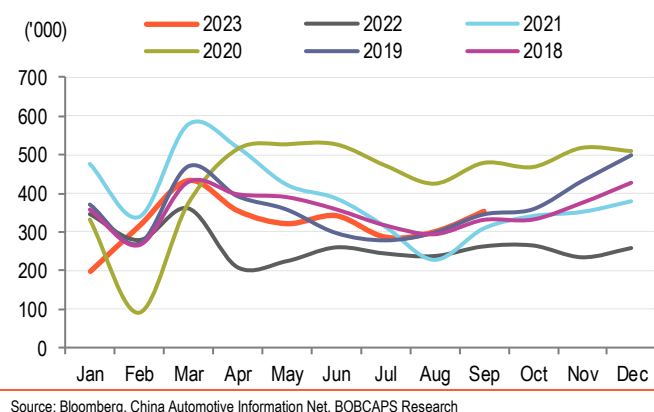
**Fig 46 – China automobiles: Vehicle production**



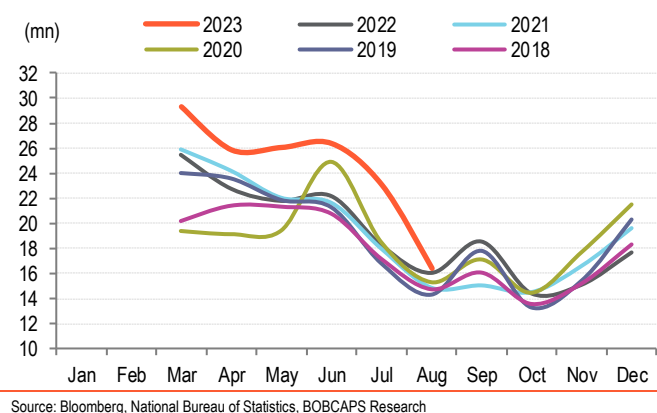
**Fig 47 – China automobiles: Passenger vehicle production**



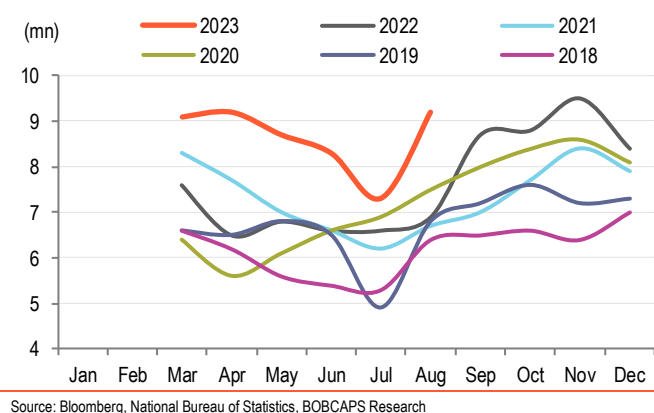
**Fig 48 – China automobiles: Commercial vehicle production**



**Fig 49 – China appliances: Air-conditioner production**



**Fig 50 – China appliances: Washing machine production**





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