

Aluminium supply woes keep growing as China orders output cuts

Smelters in China's Yunnan province are reducing output on tight power supply caused by declining rainfall while European and US capacity is being cut amid rising power costs following Russia's invasion of Ukraine



Source: Shutterstock

Yunnan province cuts supply

Aluminium smelters in Southwest China's Yunnan province, which accounts for 11% of China's aluminium output, have been required by the government to reduce their operating rates due to hydropower shortages in the drought-stricken province.

The smelters have been ordered to reduce the use of electricity by 15% to 30% from last week, which is expected to cut 800,000 tonnes to 1.6 million tonnes of aluminium production capacity.

The output reductions in Yunnan come after Sichuan smelters cut 920,000 tonnes of capacity in August, accounting for 2% of China's total.

The duration of the power cuts in Yunnan has not been officially announced yet but the market

believes it will depend on how quickly weather conditions improve in the region.

Chinese aluminium output climbs to record highs

Still, China's aluminium output has held up despite the energy crunch. The country's primary aluminium production hit a record in August surging 9.6% year-on-year to 3.51 million tonnes, according to data from the National Bureau of Statistics, beating the previous high in July. Output in the first eight months of the year gained 2.1% to 26.47 million tonnes.

However, output could have been constrained over September due to the ongoing power rationing in Yunnan province.

China's exports of unwrought aluminium and aluminium products have also risen in 2022 - up 31.5% so far this year versus a year earlier to 4.7 million tonnes - and are likely to rise further in the fourth quarter as European and the US producers have been slashing capacity over the past 12 months amid the worsening energy crisis following Russia's invasion of Ukraine.

In August, China exported 540,400 tonnes of unwrought aluminium and aluminium products, up 10.2% versus a year earlier.

Meanwhile, imports dropped 19% from a year earlier, reflecting muted domestic demand, record-high domestic production and tightening overseas supply. The country brought in 200,400 tonnes of unwrought aluminium and products in August, according to customs data.

On the raw material side, China's alumina exports are also increasing, with annual shipments through August reaching 720,000 tonnes, from just 100,000 tonnes a year earlier as buyers in Russia seek alternatives after the war in Ukraine cut off their traditional supplies.

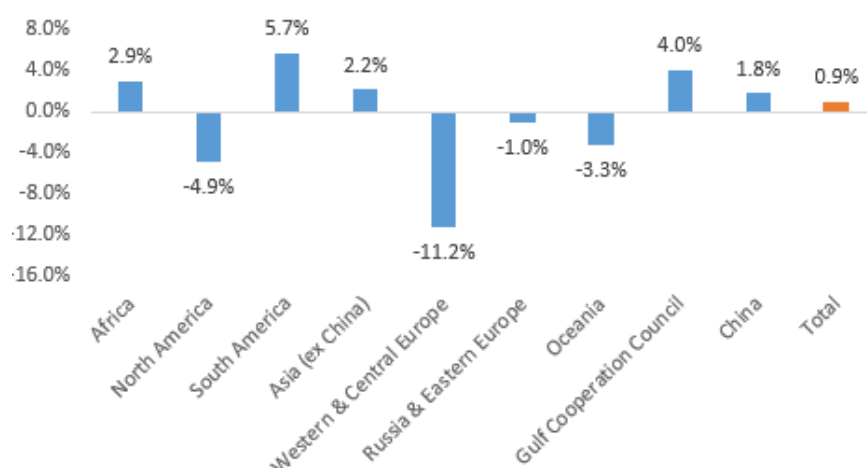
Globally, despite Chinese smelters facing energy rationing and European smelters slashing output, global aluminium production rose 3.5% year-on-year in August to 5.89 million tonnes, according to the International Aluminium Institute. Global year-to-date output totalled 45.448 million tonnes.

Several smelter cuts have already been announced across Europe since December 2021, including Alcoa's San Ciprian smelter and Hydro's plant in Slovakia due to high energy costs which account for about a third of aluminium's production costs.

About 1.48 million tonnes of capacity could be cut in Europe and the US, accounting for 1.9% of the global total. European smelters have already cut 1.18 million tonnes of output - around 11% of total installed capacity in the region.

Further smelter closures and curtailments in production are highly likely with Europe heading into the winter months and the war with Russia raging on.

Primary aluminium production (% YTD)



Source: International Aluminium Institute (IAI)

Global demand outlook worsens

The rise in Chinese output comes against weakening demand amid global economic gloom. Tighter global monetary policy, China's property crisis and the dollar's strength have all put downward pressure on the aluminium market.

However, the Chinese economy started to show some signs of recovery last week. Industrial production climbed 4.2% on the year, faster than July and above the consensus, according to the National Bureau of Statistics' latest data. Retail sales rose 5.4% from a year earlier, higher than expected and up from July.

China is also stepping up its efforts to boost its housing and construction sectors with more Chinese cities announcing credit support and subsidies for home purchases. Last week, China's Evergrande Group removed most of its construction-project freezes as China enters its peak building season, which traditionally lasts until the end of October.

Still, China's government and central banks' stimulus efforts have been mild so far in relation to Covid-19 restrictions in the country. Data last week showed home prices declining for a twelfth consecutive month in August taking house price inflation down to -2.1% year-on-year.

LME prices stuck in a range

Despite high energy prices, weak demand has continued to outweigh any potential supply concerns with the market's focus remaining more on the negative macro sentiment for now.

LME aluminium prices are now down more than 40% from their year-to-date highs of \$3,849/t reached in March and are hovering around their lowest levels since April 2021 amid fears that Russian supply could soon emerge at London Metal Exchange warehouses in Asia.

Russian aluminium producer Rusal is reportedly looking to deliver some of its metal directly to LME warehouses in Asia, as it increasingly struggles to find buyers. It is suggested that Rusal could deliver a small amount of aluminium to LME warehouses initially. Increased flows could cause some issues. Firstly, a strong increase in LME inventories could put further pressure on prices,

while there could also be a growing amount of aluminium in LME warehouses, which buyers are not willing to touch. This could potentially lead to a disconnect in prices.

LME 3M aluminium



Source: LME

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