A delicate balance for copper

Copper prices could slip moderately in 2022 given the overall global macro picture. But given supply constraints and its appeal to investors as the key energy transition metal, the stage is set for above long-term average prices over the next few years

A copper miner in Chile

Record high prices riding macro tailwinds

After touching a record high in early May of US$10,460/tonne, copper prices largely fluctuated above US$9,000/tonne, with annual average prices set to be around US$9,300/tonne in 2021, comfortably above its long-term average level. Macro tailwinds, micro positivity and investors' enthusiasm towards the key 'green' metal have contributed to the mantra of 'buying the dip' in the copper market.

Mine supply improve on a wave of projects

Despite many concerns over long-term copper supply due to a lack of investment over the last decade, this year's mine supply has surprised to the upside as planned projects come online. The previously anticipated high disruption rate has not caused meaningful production losses. This is on course to register a 3.3% year-on-year growth and should maintain a medium-to-high level over the next two years amid a wave of projects that are just beginning. However, there is a bigger issue in the logistics sector due to high freight rates and delays. While many expect the situation to improve throughout 2022, the new Omicron variant makes the outlook murky.

Similarly, refined production grew strongly by 4.8% YoY this year, driven by restarts at major smelters. The power crunch has had a more limited impact on smelter production than other energy-intensive metals. Refined supply is set to remain high over the next few years, driven by the expansion of some Chinese players such as Daye and some new projects in Indonesia and India.

Non-refined copper supply plays an increasingly important role

The supply of scrap and other unrefined copper such as blister and anode are becoming increasingly important and often have big effects on the refined market balances on the regional market. Policy shifts compounded by supply chain disruptions constantly impact these markets. As China tightened its standards on imported scrap together with a firm concentrate market, imports of blister/anode remained above trend during 2020 and 2021, although total imports of blister/anode come to 920kt for the full-year 2021 on an annualised basis, compared to just above 1 million tonnes from the previous year. This is likely due to bottlenecks in the shipping market.

> *Regional policies could throw a curveball to scrap supply in certain markets*

As for scrap, there has been a robust recovery so far this year after supply chains were hit by the pandemic in 2020. Higher prices have revitalised scrap flows amid recovering manufacturing activities post-pandemic. In the longer run, both scrap generation and recycling are set to grow from key regions following their respective green targets, which in theory would replace some demand for primary copper. Nevertheless, regional policies could throw a curveball to scrap supply in certain markets, most importantly to China.

It is estimated that the world scrap supply chain will continue to evolve and become more fragmented. This follows the rejig in Chinese scrap import policies in recent years. The European Union had proposed export restrictions on scrap. Following Beijing's move to tighten import scrap standards, Malaysia plans to lift its standards, thus quitting the role as a bridge in processing low-grade scrap and further exports to China. Other countries may take on the role, but such business is not deemed to be long-lasting due to both environmental and political concerns. Should these regional policies become enacted, they could potentially leave a supply gap.

'Green' demand contributes to the majority of the growth

On the demand side, the red metal is undergoing a shift in demand engines, with green demand contributing to more marginal growth in the overall usage. World primary copper use is poised to register strong growth of 6.5% YoY in 2021 on a lower base from last year. However, overall growth is expected to moderate slightly into 2022, whilst the green-related sectors such as electric vehicles and renewables would contribute almost half of the incremental usage next year.

However, the China property sector remains a big question mark as to whether there would be a soft landing following the Evergrande crisis and the indebtedness of some other property developers. For almost two decades, China's property sector growth and the nation's urbanisation have been the perennial engine of growth for copper demand, representing almost a quarter of the nation's total demand. In the medium term, we expect copper to continue to benefit from late-stage construction along with a recovery in property completions.

Prices to moderate but remain above long-term average

Looking ahead, supply chain bottlenecks with their effects on copper supply to the China market may not go away easily in 2022, especially given the spread of the Omicron variant. This is partially mirrored in the rise in longer-term cathode premiums that major suppliers offered to Chinese buyers for next year. In such cases, regional market imbalances will prompt import arbitrage.

The tailwinds from the macro front could turn into some headwinds as we move into 2022, which could take some wind out of copper's sails. This would include a stronger dollar and higher real rate along the US Federal Reserve's tightening cycle. Nevertheless, the low visible inventories may shield it from sharp price correction. While we anticipate that prices will slip moderately in 2022 from highs this year, the supply constraints over the long term and its appeal to investors as a key green metal are setting the stage for above long-term average prices over the next few years.

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