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Copper on firmer but slippery ground

Copper prices are at their highest since April, not least on reported trade talks progress. But it's not clear how long the rally will last

Copper looks to be standing on firmer ground for now

With copper seeing strong gains throughout December in the LME market and news that President Trump has 'signed off' a deal with China, the temptation is to increase our average forecast for next year. Copper briefly touched US$6,216/tonne on Friday (Dec 13) morning in London, the highest since April, further supported by a weakened dollar.

In the second half of this year, copper has been rangebound, with developments on the trade front dictating market movements. But it now looks to be on firmer ground, for now.

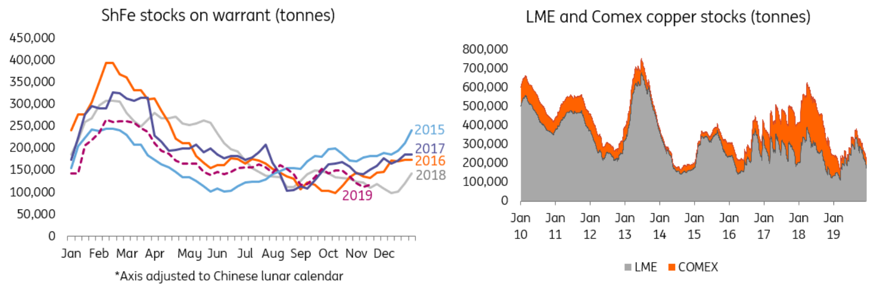
LME stock has halved by almost 47% to 176k from this year's high of 350k in late August. This provided psychological support. If the trend holds, it leaves some room for fundamentals to play a role.

> *There is little doubt that we will see excess supply in the market over the coming months*

However, the ShFE side seems to be entering into its traditional stock building season, which lasts until the end of February. According to the ShFE's Friday stock report, inventories have risen 4% week-on-week. This trend could continue over the next couple of months, barring no major surprises. One big uncertainty is to what extent stocks continue to build. If this is due to good demand or businesses preparing for next year, we will probably only see a moderate build-up and could even see a surprise to the downside.

We don't think producers will hold on to large inventories given the margin squeeze facing them. And we don't believe trading houses or end-users will either. Given that China's refined copper production has grown by more than 2% year-on-year for the first eleven months while demand has contracted, there is little doubt that we will see excess supply in the market over the coming months.

Copper stocks



Source: Source: Bloomberg, ING

No smooth ride ahead

For now, the market seems to have priced in much of the so-called 'phase one deal' and is awaiting the details; it's said it'll be signed off on the first week of January 2020. It looks like the market will be having a cheerful Christmas at least by then. However, 2020 is unlikely to be smooth going. The market may still enter a 'merry-go-round' situation, driven by dilemmas between hope and reality.

There is still no substantial resolution to the trade frictions when looking at all those aspects the US side is demanding, and we've yet to see the 25% tariff rollbacks China was asking for. Trade discussions are still signalling big uncertainties to the market. It's too early to say whether there's a firmer demand picture for copper.

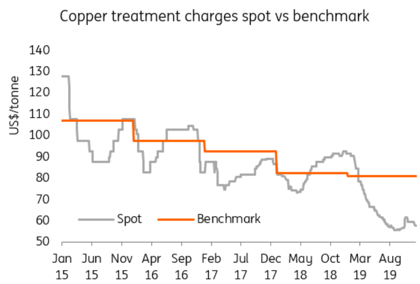
Our eurozone economist asks a good question about 'whether the sentiment data is entirely based on hopes for improvement, while the underlying economic situation doesn’t show many signs of recovery.' The same question could be asked about copper and demand for many industrial metals.

It's not certain whether investors will return to risky assets

Will investors return to risky assets? They may do, but it's not certain, as manufacturing indicators have not yet bottomed. And on top of that, there is another layer of political uncertainty. You can see that in the eurozone manufacturing PMI which came out on Monday. Our US economist recently wrote that 'Political uncertainty surrounding next year's election could also see businesses taking a more cautious approach on expansion plans, with an emphasis on "wait and see".'

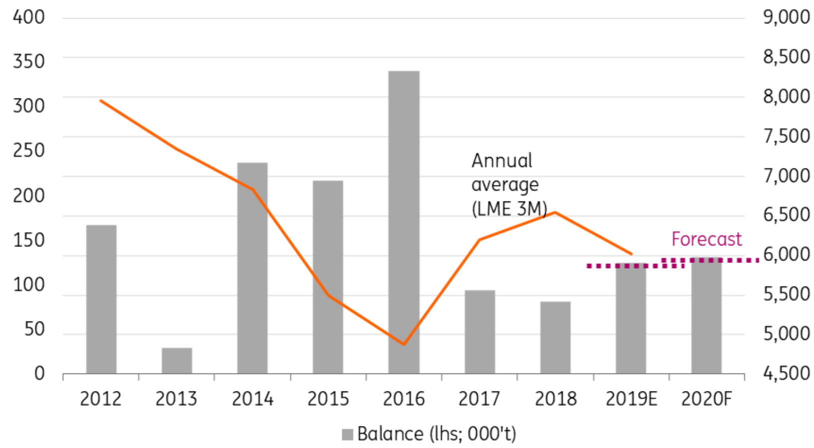
The latest data from China shows that despite fiscal stimulus, investment in infrastructure projects, which are mainly focused on transportation, has slowed down in November. There's more on that here.

Global mine supply increasing



Source: Source: Company Reports, Bloomberg, ING

Copper supply growth still outpaces demand and the market remains in a small surplus again



Source: Source: Bloomberg, ING

We're not particularly optimistic about the metal's demand in heavy sectors, such as vehicles and power. At the end of 2019, we're looking for copper demand to recover next year but this is from a small base. We currently estimate a moderate decline in China's demand growth of 0.5% year-on-year in 2019, potentially returning to 0.8% YoY growth next year on the assumption that trade talks don't deteriorate. A marginal improvement in house completions, infrastructure-led machinery sectors and the renewable energy sector should outweigh the slowdown in power grid infrastructure and the traditional vehicles sector.

Mine supply growth is set to increase although uncertainty persists with mine operations down in

South America. Currently, the disruption rate is still forecast to stay above-trend. The risk is also rising on the smelting side as a result of the declining TC/RC, which has yet to stabilise. The recent news report of a Chinese copper smelter filing for bankruptcy, though later denied, has rung alarm bells about the possibility of a margin squeeze. The smelter side remains crucial to watch next year, but we can't factor this into our calculations immediately. We currently estimate China refined copper production to grow at around 2% YoY in 2019 (global 2.8%) and 1.2% (global 1.2%) in 2020. This still leaves only a small surplus.