

Risk premium pushes aluminium higher

Three major developments in the aluminium market have seen prices top the LME complex, not least rising geopolitical risks in Europe



Three main developments send aluminium price higher

Aluminium is topping the LME base metals complex with the 3M contract gaining around 10% year-to-date as of Friday. And those extended gains come despite a strong dollar this week after a hawkish tilt from the Fed Chair, Jerome Powell at his news conference following the FOMC meeting. Some sizeable inventory outflows have taken the overall on-warrant stocks to 811kt as of Friday (Jan 28), the lowest since 2007. The stock drawdown has been supportive of prices. We think there are three main developments behind the recent aluminium market strength.

First of all, European power prices have still kept those disrupted capacities in western Europe out of the market. Since our last update, there have been more than 610kt capacity losses. The longer these capacities stay shut, the more supply losses we'll get in 2022. Without meaningful demand destructions, the European market balance points to a deeper deficit. While some may be hoping power prices could get better after the heating season, tensions around Ukraine have made things worse so that European buyers are even scrambling for coal for fear of Russian gas supplies being cut off. Another risk is that if the currently elevated power prices become entrenched, producers in the region could have more difficulties securing their power contracts. Subsequently, margin erosions could jeopardise future supply.

The ongoing Russia-Ukraine tensions bring another question: What if sanctions were to be implemented which block Russian aluminium from the market? Recent tightness in the European market has boosted aluminium ingot and billet premium. Like buyers stockpiling coal just in case, some consumers in the aluminium market may opt to secure more aluminium in case of further disruptions, so adding to the tightness. Russia is the world's single largest producer outside of China. The country's main producer, Rusal, ships almost half its products into the European market, including primary foundry alloys, ingots, and other semi-finished products.

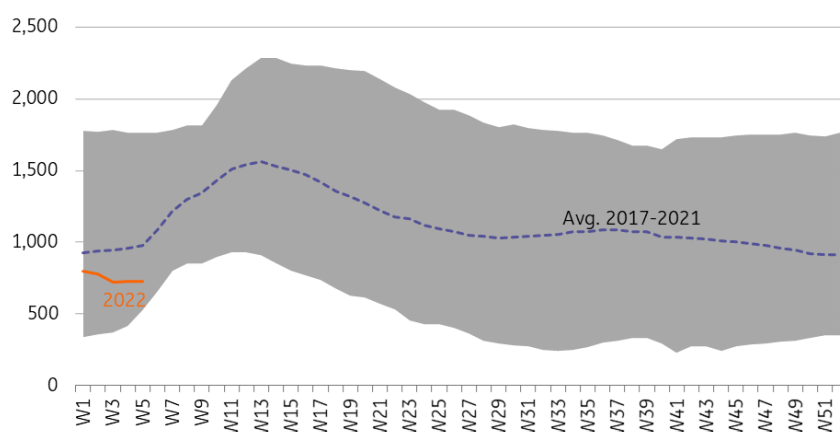
With some producers from western Europe cutting their operations due to the elevated power prices, Russia is the only country in the region that could contribute to additional supply growth in 2022. This is because Russia has just ramped up the Taishet smelter that is set to bring an additional 429kt of aluminium to the market this year, according to the nameplate capacity.

No one knows how the Ukrainian situation will unfold, but the market is pricing in some risk premium on a potential escalation of the geopolitical risk which may further rattle the already stretched aluminium market.

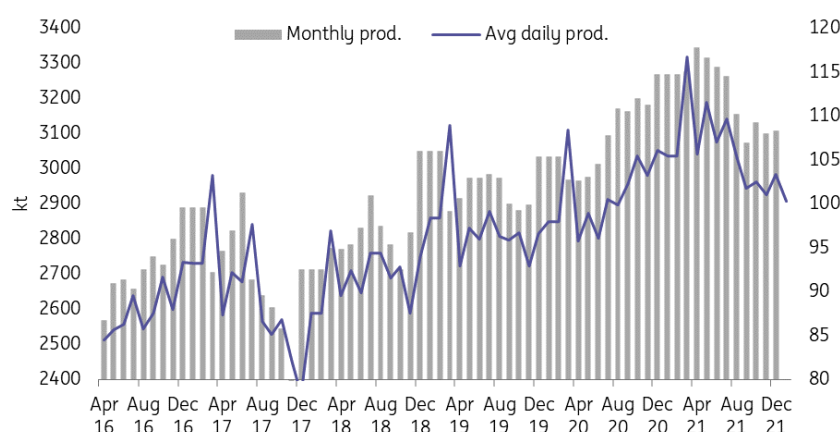
The China onshore market is heading into the holidays without stock building which is unusual, as you can see in the chart below. Historically, there could be some stock building before the Chinese New Year. This is now sitting at 726kt, compared to 714kt the week before the last new year and far below the 980kt average level from the previous five years. This may suggest a constructive picture of the local market as a result of the collapsed operation rates at smelters during the later part of 2021 (see Fig 2) and firm demand.

As Beijing has now shifted towards more pro-growth as they recently announced a slew of both monetary and fiscal measures aimed to boost the economy, we estimate that the Chinese market could see a strong sequential demand recovery post the Winter Olympics. This, compounded with lower inventories, could lead to a stronger price in Shanghai, potentially opening the import arbitrage, which could further accelerate the tightness in the ex-China market.

Fig 1. No stock building before the Chinese New Year



Source: ShFE, ING

Fig 2. Average daily production falls in 2H21

Source: NBS, ING

Still positive, but not without risks in the medium term

Overall, we don't think there's a rising tide lifting all boats for the metals' sector in 2022. Still, aluminium stands out as our top pick among metals with the most upside potential this year, as we examine in our [outlook](#) last December. However, the recent escalation in geopolitical dangers has posted more upside risks to our previous forecast for 1Q22. While we remain overall positive towards aluminium, there are some potential downside risks too. These include but are not limited to:

- The risk premium could dissipate if there were some kind of resolution on the Ukraine front.
- Increasing headwinds on the macro front if we get more aggressive interest rate rises and super-charged balance sheet reductions from the Fed.
- More importantly, the scale and timing of restarts/ramp-ups from China could swing the short-term market balance. Overall, this remains a big uncertainty because the bulk of disrupted capacities last year was due to the 'dual-control' mandate. **The outlook on the scale and timing of restarts/ramp-ups from China is very much dependent on decarbonisation-related policies and how regional governments carry out related works.**

Our base case is that we don't expect all the disrupted capacities to come back this year, and the bulk of restarts/ramp-ups may only return during the latter part of 2022. While we keep monitoring the developments, some rhetorical changes from top Chinese officials over the nation's twin carbon goal are worth paying attention to as these could swing market expectations.

On Monday (Jan 25), Chinese President Xi remarked on the nation's twin-carbon goals. While he continued to stress the importance of the goals, he also admitted that 'it is not something that can be achieved easily'. It is the first time he made it clear that **'emissions' reductions do not mean cutting production'** when carrying out relevant works. This echoes the calls from other Chinese authorities on avoiding 'campaign-style' or 'one-size-fits-all' carbon reductions that had jeopardised economic stability. We think that this may suggest some fine-tuning is on the way to achieving the 'twin-carbon' goals, and there may be less disruption to production when regional governments carry out their decarbonisation-related works this year. If this is the case, we could see larger restarts in aluminium later this year.

Author

Amrita Naik Nimbalkar

Junior Economist, Global Macro

amrita.naik.nimbalkar@ing.com

Alissa Lefebvre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Sector Economist, TMT & Healthcare

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist

samuel.abettan@ing.com

Franziska Biehl

Senior Economist, Germany

Franziska.Marie.Biehl@ing.de

Rebecca Byrne

Senior Editor and Supervisory Analyst

rebecca.byrne@ing.com

Mirjam Bani

Sector Economist, Commercial Real Estate & Public Sector (Netherlands)

mirjam.bani@ing.com

Timothy Rahill

Credit Strategist

timothy.rahill@ing.com

Leszek Kasek

Senior Economist, Poland

leszek.kasek@ing.pl

Oleksiy Soroka, CFA

Senior High Yield Credit Strategist

oleksiy.soroka@ing.com

Antoine Bouvet

Head of European Rates Strategy

antoine.bouvet@ing.com

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Edse Dantuma

Senior Sector Economist, Industry and Healthcare

edse.dantuma@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Rico Luman

Senior Sector Economist, Transport and Logistics

Rico.Luman@ing.com

Jurjen Witteveen

Sector Economist

jurjen.witteveen@ing.com

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Nicholas Mapa

Senior Economist, Philippines

nicholas.antonio.mapa@asia.ing.com

Egor Fedorov

Senior Credit Analyst

egor.fedorov@ing.com

Sebastian Franke

Consumer Economist

sebastian.franke@ing.de

Gerben Hieminga

Senior Sector Economist, Energy

gerben.hieminga@ing.com

Nadège Tillier

Head of Corporates Sector Strategy

nadege.tillier@ing.com

Charlotte de Montpellier

Senior Economist, France and Switzerland

charlotte.de.montpellier@ing.com

Laura Straeter

Behavioural Scientist

+31(0)611172684

laura.Straeter@ing.com

Valentin Tataru

Chief Economist, Romania

valentin.tataru@ing.com

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials

suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research
marieke.blom@ing.com

Raoul Leering
Senior Macro Economist
raoul.leering@ing.com

Maarten Leen
Head of Global IFRS9 ME Scenarios
maarten.leen@ing.com

Maureen Schuller
Head of Financials Sector Strategy
Maureen.Schuller@ing.com

Warren Patterson
Head of Commodities Strategy
Warren.Patterson@asia.ing.com

Rafal Benecki
Chief Economist, Poland
rafal.benecki@ing.pl

Philippe Ledent
Senior Economist, Belgium, Luxembourg
philippe.ledent@ing.com

Peter Virovacz
Senior Economist, Hungary
peter.virovacz@ing.com

Inga Fechner
Senior Economist, Germany, Global Trade
inga.fechner@ing.de

Dimitry Fleming
Senior Data Analyst, Netherlands
Dimitry.Fleming@ing.com

Ciprian Dascalu
Chief Economist, Romania
+40 31 406 8990
ciprian.dascalu@ing.com

Muhammet Mercan
Chief Economist, Turkey
muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content

+44 (0) 207 767 5331

owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM

+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com