

Snap | 6 January 2022

## Aluminium breaks higher on supply constraints

Aluminium supply constraints due to the European power market, risk stemming from the Indonesian coal embargo, and hefty LME cancelled warrants have sent light metal prices to a two-month high



Source: Shutterstock

Industrial metals have mostly entered the new year on a strong footing although trading in the first few days of 2022 has been somewhat mixed. Nickel slipped by more than 2%, whilst supply-constrained metals continue to extend gains, with aluminium outperforming the complex as surging power prices threaten supply and fundamental positivity drives momentum.

The light metal surged by more than 3% on Wednesday (5 Jan) during the London session with the 3M contract touching the highest intraday level, at US\$2,938/tonne - a two-month high, before hawkish Fed minutes dragged the whole complex down on Thursday.

In the meantime, there have been hefty cancellations of LME warrants for three days in a row, primarily from the LME Malaysia warehouse, which could potentially lead to large stock outflows, sparking optimism over strong spot demand. Stocks should have started to build in the China onshore market following seasonal patterns. But instead, these have continued to decline this week to around 790kt as of Thursday, far below the five-year average. This is

helping to soothe concern over a seasonal lull in demand.

As we enter 2022, European producers are still plagued by elevated power costs and there seems to be no sign of a quick solution to the issue. Baseload power prices have surged not only at the front end of the curve but in the long-dated contracts as well. We have seen several producers in the region announce curtailments at the end of 2021, and the risk to supply growth is still tilted to the downside. We have forecast a deficit for the aluminium market in 2022 ([2022 Outlook: Aluminium to slip into a deeper deficit](#)). With low gas storage and high volatility in the gas market, many uncertainties surround the European power market. It would be tough for smelters to secure a competitive power deal in this market.

In Asia, however, the latest Indonesian coal embargo has thrown a curveball to the regional energy markets at the start of the new year, risking supply to its main buyers, including China, India and Japan. The situation there has remained fluid as consumers such as Japan have requested the removal of the ban, and domestic coal miners are [seeking exemptions](#). It is reported that Indonesian authorities held a meeting to review the ban following pushback on Wednesday, but there hasn't been any confirmation at the time of writing. During 4Q21, India managed to avoid a significant impact on aluminium production despite coal inventories falling to critical levels, as their industry association called for expanding coal imports. As for China, the worst impacts from the power crunch in the fourth quarter is now in the rear-view mirror thanks to the authority's strong intervention in boosting domestic coal production. Meanwhile, winter power demand has so far remained in a reasonable range. Yet the Indonesia embargo may have little impact on China in the short term as domestic power plants have plenty of coal stocks at hand to ensure power generation. However, an extended embargo by Indonesia would risk coal shipments to India and a delay to aluminium restarts in China.

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