Copper fate hinges on Chinese demand

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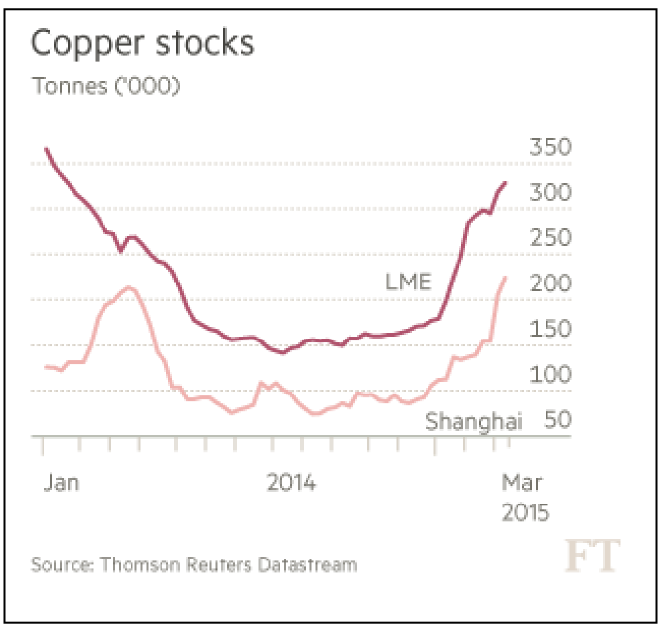
Copper prices have rebounded from five-year lows hit in January, giving a glimmer of hope that the end of Chinese new year could produce renewed demand for the industrial metal in the world's largest consumer.

Yet two weeks after the holiday, signs still have not emerged of a real pick-up in consumption after China's imports of copper fell to their lowest level since 2011 last month.

How strongly demand comes back will indicate whether buyers have just held off on purchases or whether the country's economic slowdown is really starting to eat into sectors that heavily use the metal in wiring, such as property and infrastructure.

While the Chinese central bank cut interest rates this year, there has been no significant sign of stimulus as leaders set the lowest economic growth target since 1999 during annual meetings of its national legislature, which started last week.

Metals analysts and traders have flocked to China since the end of the holiday, in an attempt to gauge the ground conditions — a sign of how critical China is to the global market as a consumer of more than 40 per cent of the metal mined by companies such as Glencore, BHP Billiton and Codelco.



Copper's fortunes depend on the build-out of the electricity grid, as well as wiring used in cars and consumer goods.

Miners also hope that copper will have a future in electric cars, wind turbines and high-efficiency power transformers.

Rio Tinto believes the world will need the equivalent of Chile's Escondida mine — which produces more than 1m tonnes of copper a year — every 15 months to meet global demand over the next 10 years.

Yet the price has belied those optimistic forecasts. Down 25 per cent from last summer, copper plummeted in January on the back of bets made by domestic Chinese funds who saw demand on the ground weakening.

Data from the Shanghai Futures Exchange show that the same funds have not reduced their short positions following the end of the new year holiday.

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> Gayle Berry
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> Analyst at Jefferies

Chaos Ternary Futures, a unit of fund Shanghai Chaos, has built up its short position in the most traded copper futures contract expiring in May, according to data from the exchange, adding 1,242 lots on Monday. It first bought the position in February, the data show.

The fund made its first appearance shorting copper at the end of November, according to Macquarie.

Jinrui Futures, a unit of Jiangxi Copper, China's biggest copper producer, has the biggest long position in the May futures contract, though it has started adding short positions after the sharp fall in the copper price in January.

"People are still pessimistic about copper," says Li Chunlan, an analyst at consultancy CRU in Beijing. "When they talk to downstream users, they are not seeing good sentiment now."

Stockpiles of the red metal have been piling up at warehouses. Stocks in Chinese warehouses monitored by the Shanghai Futures Exchange have doubled to 224,000 tonnes this year, suggesting lacklustre demand.

Domestic premiums to obtain spot metal have also tended towards a discount, according to consultancy CRU.

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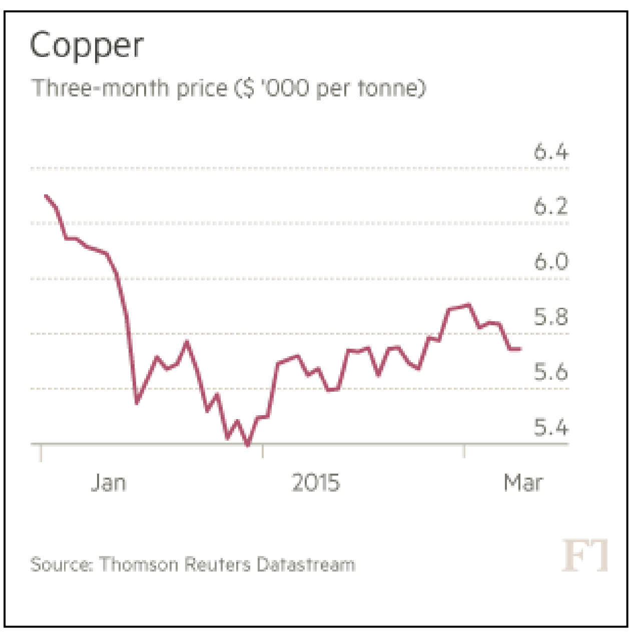

Copper has also been flowing into warehouses outside China monitored by the London Metal Exchange. These could double before the summer, according to Société Générale, as traders unload material.

While it is not unusual for stocks to build after the Chinese holiday, a further build this week would suggest the market is saturated, Jefferies says.

The world's largest miners whose fortunes depend on copper remain optimistic, however.

While there was a void in Chinese buying from the middle of December until February due to tighter credit and a seasonally later holiday, signs are emerging that it has picked up again, Glencore, the Swiss-based resources group, told investors this month.

Ivan Glasenberg, chief executive, says: "We do believe we are transforming into a deficit on copper. That is based on demand still being there. Chinese growth still being there.

"And the big question is will the supply be as big as people are stating it is. And as we've seen, there have been a lot of surprises on the negative on the supply side where expectations are not where they're going to be."

Unlike other commodities such as iron ore, the world's largest copper miners have been cutting their production forecasts this year due to disruptions from strikes or engineering issues. Further problems could support copper prices if Chinese demand weakens.

Robin Bhar, an analyst at Société Générale, says: "Copper still has downside risk with rising supply and still weak demand. But the 64 million dollar question is whether Chinese physical buying is going to increase."