

Covid 19 corollaries

October 29, 2020

Export salve for aluminium

Indian aluminium manufacturers have exports to thank for offsetting a sharp decline in domestic offtake this fiscal.

On the domestic front, primary aluminium demand is estimated to have plunged 45-50% on-year in the first quarter following the nationwide and local lockdowns to contain the Covid-19 pandemic. The resultant economic contraction, labour shortage, and logistic disruptions affected key demand segments – power, construction and automobiles – which account for over three-fourths of the demand pie.

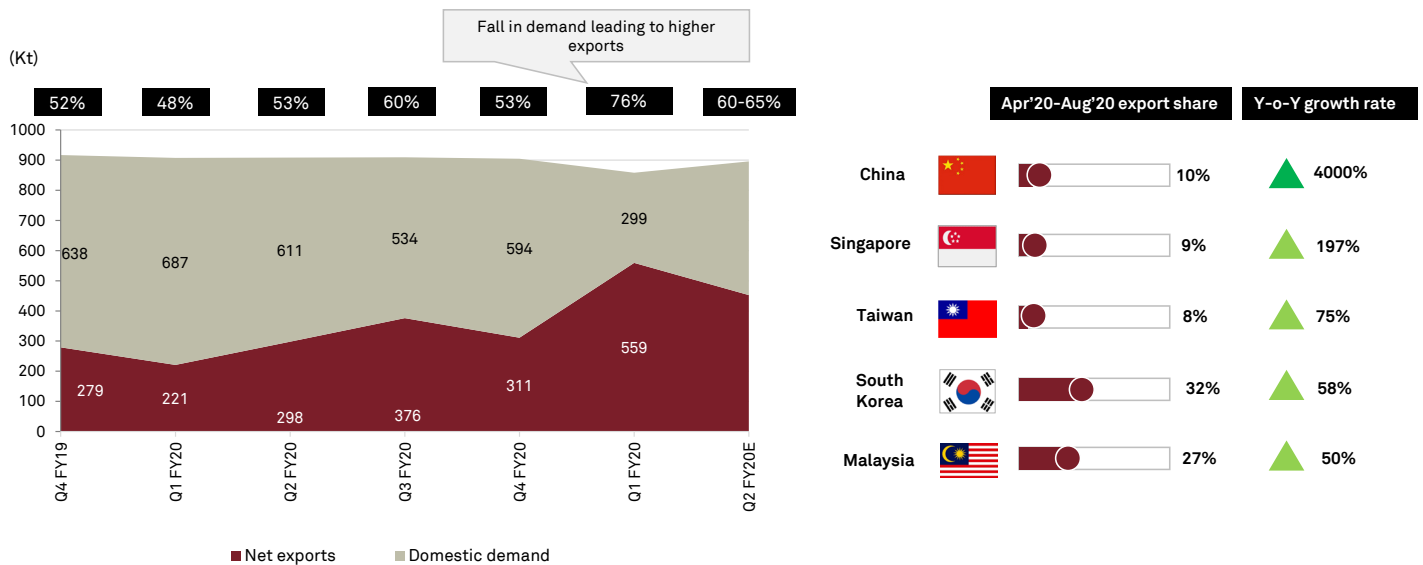
Yet, primary aluminium production being a continuous process, and categorised under essential services, most smelters were operational during the entire lockdown period. To be sure, India's primary aluminium production fell just 5% on-year during the quarter, with utilisation levels largely unchanged.

Exports ensured inventory management of the domestic surplus. Primary aluminium exports rose ~50% on-year in the first quarter and constituted over 75% of total primary aluminium production as against 48% in the same quarter of last fiscal.

Among the destinations, exports surged to countries that have had early success in containing the pandemic, such as China, South Korea and Malaysia.

Exports to China rose a massive 4500% on-year over a low base. In fact, the sharp rise in exports to China saw its share in India's primary aluminium export basket expand to 10% in the first quarter of fiscal 2021 from a mere ~0.5% in the same period last fiscal.

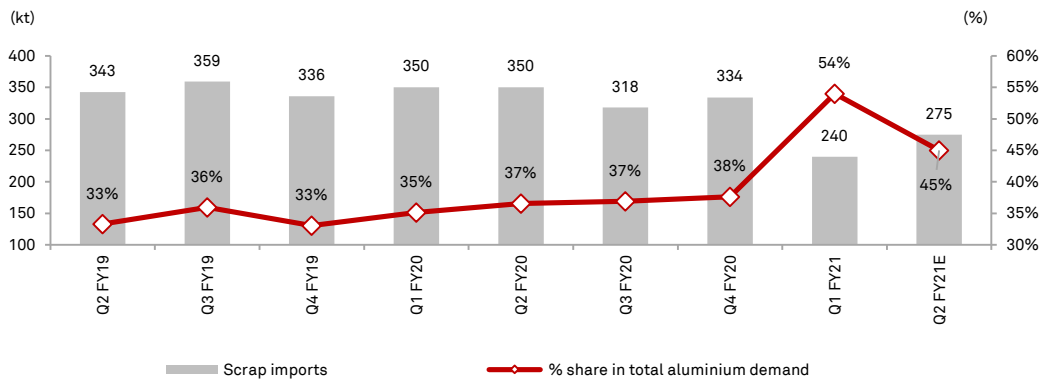
Over three-fourths of primary aluminium produced was exported in the first quarter



E: Estimated
Note: Black bars on top indicate exports as percentage of primary aluminium production
Source: DGFT, company reports, CRISIL Research

Primary aluminium exports began rising from the second half of fiscal 2020, when China imposed a ban on scrap imports.

Share of scrap imports rose marginally last fiscal following Chinese ban



E: Estimated

Note: % share is out of total demand

Source: DGFT, company reports, CRISIL Research

Following the ban, excess scrap in global markets is being redirected to India, leading to surge in scrap imports and increased scrap blending, further straining the already weak domestic demand for primary aluminium. This is likely to continue to spur exports by primary aluminium manufacturers.

Nevertheless, as economic activity picks up in the second half of the fiscal, demand for primary aluminium is expected to improve. Hence, the decline is projected to more than halve from the plunge estimated in the first quarter, at 15-20% on-year.

Elevated prices to ensure primary aluminium makers keep smelters fired up

Domestic primary aluminium manufacturers will also benefit from rising aluminium prices, apart from the rising exports.

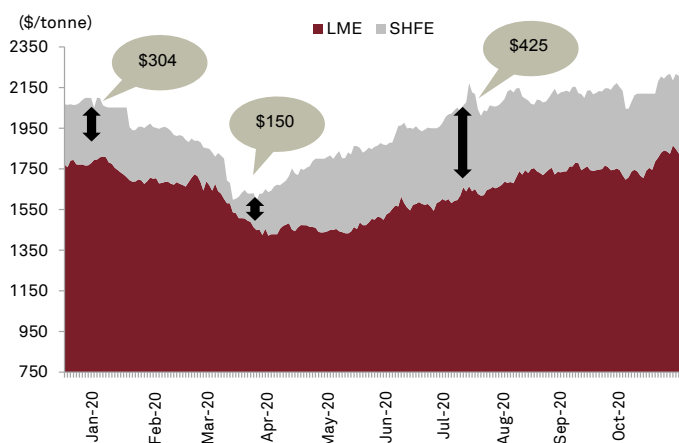
Between January and May, the pandemic led to aluminium LME prices falling 18% to \$1,450 per tonne. Since then, however, a rebound in China’s economy, spurred by government spending, has led to global aluminium prices rising sharply.

The price arbitrage between the LME and the Shanghai Metal Index (SHFE), which reached ~\$425 per tonne in July from ~\$150 in April 2020, also drove up LME prices.

The upshot? In September, prices soared to \$1,750 per tonne, and further to \$1,850 per tonne in October.

With demand reviving in other major economies such as the US and Japan as well, LME prices are projected to sustain at \$1650-\$1750 per tonne this fiscal.

Aluminium LME prices exceed pre-Covid-19 levels

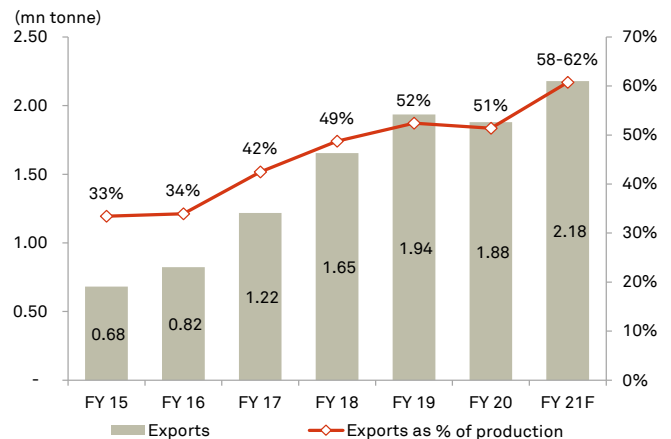


F: Forecast

Note: Callouts indicate price difference between LME and SHFE prices

Source: DGFT, company reports, CRISIL Research

Export share of primary aluminium production to touch 60% in FY21



Thus, although exports have fetched lower realisations historically, domestic primary aluminium manufacturers are likely to continue tapping the export market in the near term owing to elevated metal prices and a weak rupee. This should help offset weak domestic demand.