

H2 2013 Thermal market review – A supply response at last

By Mark Gresswell

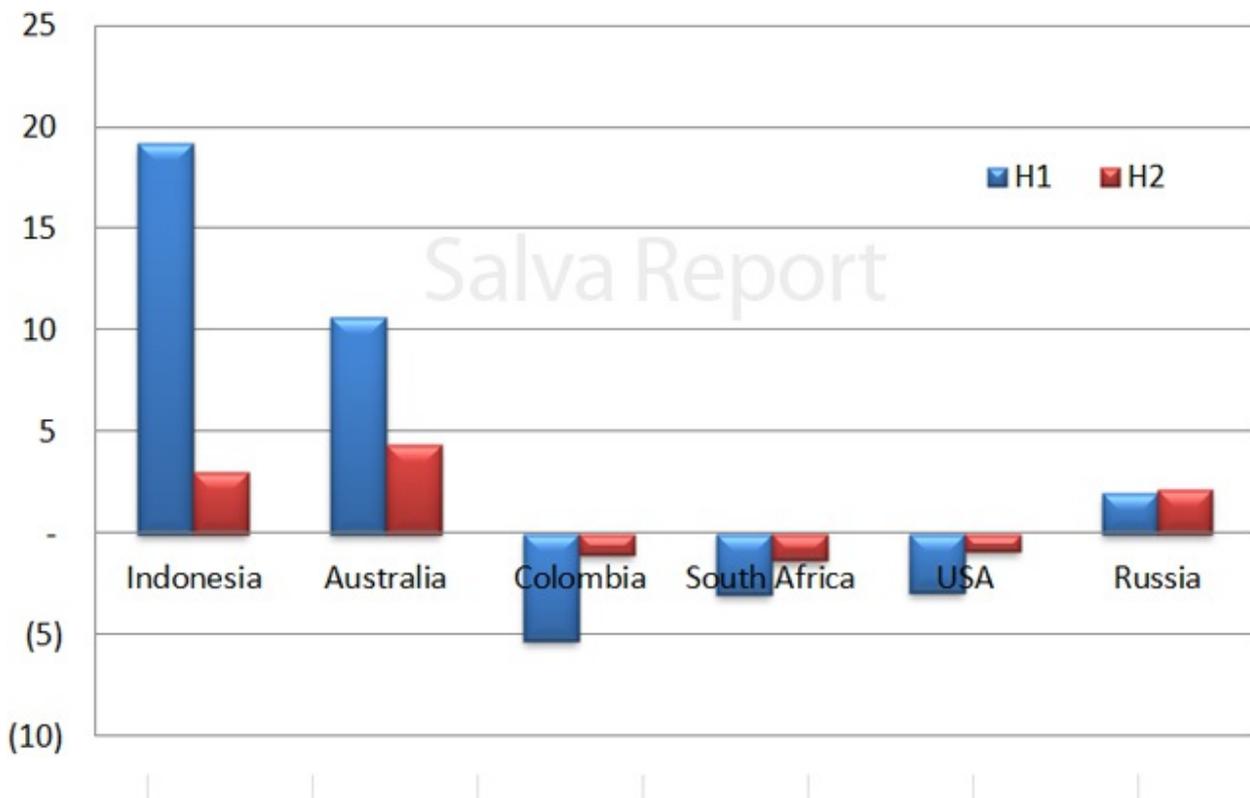
A long-overdue easing of supply growth in H2 2013 has provided some relief for thermal coal markets, with prices rising around 8% from their lows in July. Supply growth out of Indonesia and Australia, which led the charge in H1, slowed noticeably in H2 (see chart below). When combined with sluggish supply from the USA and Colombia and steady demand, markets were able to rise from their lows – although still not firing by any means.

While the market remains oversupplied and prices are still weak, other positive signs are emerging, with mergers and acquisition activity picking up recently, especially in the USA and Australia. This may well signal the bottom of the market, as many of the buyers in these transactions are existing suppliers to the market and therefore see potential upside.

Supply Highlights

Supply growth by exporters is illustrated below for each half of 2013. Note that not all H2 figures are for the entire half (not yet available), but generally very close.

2013 Export Growth (Mt, yoy)



Indonesia

- Flooded the market in H1 with 204Mt, but export growth slowed markedly since;
- Salva figures for October and November both show a decline from 2012 levels;
- Indonesian exports will still be over 400Mt for the year;

- Indonesian suppliers are not immune to weak international markets, and particularly to slowing demand from their major customers, China and India, which happened in H2.

Australia

- Export growth also eased in H2, as in Salva's view, producers have squeezed as much as they can from existing assets to reduce per unit costs;
- Australian exports will still be around 184Mt for 2013, up from 171Mt in 2012;
- Most expansions are now operating at or near nameplate capacity;
- The Australian dollar has eased from US\$1.06 to around US\$0.90, providing a helpful buffer to producers.

Colombia

- Despite a strong November, Colombian exports for 2013 will be 6-7Mt lower than the 2012 performance of 80Mt.
- Strikes and infrastructure hurdles were the main causes of this;
- Drummond exports have been halted in early 2014 due to regulatory issues.

South Africa

- Exports have been erratic, but mostly trailed 2012 levels through 2013;
- Final 2013 exports will be 4-5Mt lower than the 2012 levels of 76Mt;
- South Africa is struggling due to its geographic location which makes it a marginal supplier into both Asia (ex-India) and Europe.

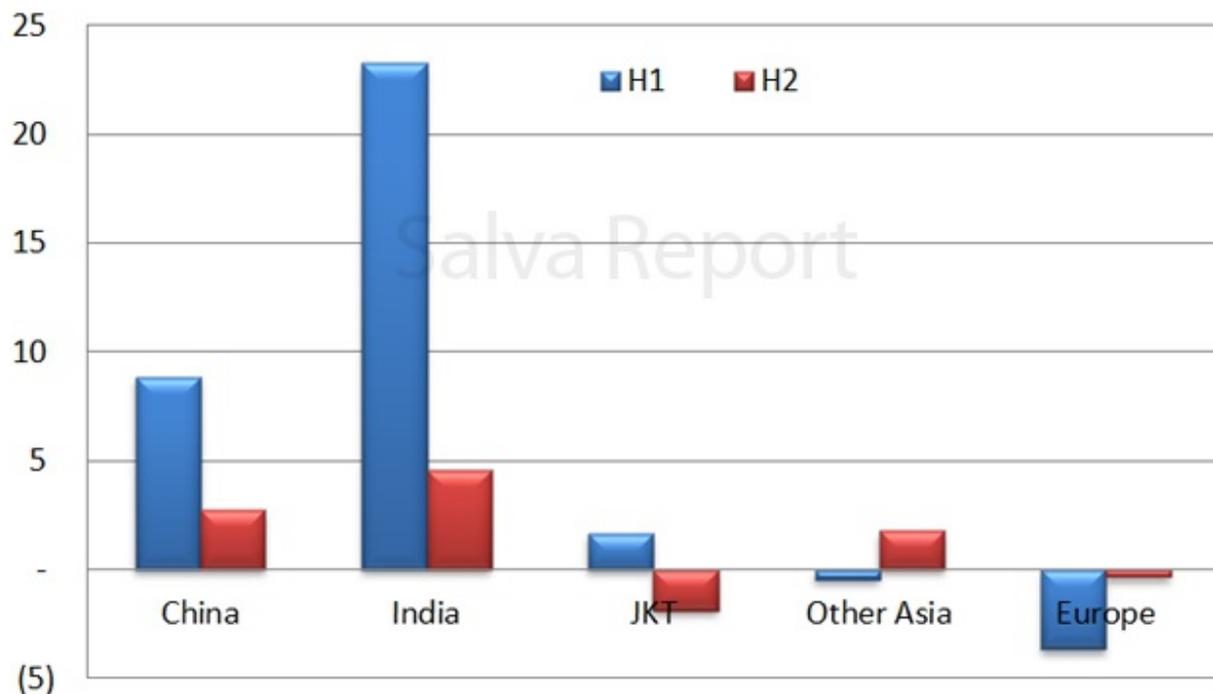
USA

- Exports have fallen below 2012 levels since March, and in November fell below 3Mt;
- US production continues to fall, and 2013 output was 80Mt lower than 2011, largely due to the shale gas boom;
- Sluggish markets in Europe and strong competition from Russia have slowed US exports.

Demand Highlights

Globally, import demand growth slowed in H2, although to be fair, H1 was never particularly strong outside of India and to a lesser extent China (see chart below). This was due to a range of factors including weak currency (India), coal generation already operating at full capacity (Japan, Korea) and strong hydro performance (southern Europe, India).

2013 Import Growth (Mt, yoy)



China

- Despite growing domestic production (up 6%), imports have also grown;
- Weak international prices have meant imports competed strongly into China;
- Power generation growth remains strong, while hydro has eased;
- Chinese imports in 2013 have moved towards higher quality thermal coals, particularly Australian.

India

- India led global import growth in 2013, with imports up to 136Mt from 110Mt in 2012;
- A weak rupee and stronger seasonal hydro generation led to a slowdown in H2
- Coal-fired capacity continues to surge, with Salva figures showing 21GW added in 2013;
- Coal accounted for more than 73% of power generation in 2013, up from 66% in 2011.

Japan – Korea – Taiwan

- Japan's nuclear fleet and some Korean units were almost completely offline during 2013, so coal burn was at very high levels;
- Several Japanese coal units which were sidelined by Fukushima have recently been restarted;
- Korea will implement a \$20/t tax on 1 July, 2014. This will presumably move consumers to higher quality thermal coals as the tax is flat regardless of coal quality;
- All three importers have increased their share of Australian imports, mostly at the expense of Indonesian material.

Europe

- A story of "two Europe's", with the northwest (UK, Germany) increasing imports strongly, while the south (Spain, Italy) dropped volumes sharply;

- Overall volumes for 2013 will be around 3-5Mt lower than 2012;
- Weak coal and carbon prices have shifted coal ahead of gas in the order of merit, so Germany and the UK have taken advantage;
- Hydro performance in southern Europe has been very strong and displaced some coal burn.

Mark Gresswell is the Chief Analyst at Salva Report and is based in our Brisbane Office. Mark can be contacted on mark.gresswell@hdrinc.com.