China FOCUS

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For more information please contact:

Dr Xinmin Hu
xhu@lantaugroup.com

Macro Economy

Prospects for increased economic growth remain uncertain. Preliminary GDP growth in 1H 2013 was 7.6% y-o-y, in line with a non-binding goal of 7.5% for 2013. Data in July show signs of enhanced economic activity, suggesting a reverse of the recent slow-down. Industrial output grew 9.7%, exports and imports grew 5.1% and 10.9% respectively, and manufacturing PMI was 50.3 in July 2013, up from 50.1 in June.

One area of particular concern is mounting local government debts. In June 2013, an audit by the National Audit Office of 36 local governments (which account for 32% of total local government debt) found total debt of ¥3.85 trillion by the end of 2012. If other local governments have a similar situation, total local government debt might amount to ¥12 trillion, or 23% of 2012 GDP. A further review has been ordered by the State Council.

China plans to promote new “pillar industries” as a future driver for economic growth, including the energy conservation and environmental protection industries. China’s first Carbon Emissions Trading Scheme, among the seven approved by NDRC, went into operation in Shenzhen in June this year.

Regulatory Updates

The impact of the re-organisation of the National Energy Administration (NEA) and its responsibilities, the restructuring of approval authorities for energy projects, and the announced 2013 economic reform agenda has become clearer in recent months:

- NEA is assuming the responsibilities of the former SERC in the power sector, with SERC’s regional and provincial offices now under NEA leadership.
- Provincial and local governments have been assigned approval authority for privately funded hydropower projects on non-key rivers, natural gas fired distributed generation, wind power projects, coal-fired back-pressure CHP projects, certain power network projects and oil and natural gas pipelines within provincial boundaries.
- A number of regulations and practices have been abolished in the power sector such as the setting of quotas for market-based electricity, (which have not been used since trials of electricity markets stalled), and direct power purchase agreements between large users and generators. The government’s commitment to market-oriented reforms in the power sector, however, remains unclear.
- NDRC announced for the first time the national benchmark for on-grid prices of ¥0.43/kWh for nuclear power plants commissioned after 1 January 2013.

Power Industry

China (all sectors) consumed 2.496 TWh of electricity in January-June 2013, growing at 5.1% y-o-y, higher than 4.3% in the first quarter. Industry consumption currently accounts for 73.8% and residential use about 12.6% of the total consumption. Primary and tertiary industries account for 1.8% and 11.7% respectively.

As China continues to broil in a persistent heat wave, several provinces registered record high and growing peak loads. Maximum load in July reached 208,500 MW and 83,471 MW in East China Grid and Guangdong respectively. So far there have been no reported black-outs. But some provinces such as Jiangsu have activated the “Orderly Use of Electricity” Plan.

By end-June 2013, China’s total installed generation capacity was 1,142 GW (for plants of size greater than 6 MW). Coal-fired generation capacity currently accounts for about 73.04%, hydro 19.42% and nuclear 1.28%. The capacity factors of all units, hydro and thermal plants are 50%, 35.3% and 55.5%, respectively. Hydro plant capacity factor is high compared to “normal” years due to higher than normal rainfall, which squeezed the utilization hours of coal-fired plants. The total completed investment in the power sector in the first half year was ¥306 billion with network investment 8% higher than investment in generation.

On 24 May 2013, NDRC re-defined end-use categories for retail tariffs. There will be three groups: residential use; agriculture use; and the remainder (including industry, commercial and others). This is the first time that China has linked tariffs with usage characteristics, which will have impacts on some end-users prices.

Fuel Markets

Gas and Oil

China consumed a total of 81.5 billion cubic metres (bcm) of natural gas in Jan-June 2013, up 13.1% y-o-y, on track for 2013 annual consumption to reach 170bcm (compared to 147bcm in 2012). Domestic production increased 9.0% y-o-y to 58.8bcm and imports increased 24.6% to 24.7bcm. Crude oil import dependence was 57% with domestic production at 104mt and import volume at 138mt for the first six months of 2013. CNPC signed an oil and LNG contract with Russia’s Rosneft and Novatek that will supply China with 300,000bbld of crude oil and 3mtpa of LNG respectively from later this decade for over 25 years. This contract is worth around U$270bn at current market price, an unprecedented value for deals of this kind. A natural gas deal for 30 years between CNPC and Russia’s Gazprom might also be closed soon if China’s shale gas development is further delayed.

Effective10th July 2013, NDRC increased the city gate price for pipeline natural gas (both domestic onshore production and imported pipeline gas from Central Asia) across China. Residential gas prices remain unchanged. The national average city gas price will be increased from ¥1.69/m3 to ¥1.95/m3, up by ¥0.26/m3.

Coal

Thermal coal prices at Qinhuangdao Port continued recording fresh lows and were ¥555/mt 5,500kcal/kg NAR in the week ending 14th August , falling 10% from ¥610/mt two months ago. This, together with growing coal imports, hurt most of China’s coal producers, but benefitted China’s coal-fired generators. Domestic coal production dropped 3.7% to 1.79 billion tonnes while net imports increased 14% in January-July 2013. Production reductions mostly hit small-medium non-state-owned coal producers, who at the higher end of cost of production. It was reported that China’s NEA was considering imposing a minimal calorific value for coal imports, which could shield domestic coal producers from overseas competition for low-rank coal. It could also stop or slow down the price fall resulting from weak coal demand growth since 2012. This will increase generation costs for some coal-fired plants in the south and southeast coastal areas. However, the effectiveness and timing of such administrative intervention remains unclear.

Key things to watch: responses to slow economic growth, coal industry performance, and policy details of energy conservation and environmental protection as “pillar industries”.