China's steel exports are falling steeply

- Steelworld Research Team

China's exports of steel product have fallen sharply over the first few months of this year. The January - May total was 34.2 million tonnes, down 26 percent on last year's equivalent figure and the lowest since 2014.

The recent historical comparison for such a dramatic and sustained drop in steel exports was in 2009, when demand in the rest of the world was imploding in the aftermath of the global financial crisis. Is this a sign that China's much hyped capacity closure program is finally starting to bear fruit. The rest of the world's producers would love to think so but the evidence suggests things are a little more complicated. Beijing does target well and it's already way ahead of its goal for steel capacity closures this year.

The problem is that these shut downs have had no discernible impact on steel production. China produced 72.78 million tonnes in April, an all-time record. Production eased very slightly to 72.26 million tonnes in May but that was still the second-highest production month after April. This counterintuitive outcome is down to what exactly has been closed. The initial round of capacity elimination appears to have included a large amount of non-productive capacity, an easy win for producers and local govt. looking to fall into line with the new national policy.

A second focus has been on induction furnace operators. Such producers, using scrap rather than iron ore as their input and frequently accused of manufacturing sub-standard product, are largely unapproved and therefore "illegal" in the eyes of Beijing. For that reason they are also unreported. But quite evidently higher production has not fed into higher exports. Is there some form of voluntary restraint at work here? After all, China has recently been the subject of unprecedented political pressure to rein back its steel exports and trade cases are piling up thick and fast. The European Union has just initiated another set of duties on Chinese steel, these ones on hot-rolled flat products, and the two entities are still dueling over the broader issues of Chinese overcapacity and, in Europe's eyes, over-exports. Meanwhile, the mother of all sanction packages is looming in the United States, where the Trump administration has been investigating steel imports on national security grounds. The so called Section 232 probe is nearly done, according to US officials. China might reasonably be expected to have taken some of the heat out of the diplomatic storm by stemming the flow of exports. How long it can continue doing so is the subject of much debate among analysts. The consensus narrative is that the construction sector will start losing momentum imminently before entering a period of much slower growth over the second half of this year. A caveat to the consensus is that the strength and durability of the 2016 stimulus package have already surprised many commentators. But neither building activity nor those supercharged profit margins are going to run indefinitely. At some stage there will be a slowdown, which will feed quickly into the steel sector, and super quickly if it coincides with seasonal weakness over the coming summer holiday season. Don't expect China's steel producers to adapt supply fast enough. Their track record is poor when it comes to adjusting production to changes in demand tempo. Rather, the pattern has tended to be for demand weakness to lead to falling prices, margin compression and accelerated exports. Current low export levels are first and foremost down to strong domestic demand. If that fades, Beijing's control over its steel sector and those politically toxic export flows is going to be put to the real test.