
Supply concern to keep Zinc prices higher in near term
Expectation of rate cut from Fed and weak economic data to keep gold prices higher

SUPPLY CONCERN TO KEEP ZINC PRICES HIGHER IN NEAR TERM

- ▲ Zinc prices have rallied more than 9% in two weeks from the recent low of \$2290 per ton as LME warehouse inventory continued to drop to the lowest level in two decades amid a variety of supply outages. Cash zinc is trading at a \$41 premium to three-month LME prices which is up from zero during July-September. A rise in premium is suggesting lower availability of metal in the near term.
- ▲ LME warehouse stocks were at 203,650 mt at the start of October 2018, now stand at 59,725 mt in Oct'19, which is a drop of more than 70% in one year. LME Zinc warehouse stocks are near 2-decade lows. Warehouse stocks in SHFE are showing a different trend as inventories increased to 68,560mt from 29,204mt levels for the same period.
- ▲ The global zinc market saw a 106,000-tonne shortfall over January-July, the International Lead and Zinc Study Group (ILZSG) said in a report released this week. The world's zinc mines lifted production by 1.9% in the first half of this year; however, world refined metal production fell by 0.4% over the same period.
- ▲ Refined Zinc production is lower because many smelters are facing outages, except the ones in China. We expect this shortfall to continue further in coming months as many smelters have reported an outage in August, September and October as well.
- ▲ Skorpion smelting unit owned by India's Vedanta will close the refinery for nearly four-month, starting from early November 2019 to end of February 2020. Last year's refined zinc output was 67,000 tonnes from this plant, and four-month closing will lead a shortage of more than 22,000 tonnes.
- ▲ Canada's Teck Resources will lose 20,000-30,000 tonnes of production from its Trail smelter after an electrical equipment failure in August.
- ▲ Canadian Electrolytic Zinc Ltd (CEZ) will produce 15,000 tonnes less than expected this year due to unplanned maintenance in the second quarter. Company is facing "filtration capacity limitations" reported in their quarterly report.
- ▲ Mooresboro refinery in North Carolina which produces 155,000 tonnes of zinc every year is closed since April 2019 after a fire in their plant. This plant could start production only in the first quarter of next year.
- ▲ Russia's Eletrozinc Smelter plant lost annual output of 110,000 tonnes after a devastating fire in October 2018, is not looking to restart production this year.
- ▲ JPMorgan's Quarterly report expected some relief from Chinese smelters and according to their expectation zinc production is set to rise by 6.5% this year. China's output of refined zinc continued to increase and hit a record monthly high in September. Chinese smelters have ramped up raw materials feeding and postponed maintenance to get the benefit of incentives. According to a separate survey report of Shanghai Metals Market (SMM), about 515,700 mt of refined zinc was produced across China in September '19, up 3.3% from August and up 15.43% from September 2018. Production in January-September amounted to 4.25 million mt, up 7.08% from the same period last year.

Outlook

- ▲ World zinc mine supply is unquestionably increasing, and demand undoubtedly is deteriorating due to trade war between US and China. Still, production shortage of refined zinc from many smelters is keeping zinc prices up in short to medium term. The smelter bottleneck could prove much stickier than expected, and more rallies could be seen in zinc prices in the near term unless China reduces some of the supply deficit. We expect supply constraints to continue in the near term and warehouse stock to drop further from the current level to meet demand. Trade negotiations between the US and China could also provide direction to prices as Zinc supply deficit to widen further in the case trade war between US and China settles on a positive note.

EXPECTATION OF RATE CUT FROM FED AND WEAK ECONOMIC DATA TO KEEP GOLD PRICES HIGHER

- US government data showed that new orders for US-made capital goods other than defense equipment fell more than expected in September and shipments also declined. September capital goods orders declined by 0.5% against a forecast of a 0.2% decline. Also, August numbers were revised down by 0.2% to 0.6%. Gold prices rallied after disappointing data.
- US-China tariff war and the slowdown in other economies has clearly affected the business sentiment.
- Weak economic data have increased chances for a rate cut in the upcoming meeting next week. US Federal Reserve has already cut interest rates twice this year. Markets widely expect the Federal Reserve to cut 25bps of the interest rate at the Oct. 29-30 meeting. But eyes are on the Federal Reserve's statement as the market expects a more dovish stance from 'act as appropriate'.
- Uncertainty on Brexit increased after UK Prime Minister Boris Johnson called for a general election on December 12.

Outlook

- Gold prices bounced from the recent low after the US reported weak economic data. Uncertainty increased over Brexit and pushed gold prices higher. There is a high possibility of another rate cut by US Federal reserve in meeting next week by 25 bps, but any change in stance would decide the fate of gold prices. We expect CME Gold future contract to remain positive with support levels around \$1477-1465 per ounce while key resistance levels could be seen around \$1521-1526 per ounce.

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