

## MARKET REPORT

JULY - AUGUST 2018

### ECONOMY

The most significant economic event during this period was the decision of the Bank of England, early in August, to raise the base rate to 0.75%, now above 0.5% for the first time since March 2009. The BoE gave their opinion that the base interest rates will not be above 3% for decades. They expressed concerns that inflation might rise too rapidly. Unemployment is at a 43 year low and wage growth was beginning to accelerate but remains below the inflation rate. There was a backlash from companies, headed by the British Chambers of Commerce and the Institute of Directors, challenging the view that inflation pressures were building. The inflation rate is now at 2.6% but with wage inflation at 2.5% household budgets are coming under pressure. Energy prices for domestic consumers are set to rise again. Not surprisingly most of the High Street banks have ignored the change as far as savers are concerned.

For the three months up to the end of July, surveys have shown a reduced level of confidence among businesses, influenced largely by the trade disputes, particularly between China and USA, into which Europe has been dragged unwillingly, and Brexit uncertainty.

During Q2 2018 the UK economy picked up with better retail sales, better services data and improved construction levels, giving a growth rate of 0.4% for the quarter. But the activity in manufacturing fell during the last month of the quarter, with manufacturing output falling, the second successive quarter fall in the sector, in spite of encouraging export performances. A CBI survey confirmed that investment by businesses is falling, with uncertainty over Brexit.

UK employment levels at 75.7% are now at their highest levels since records began in 1971.

Sterling has fallen during August and now £1 will buy \$1.30 or 1.12 euros. The corresponding figures in our June Market Report were \$1.32 and 1.13 euros. The FTSE 100 is now at 7590 and the FTSE 250 at 20776.

The Eurozone has not been immune to the economic pressures facing the UK, such as the tensions over trade disputes, and the growth rate for Q2 2018 was 0.4%, matching the UK value. Business confidence in the euro zone is also falling over high unemployment and immigration. The forthcoming elections in Sweden may well reflect those concerns.

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## ALUMINIUM

On the LME primary aluminium started July on \$2153 per tonne and during the month slowly sank to \$2061. It fell further in August, at one point, as the US dollar strengthened it was below \$2000, and it ended August on \$2112.

Traders are now paying high billet premiums with uncertainty over deliveries for Q4 2018. This has been the case since April, with US sanctions against Rusal. Metal Bulletin are reporting billet premium of \$520-560 per tonne, duty paid, delivered in the Ruhr, with 30 days payment terms. Italy is paying \$530-570 with 60 days payment. For good quality foundry ingot, for road wheels for example, LM25 and L99, the premium in Germany is quoted at \$420-460, duty paid, 30 days terms. For primary ingot, duty paid, the premium is around \$150-160 duty paid.

Arconic, the aluminium products company spun off from Alcoa, is being pursued by four major private equity funds all keen to buy it. The management of the company are said to be uninterested unless they receive a bid that was too good to refuse. Arconic themselves have put a building products unit up for sale that provided the external cladding that was used on the Grenfell Tower in Kensington.

Alcoa reported earnings for Q2 2018 of \$904 million before tax, interest and depreciation, up 38% on Q1 2018. They achieved higher alumina and aluminium prices but were also hit adversely by higher energy and raw material costs.

Hindalco Novelis is about to close on a deal to buy Aleris Corp which is at present owned by private equity companies. The price is said to be in the \$2.3 – 2.5 billion range.

## AUTOMOTIVE

For the first half of 2018, UK car manufacturing was down on H1 2017 by 3%. For home consumption the production was 13% down on last year but for the more significant export market deliveries were down by less than 1%.

The SMMT data for car manufacturing in July 2018 is now available and the month has been disappointing. The total of cars manufactured in July 2018, at 121,051, was down on July 2017 by 11%. For the home market the fall was a drastic 35% and for export a more reasonable figure, but still a fall, of 4%. For the year-to-date the total production at 955,453 is 4% down on this time last year.

The SMMT data for new car registrations for July 2018 confirms that the industry is holding its own with sales, even as the economy has slowed recently. The total for July 2018, at 163,898 vehicles registered, is 1.2% up on July 2017. Registration of diesels continues to fall and today accounts for 32% of the total sales. Last year it was 43%. The market share of AFV creeps up, now at 6.5%. But looking at the year-to-date 2018 is still trailing 2017 by 5%.

Ford dominate the new car registrations with three places in the top ten, 1<sup>st</sup>, 4<sup>th</sup> and 8<sup>th</sup>. Of the UK produced cars Nissan Qashqai are 3<sup>rd</sup> Vauxhall Corsa 5<sup>th</sup> and MINI 7<sup>th</sup>.

In July the government published their “Road to Zero” strategy, with plans to position the UK as a leader of design, manufacture and adoption of zero and low emission vehicles. Included was the understanding that the internal combustion engine, including diesel, will continue to have a role to play in the future. The industry view from SMMT however is that the government’s future targets for low and zero emission vehicles by 2030 are too ambitious. Manufacturers and parts suppliers for diesel engines are now in a very difficult position.

Manufacturers across Europe are struggling with new testing procedures to measure emissions. The new system becomes compulsory in September 2018. Some manufacturers have withdrawn models from the market while testing is still being carried out, Peugeot 308 GTI for example. Other companies are not fulfilling orders placed today for new cars until November. VW for example are delaying manufacture of up to 250,000 vehicles in the second half of this year while the test results are awaited. Since some parts of the industry have been caught in the past with their hands in the till, it can’t come as a surprise.

In Q2 2018 Jaguar Land Rover made a pre-tax loss of £264 million, blaming Chinese concerns over trade, uncertainty over Brexit and the moves against diesel engines; what could be described as the automotive industry’s “perfect storm” Shares in the company on the Bombay and New York stock exchanges fell. The company expects that sales this year will recover and they remain committed to roll out their electric vehicles such as the 1-Pace, their first all-electric car.

Questions still remain over the future of the Vauxhall plant at Ellesmere Port which now only assembles the Astra. This model will be wound down from 2021. The Groupe PSA, owners of Peugeot and Citroen, are due to make an announcement on their future electric cars before the Paris Motor Show which opens at the end of September. There are hopes that Ellesmere Port could be chosen as the preferred site for Vauxhall electric cars. The UK government has lobbied PSA on behalf of Ellesmere Port, pointing out that they expect the UK to play a major role in electric and hybrid vehicles, with Nissan in Sunderland, Geely in Coventry and MINI in Oxford already committed to electrics and hybrids production.

Dyson intend to build ten miles of test track in the Cotswolds for testing electric cars. They are investing £2 billion to develop electric cars. The company announce last year that they have secretly been researching battery electric vehicles for the past three years.

Aston Martin are setting up a flotation of £5 billion on the London stock Exchange and will be increasing production of sports cars, 20% up this year and a further 50% up within two years. They plan to re-introduce the Lagonda marque, with an all-electric car to match Rolls-Royce and Bentley. They expect that their new plant in South Wales will take production up to 14,000 cars per year.

Ford globally, and Ford Europe in particular, are in sever problems. During the three months this year of April, May and June Ford Europe lost \$73 million. Their models are said to be dated and they are suffering over the move away from diesel. They may concentrate on SUVs. Globally they employ 200,000 people and cuts in the workforce are envisaged of up to 12% and most of these are likely to be in Europe. Ford cars for Europe are built in

Germany and Spain and this is likely to be where most of the cuts will fall. But Ford employs 12,000 in the UK, with major production units at their engine plants in Bridgend and Dagenham. The Ford Mondeo is particularly scheduled to be taken out of production, but looking at UK sales, with Ford taking three places in the top ten, the Mondeo is not one of them.

## **AEROSPACE**

The world's big three for airshows these days are Paris, Dubai and Farnborough, each held every other year. This year it was the turn of Farnborough in July. The show received little publicity outside of the aerospace industry and in the event, it was described as lackluster. Never-the-less Airbus and Boeing continued their duopoly, with a total of about 1100 passenger and freight aircraft ordered. Boeing took the lion's share, announcing 673 orders and Airbus 431 aircraft; in both cases exceeding the orders placed at last year's Paris Airshow. None of these figures caused any surprise since discussions had gone on prior to the show months ago.

At the show it had been expected that Boeing would unveil their new Boeing 797, which is designed to fit somewhere between a single-aisle 737 and a wide-body 787. But it's still under wraps. What is becoming key to the future is the relationship between on the one hand Boeing with Embraer and on the other hand between Airbus with Bombardier. The A380 has not been the big success that Airbus had expected due to its size and lack of flexibility. The competition is now for the smaller, more flexible planes, originally coming from Embraer and Bombardier, now both tying up with much larger companies.

Airbus is firming up on plans to assume control of the Bombardier C Series and they plan to build up to four each month at their plant in Alabama, where they already have an Airbus facility. Boeing and Embraer are still working on the detail of their \$4.75 billion partnership, particularly with the Embraer E2.

Boeing and Airbus are not the only players in the UK aerospace sector and there was good news this month for Cobham, the UK's third largest aerospace and defence group. Their dispute with Boeing over payments for work on an aerial tanker aircraft, the KC-46 Pegasus, continues but the company have an order book worth £1 billion. Around the world Cobham employ 10,000 people.

## **BUILDING AND CONSTRUCTION**

If the last winter was bad news for the building and construction sector then this Summer has been a godsend. In July construction buyers were busier than they have been for a long time and there was the largest rise in industry employment levels since December 2015. For July the Markit/CIPS PMI Index for construction registered 55.8 against 53.1 in June, the fastest turn around since May 2017. The pundits had predicted 52.8 for July. House building was the best performing sector, with commercial projects at their highest level for over two years. In civil engineering, construction orders are not keeping pace with the rate at which projects have been completed.

The July Index across the whole of the EU for construction shows the UK with the highest Index level for any country, Germany 50.0, France 48.2, Italy 53.3. The Index averaged across the whole of the EU was recorded as 50.3.

## **PACKAGING**

Although the government has pledged to introduce a deposit return scheme for drinks containers it has not yet made any announcement on how the scheme will work. However, some UK supermarkets have already installed reverse vending machines for plastic bottles and aluminium cans at test sites for a six-month period. The machines give customers a 10p voucher to spend in the shop for each plastic bottle or aluminium can they return. One supermarket is capping the total of containers returned by any one customer to 20 per day to discourage people from arriving with containers collected from the surrounding area. Another supermarket is only taking bottles bought from their own store and cans are not included in their scheme.

The Ardagh Group is a major global player in metal and glass products, with 108 plants in 22 countries, 10 of which are in UK. They recently acquired a beverage can business and in early 2017 they announced that their Rugby plant, producing steel beverage cans, will be converted to an aluminium can business. That conversion is now completed. They also have an aluminium beverage can production unit at Wrexham.

## **ENERGY GENERATION**

EDF, building the UK's first nuclear station in a generation, are facing a further set-back with their similar design station in France at Flamanville, where defective welding in the section that takes the steam to the generator will have to be repaired. The start up date at Flamanville is now ten years later than expected and the cost is already three times the original estimate. EDF insist that Hinkley Point C can be up and running by 2025, having learnt from their experiences with the French plant. The Hinkley Point plant is being heavily subsidized by the UK government but the General Court of the European Union has ruled that there is no infringement of state aid rules.

Adding to the concerns over nuclear stations the plant planned for Moorside in Cumbria is likely to be abandoned if a buyer is not found urgently. Toshiba, the owners, bought into this project in 2014 with plans to use Westinghouse designs. Westinghouse themselves faced increasing costs for a nuclear station in USA which bankrupted the company, leaving Toshiba holding the parcel when the music stopped. Hopes of a South Korean company coming in with their own design failed when the UK government refused to offer similar terms enjoyed by EDF at Hinkley Point.

Ineos have been granted planning permission for a shale gas exploration well in Derbyshire. They have not yet applied for permission for fracking there, waiting to see the results of the test well. Their application for the test well bypassed the Derbyshire County Council who were known to be opposed.

In Lancashire Cuadrilla have been given permission from the government to begin fracking near Blackpool. It had been halted there in 2011 when minor earthquakes gave cause for concern. It is not commonly known that the UK is subjected constantly to a stream of minor earthquakes, which generally pass without notice. Friends of the Earth remain unconvinced.

Oil prices are now around \$76 per barrel for Brent Crude. The higher prices in recent months has meant that in Q2 2018 BP's profits trebled to \$1.8 billion. There is a view that oil prices will remain relatively high because there is a shortage of capacity, particularly since Russia and Saudi Arabia increased their production. On the other hand, tension between China and USA could result in reduced demand for oil.

### **OTHER MATERIALS**

RTZ has struck a deal to sell its interest in the world's second largest copper mine for \$3.5 billion. The Grasberg mine in Indonesia is also the world's largest goldmine. The investment has been contentious for RTZ investors, not least because of the poor safety performance. The buyer is the state-owned mining company Inalum. Indonesia is about to introduce legislation that means that the state must hold the majority share of mining companies.

Copper on the LME is now selling at around \$5980 per tonne and in recent weeks it has fallen steadily from the early June value of \$6990.

### **ALUMINIUM FEDERATION 31 AUGUST 2018**