

FIS Capesize v Panamax Q121

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CAPE v PMX Q1 21 Below 5 Year Average

Synopsis

The Capesize Q1 21 versus the Panamax Q1 21 seasonality spread is currently USD 2,000 below its 5 year average value. Historically the spread will narrow into January with a 5-year average valuation of USD 887 by Jan 31st. However, average values tend to remain above the USD 1,500 level into the new year. It is worth noting that the current 3-year average valuation is currently USD 3,000 higher with the Jan 31st price at USD 1,167.

With Iron ore futures maintaining a bullish trend on the back of rising imports (up 11% in the Jan—Aug period) and a strong economic recovery in China, the Cape v's Pmx spread continues to trade near a flat ratio level, suggesting that it is underperforming. In part this is due to the strong Panamax numbers on the back of agricultural imports into China from the U.S. phase 1 trade agreement.

However, the Q1 cape numbers are USD 1,600 below its 5-year average values, indicating the lag in the spread is coming more from the Capesize underperforming rather than an a strong overperformance in the Panamax.

The Caixin manufacturing Purchasing Managers Index (PMI) has shown a sharp recovery. Having dropped sharply earlier in the year at the COVID-19 peak, the robust recovery is seeing the highest PMI figures in over three years. Just based on a simple observational view, the falling Capesize index is going against the Chinese economic trend which at above 50 is expanding.

Monthly Capesize index with Caixin PMI

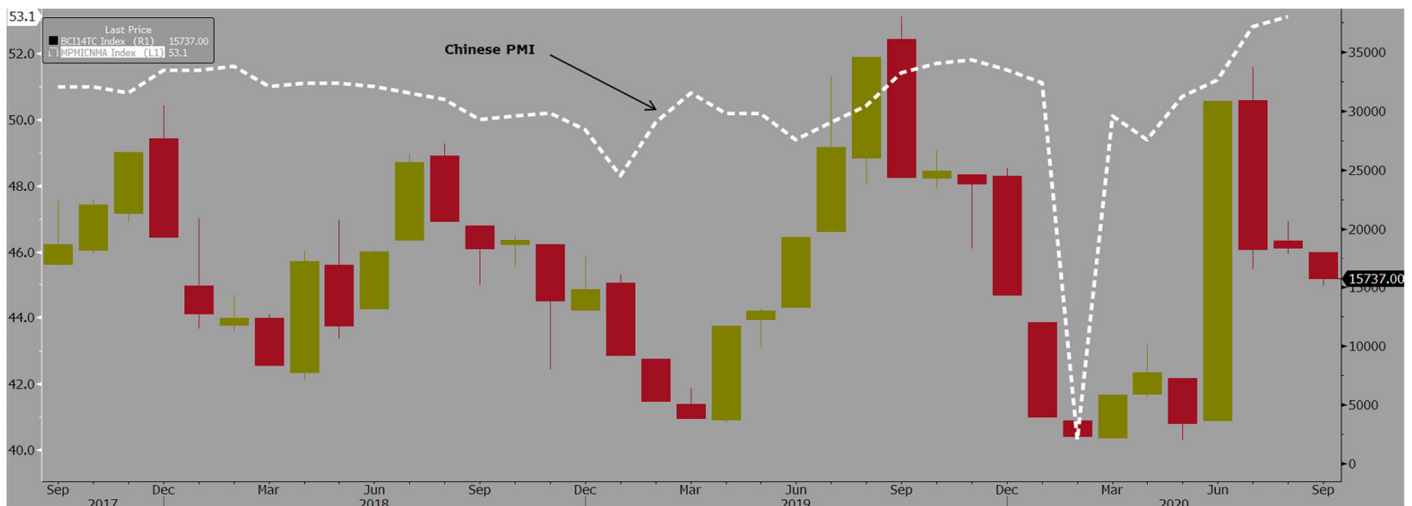


Chart Source Bloomberg

If Chinese economic data continue to perform and iron ore imports continue to rise, then there is an argument that we should see some form of mean reversion to the 5-year average value (and potentially the 3-year average) on the Q1 Capesize and therefore the Capesize v Panamax spread.

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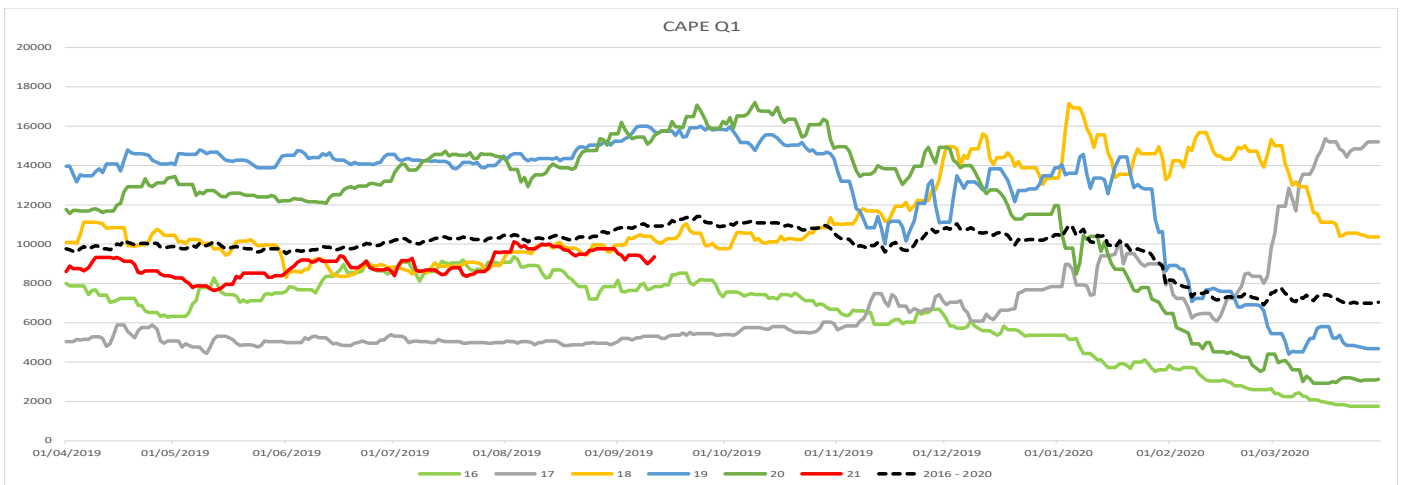
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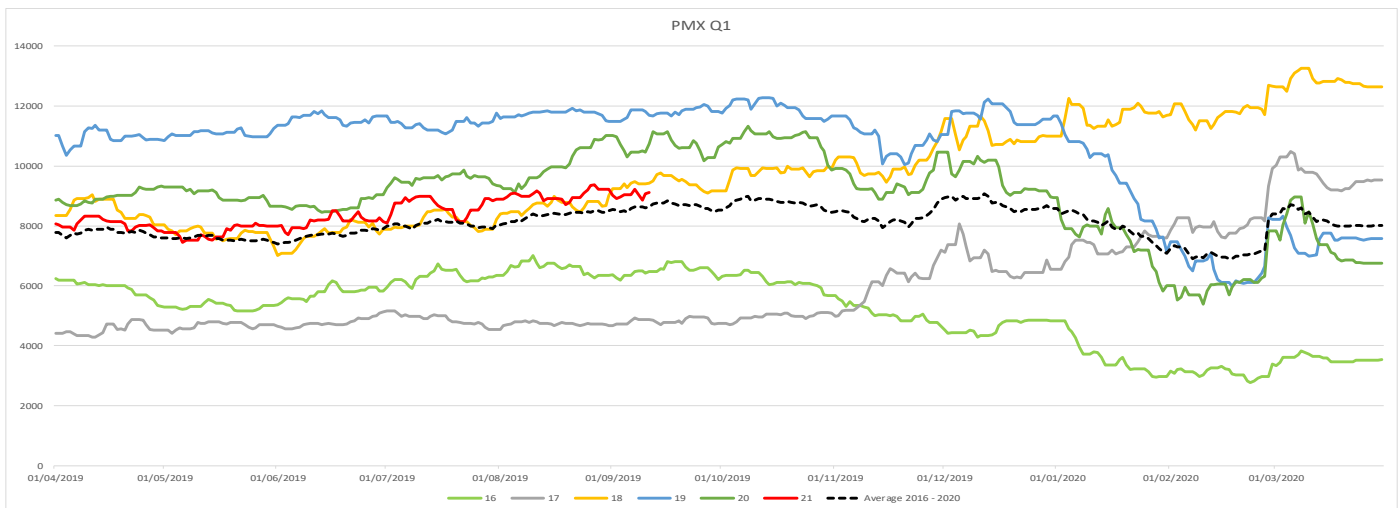
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The charts below illustrate the undervaluation in the Capesize market and slight over valuation of the Panamax. The situation for Panamaxes is a little different. Yes there is an agreement to purchase agricultural goods from the U.S., but ultimately there is a need to import these goods to feed livestock and humans alike. It just means that China is importing from North America as well as South, this would explain why prices are closer to their mean valuations compared to the Capesize Q1.

Capesize Q1 below the 5 year Average value



Panamax Q1 slightly above the 5 year average value



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The final chart is of the spread itself. We can see the valuation is below the 5-year average. We can also see that 2019 and 2020 put in strong performances with the spread. Last year it was scrubbers being fitted that kept the futures pricing high, this year we have economic expansion and high steel demand pushing iron ore higher.

The expanding PMI and the undervaluation of the Q1 21 futures would suggest that something has to change. At this point it would seem the logical that the futures will start playing catch up rather than the world's second largest economy taking its foot off the pedal.

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