



COMMODITIES UPDATE

The slump in the Baltic Dry Index is all about iron ore

- **Some commentators have pointed to the slump in the Baltic Dry Index as a sign that shipping bottlenecks are easing. But we think it is more a symptom of lower Chinese steel output and plunging iron ore prices.**
- The Baltic Dry Index (BDI) is a composite measure of the cost of shipping dry bulk commodities, such as coal, iron ore and grains, by sea. It is sometimes credited with being a bellwether for global economic activity, but we view it more simply as an indicator of the demand and supply of commodity cargo ships.
- After tripling since the start of the year, the BDI has now fallen by just over 50% since its early-October peak. However, **the decline in the BDI has not been mirrored in other shipping cost indices.** Container shipping costs have dipped recently, but they remain historically very high. (See Chart 1.)
- Instead, **we think the drop in the BDI is related to the recent plunge in the price of iron ore** (see Chart 2) which is, in turn, a reflection of the sharp drop in China's steel production. Iron ore typically accounts for around 20-30% of the dry bulk trade and China consumes around 2/3 of the world's seaborne iron ore.
- In recent months, **China's steel production has been falling** (see Chart 3) and it was down by 23% y/y in October. Of course, some of the decline last month was rooted in power rationing (see [here](#)), but **given that the government is keen to curb steel output more generally, we are not expecting a marked rebound.**
- For now, China's iron ore imports have held up relatively well given the downturn in steel production, but stocks at ports are rising and we think it is just a matter of time before imports plunge. Regardless, **Chart 4 suggests that the BDI has further to fall even at current import levels.**
- So, **if the BDI continues to slump, it should not be seen as a sign that global logistics are improving or that supply chain bottlenecks are easing,** it will merely reflect weakness in China's commodity demand.

Chart 1: Freight Indices (1st Jan. 2020 = 100)

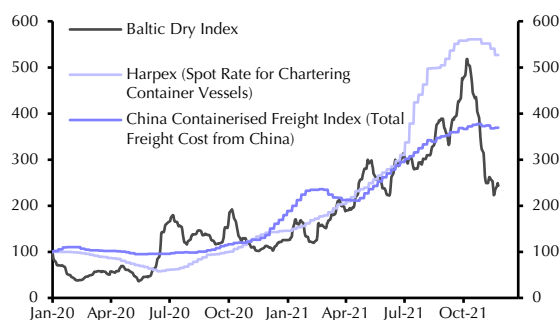


Chart 2: Baltic Dry Index & Iron Ore Price

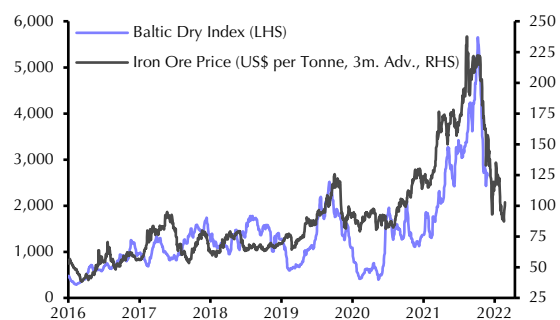


Chart 3: China Steel Prod. & Iron Ore Price (% y/y)

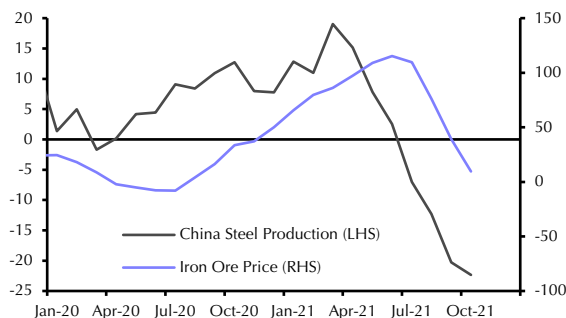
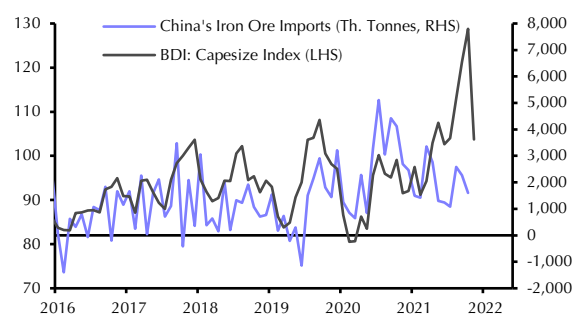


Chart 4: China Iron Ore Imports & Baltic Dry Index



Sources: Refinitiv, WSA, Capital Economics



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