



## >The "*Canadian Problem*" & Why the MW Premium Could Spike

US MW Premium Alert & Special Analysis

June 23, 2020

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## The “*Canadian Problem*” and Why the MW Premium Could Spike

- As anticipated by HARBOR, there are rising odds the Trump Administration may reimpose the 10% Section 232 Tariff on Canada or a hard quota on its aluminum exports to the US in order to “fix” the “*Canadian Problem*”. The final decision could be announced as soon as this week and implemented the week after. If confirmed, this would be very bullish for the MW premium.
- However, there is still some confusion among some market participants regarding the “*Canadian Problem*”, its “fix” and its potential impact on the MW premium.
- The noise seems to come from the debate between two sides: a) one US aluminum association (APAA) which is led by two US smelting companies, and b) two other associations which are both led by Canadian aluminum producers, the AA (a US aluminum association) and the AAC (a Canadian aluminum association).
- In this context, HARBOR has identified 7 key questions and answered them with empirical evidence and independent analysis.

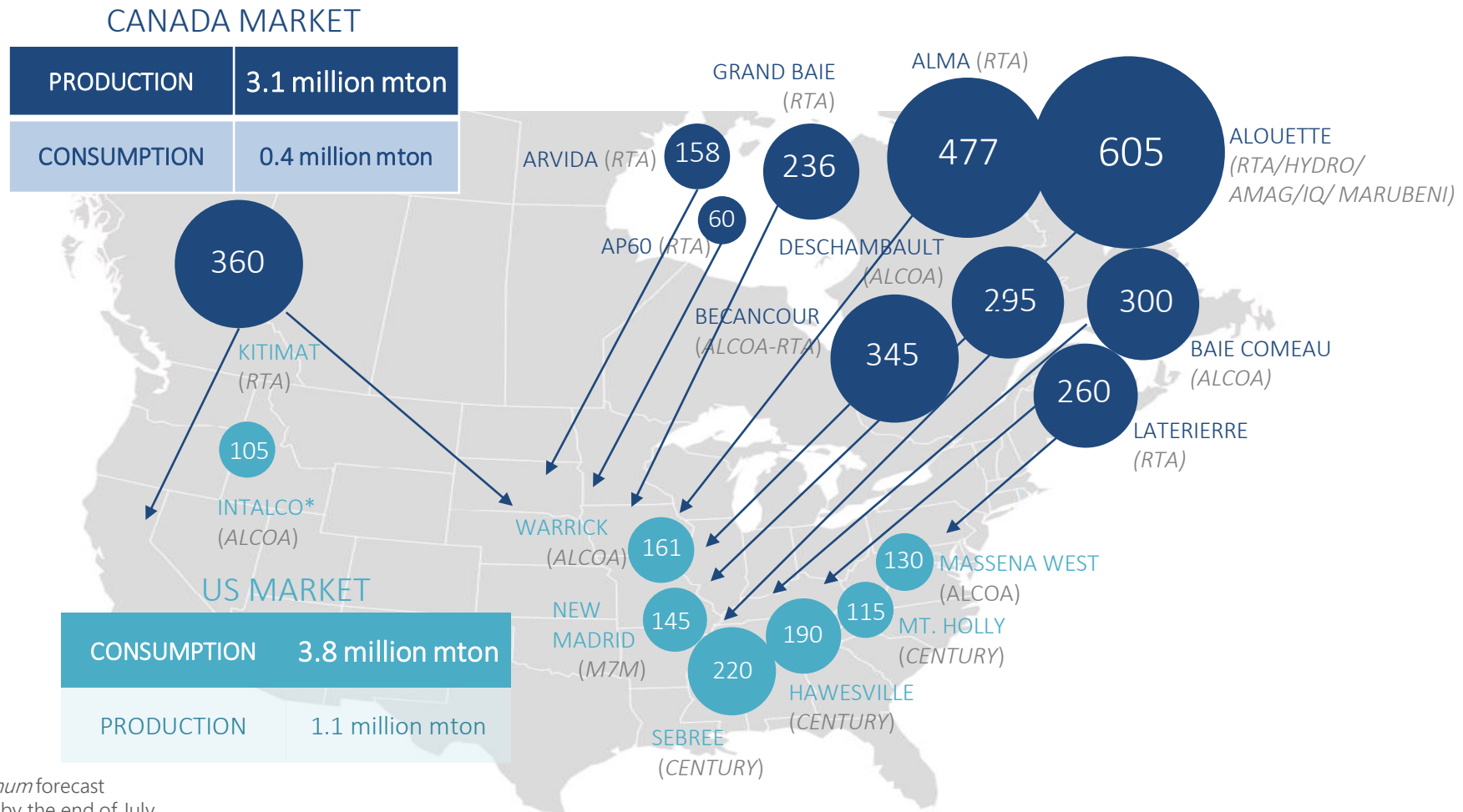
## 1. Are US and Canadian smelters friends or foes?

Neither. They are competitors for the US market.

# Canadian smelters are US smelters' biggest competitors for the US aluminum market

## NORTH AMERICA PRIMARY ALUMINUM PRODUCTION & CONSUMPTION

(thousand mton; 2020F)



Source: HARBOR Aluminum forecast  
\*Intalco to be fully idled by the end of July

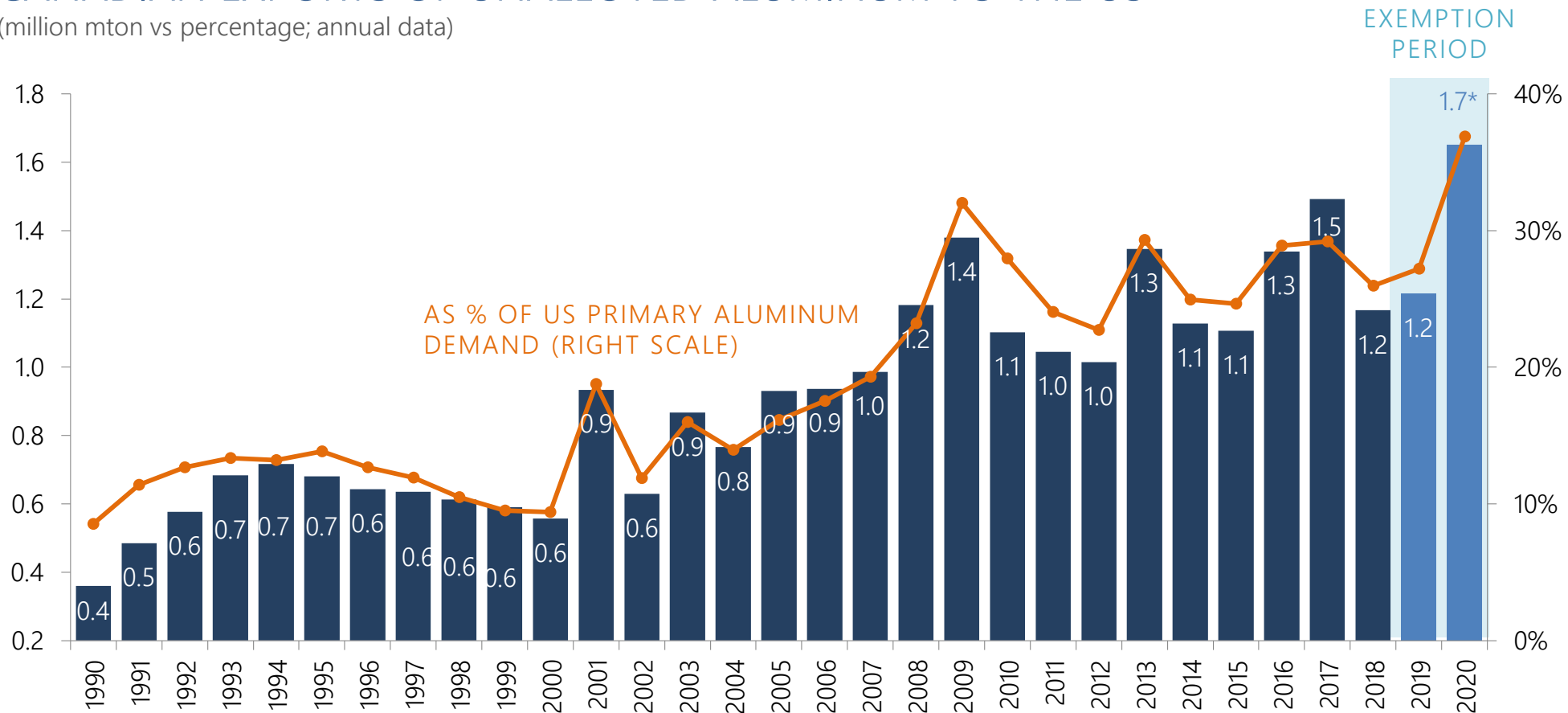
## 2. Did Canadian exports of aluminum to the US surge after the Canadian exemption?

Yes. More clearly in the case of unalloyed aluminum exports, which is the type of aluminum that matters for the MW premium.

# Canadian exports of unalloyed aluminum surged to records after the exemption (May 2019)

## CANADIAN EXPORTS OF UNALLOYED ALUMINUM TO THE US

(million mton vs percentage; annual data)



\*January-April 2020 annualized data.  
Source: HARBOR Aluminum and US Census data.

3. Absent the Canadian exemption, would the surge in Canadian exports to the US have occurred as it did?

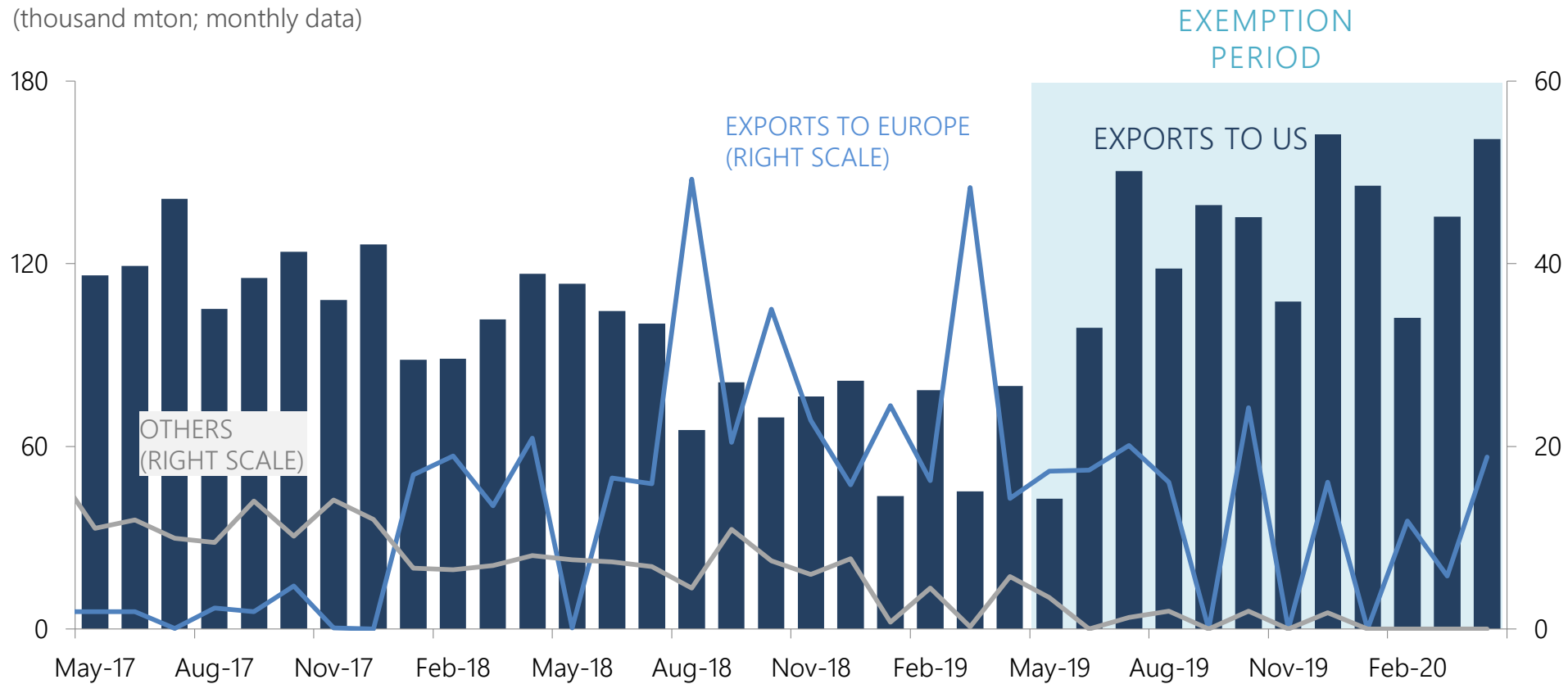
Not likely. Canada would have probably not reduced its exports to Europe and other countries as it did after the exemption.



# Since the exemption, exports to the US surged while exports to other countries plummeted

## CANADIAN UNALLOYED ALUMINUM EXPORTS

(thousand mton; monthly data)



Source: HARBOR Aluminum with Statistics Canada data.

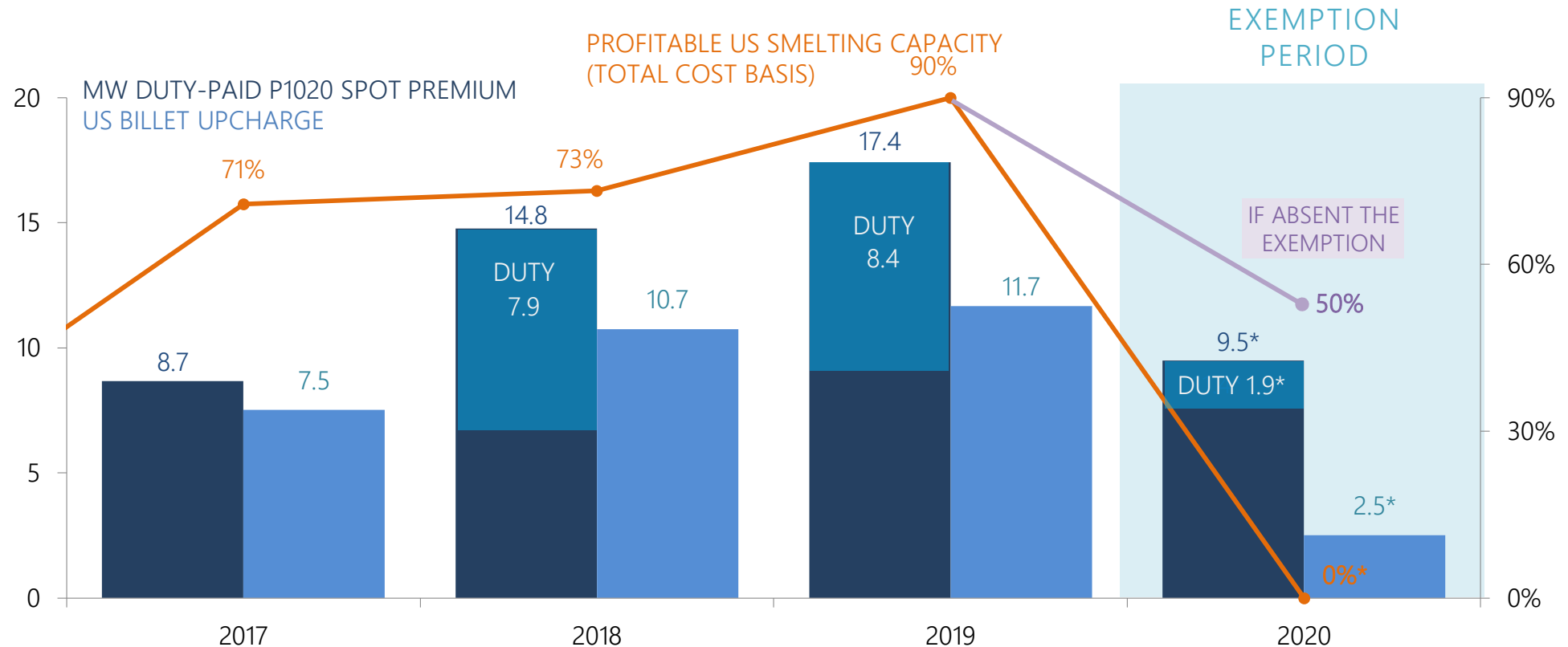
4. Absent the Canadian exemption, would US smelters have remained profitable as the Trump Administration wanted (Section 232's goal)?

Yes. About half of US smelting capacity would have remained profitable despite the collapse in LME prices that followed the COVID-19 pandemic

Absent the exemption, MW premiums would not have collapsed as they did and half of US capacity would have remained profitable

## US MW P1020 & BILLET PREMIUMS VS PROFITABLE US SMELTING CAPACITY

(cent/lb vs percentage of total operating capacity; January-April data)



Source: HARBOR Aluminum.

\*As of May 2020.

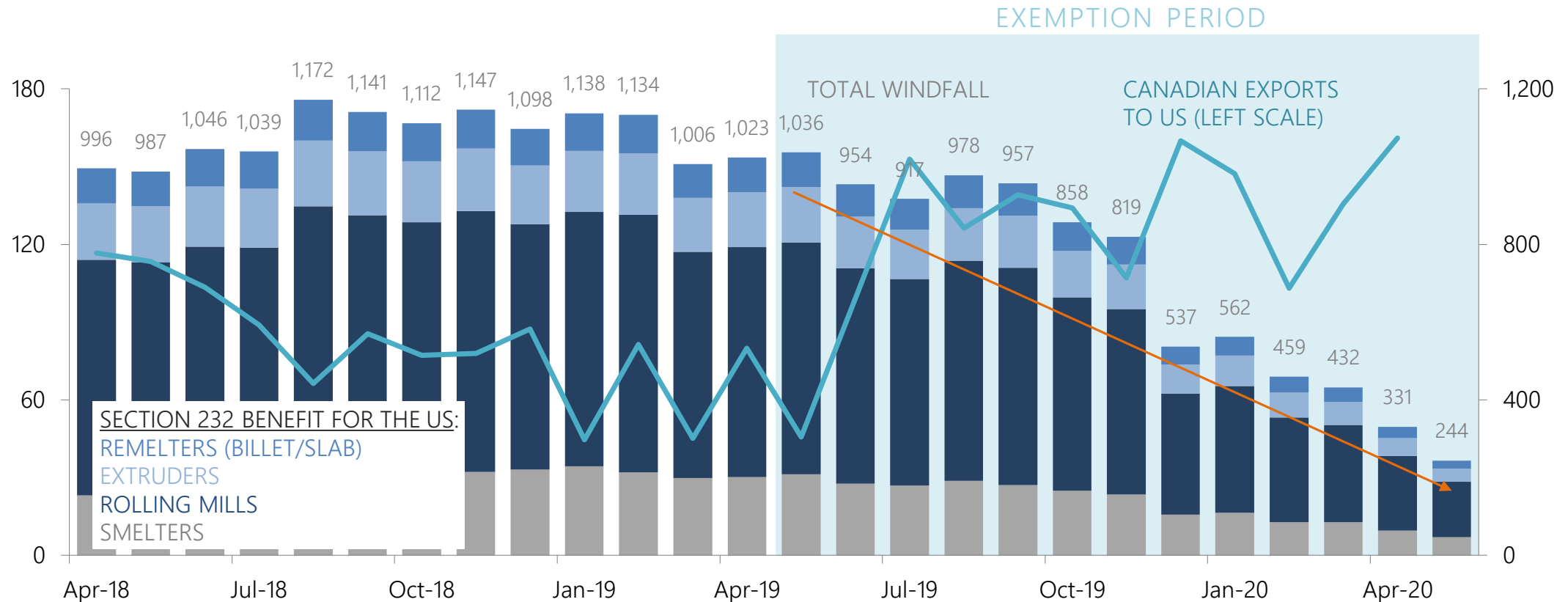
5. Absent the Canadian exemption, would US smelters, rolling mills, extruders and remelters had been more profitable today?

Yes. Remember, the higher the duty embedded in the MW premium, the higher the income & profit for US smelters, and the higher the profit for US downstream with a casthouse (via wider scrap spreads).

# Surge in Canadian exports that followed the exemption, collapsed the MW premium and reduced US aluminum industry profitability

## CANADIAN UNALLOYED EXPORTS TO U.S. VS SECTION 232 WINDFALL FOR U.S. ALUMINUM INDUSTRY

(thousand mton vs USD millions annualized; monthly data)



Source: HARBOR Aluminum and US Census data.

6. What does the US Administration think about the Canadian exemption, export surge, and impact on US aluminum industry?

It is a *“problem”* that needs to be *“fixed”*.

## The Trump Administration is working on “fixing” the “Canadian Problem”

USTR Robert Lighthizer testified in congressional hearings on June 17, 2020 that:

- *"the problem, unfortunately, is not just China [...] it is also a problem with Canada that we are working on"*
- *"there have been surges on steel and aluminum [...] substantially from Canada, some from Mexico, and it is something that we are looking at and talking to both Mexico and Canada about"*
- *"we would let them out of the tariffs on the condition they maintain the same trade flows. If they didn't and we put tariffs on because they surge, they would only retaliate in that sector and not in other sectors"*

7. In this context of a “fix” to the “*Canadian Problem*”, what is the expected impact on the MW premium?

Bullish. As forecasted since last year, the MW premium would rally toward 14-16 cent/lb.



## Working to "fix" the "Canadian Problem" implies only upside risk for the MW premium

### Why Bullish the MW Premium?

- Canada's Section 232 tariff exemption removal is very much on the table--and with higher odds than previously thought.
- In our view, the US is looking either to entirely remove the exemption or impose a hard export quota on Canadian exports of unalloyed aluminum (P1020, off-grade, purity).
- It seems a change to "fix" the "Canadian Problem" could be announced as soon as this week. This would be bullish for the MW duty-paid premium as it would restore the embedded duty in the premium from 1.9 toward 7.9 cent/lb (which would be the entire 10% duty) and confirm our forecast of higher MW duty-paid premiums in the next weeks to as high as 14-16 cent/lb.

### MW DUTY-PAID SPOT P1020 PREMIUM (cent/lb)

