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26 October 2021

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Public File

Dear Sir/Madam

Investigation No. 557 – Copper tube exported to Australia from China and Korea – MM Kembla Response to submissions by Zhejiang Hailiang Co.

1. Introduction

We refer to the submissions by Zhejiang Hailiang Co., Ltd[1] ("Hailiang") following publication of Statement of Essential Facts No. 557 ("SEF 557").

The submission includes comments/statements that require responses by MM Kembla. Additionally, Hailiang contests that MM Kembla has raised issues "which have not previously been disclosed". MM Kembla refutes this claim as the matters raised in MM Kembla's response to SEF 557 were all matters previously raised and discussed with the Anti-Dumping Commission ('the Commission").

MM Kembla has used the same heading references that appear in the Hailiang 15 October 2021 submission to address these concerns.

2. Fixed price copper

MM Kembla welcomes Hailiang's acknowledgment that "producers will hedge the risks associated with future copper price fluctuations. Hailiang suggests that the prices on the LME and Shanghai Metals Market (SMM) "are the same" when the reality is that they are not. It is MMK's experience that all purchases from Hailiang have been priced at the traded 3-month screen price. MMK has provided specific examples where this is the case in Investigation No. 557 – Copper tube exported to Australia from China and Korea – MM Kembla Response to Statement of Essential Facts - Confidential Attachment 2.

Hailiang confirms that its domestic selling prices are set in accordance with SMM spot prices. These are different to prices established on LME 3-month forward prices. It therefore cannot be accepted that copper purchases for domestic sales and export sales are similar with no adjustment warranted.

[1] EPR Document 041.

The Hailiang submission does not address the underlying issue that export fixed sales prices and quantities are generally set at the time of ***order placement***, which is typically three months before shipment and invoicing. To accurately compare export sales prices with domestic prices the Commission must make due allowance under subsection 269TAC(8) to address differences in copper pricing between the two markets.

The material terms of sale for fixed price tube exports are established at the order placement date. Price and quantity are not subject to any continuing negotiation between the buyer and the seller after this date. The material terms of the contract are therefore established on order date. The commissioner should not use the date of invoice to make the comparison between export price and normal value as the terms of the contract are often not finalised on this date.

Hailiang states that *"in SEF 557, it was established that the market trend and price levels of domestic copper was in line with, and consistently higher than that of the LME"*.

The commissioner should note here that the reason that the domestic copper price is consistently higher on the SHFE / SMM is due to market arbitrage impacts between the LME and SHFE prices which include VAT and CIF delivery charges in the domestic China price. (Refer: https://www.lme.com/Education/Online-resources/LME-insight/LME-SHFE-Cross-Market-Arbitrage).

Hailiang would be very aware of this price arbitrage between LME and SHFE.

Hailiang also misrepresents MM Kemblas submission by saying *"there is no support for MMK's contention that adjustment is warranted to domestic prices due to its view that export prices are based on higher LME copper prices".* This statement by Hailiang obfuscates the underlying concept that the export prices are, on average, higher than the domestic prices merely because of the time lag between order date and invoice date. Export prices were, on average, fixed at order dates when the international prices for copper were elevated compared to the prices at the time of invoicing. This downward movement in copper prices occurred in all copper futures exchanges.

The commission also observed "*that Hailiang's domestic purchase price for copper cathode during the investigation period has been higher than the LME price in all but two months and almost 3% higher on average over the investigation period*". (SFE Para 7.4.1). There are two reasons for this price difference that the commission should be aware of:

- Hailiang would always pay a premium above the LME base price to buy copper cathode. Cathode premiums are typically around $70 to $100/tonne;
- There appears to be a two-month lag between when the copper price is established on cathode purchases and the receipt by Hailiang. This is a similar concept that there is a lag setting the export sales price at order date, three months before invoice date.

The commission should also note that the basis for establishing sales prices does not need to match the basis for purchasing the copper. Whether Hailiang uses the SMM price or the LME price as the basis for its sales pricing is not relevant. What is relevant is the domestic copper price used are cheaper than for exports based on invoice date, due purely to the timing difference in the copper benchmarks used in the comparison of weighted average prices. MM Kembla has demonstrated the impact of this difference using the weighted average invoice date price for the period of investigation particularly due to the 31% drop in the LME copper price during quarter 3 of the investigation period.

4. Copper price volatility during Investigation Period

Hailiang has misquoted the Kembla response dated 4 October – "*the domestic price **lower** by the value of the average LME price fall of $xxx/tonne".* The actual statement reads the opposite, stating "*the domestic price **higher** by the value of the average LME price fall of $xxx/tonne".*

The essential concept submitted by MMK in paragraph 4 is that the commission should not use the invoice date to make the comparison between export price and normal value. The commission must acknowledge that export prices are contractually agreed on average three months prior to shipment / invoice date. The only basis for fair comparison of export and domestic sell prices on date of order, with allowances made for differences in copper cost between the two markets.

Hailiang further claims:

> *"Hailiang Group does not take a position by speculating on future price fluctuations on its hedging contracts with a view to achieving additional profit. This is not the purpose of the copper hedges. The copper hedging contracts are designed solely to eliminate the risks to profits of future sales from copper price fluctuations, by locking in a purchase price at future sales prices. This applies to both domestic and export sales. Therefore, there is no difference in costs or prices of the domestic and export sales caused by the hedging positions, and as such no adjustment is necessary."*

This statement supports MM Kembla's argument that the commission has not addressed the underlying issue that export sales prices and quantities are generally set at the time of order placement, which is typically three months before shipment and invoicing. The exception to this is for fixed copper price contracts (contracts where copper price is fixed for a specified number of tonnes and future orders draw down on this tonnage) could be as many 12 months until invoice. To accurately compare export sales prices with domestic prices the commission must make due allowance for copper cost differentials under subsection 269TAC(8).

The hedge put in place as described by Hailiang's statement above is to align the timing for sale and purchasing of copper to mitigate the risks of these timing difference. This further supports MM Kembla's position that quarterly comparisons of normal values and export prices are not a representative basis for assessing dumping in the current circumstances. A more appropriate basis involves transaction by transaction comparison utilizing order date.

Zhejiang Hailiang states:

> *"MMK's objection appears to be caused by the fact that prices for domestic and export transactions are set everyday having regard to the prevailing price of copper inputs, and the prevailing copper price changes each and every day. It is unclear how this situation is any different to all the other commodity-based products subject to dumping investigations, which a primarily driven by the cost of a key commodity input. This would include all steel, aluminum and paper products which are manufactured from inputs subject to fluctuating prices."*

With the copper cost accounting for up to 95% of the total manufacturing cost and the high cost of copper versus other commodities compared to other cases examined by the commission) the variation in the copper raw material has a far greater impact than the raw material cost in other cases (e.g. aluminium . For aluminum extrusions which was subject to previous investigations by the commission the raw material cost of aluminum only accounted for up of 65% of total manufactured cost. Due to the higher percentage of total manufacturing costs of copper raw material and the fact that the copper price is historically up to 3-4 time the cost of aluminum any timing difference during the POI are far more material (and would therefore warrant a timing adjustment).

During the investigation period the LME copper price was almost 50% more volatile than LME aluminum price. This combined with the 31% drop in copper prices in quarter 3 of the investigation period makes using the quarterly weighted average price based on invoice date rather than order date significantly misleading.

6. Sales by Hailiang Australia do not support the "no dumping" finding

MM Kembla has used evidence-based costs to calculate the Deductive Export Price ("DEP") for Hailiang copper tube sales. The commissioner will also use actual costs from Hailiang where these are available. The commissioner should expect Hailiang's costs to be very close to those used by MM Kembla and should question costs that are materially different. Note that MM Kembla is also a very large importer of copper tube, and it will have competitive cost structures compared to other importers.

The key concept MM Kembla seeks to illustrate through the DEP calculation was that the deduced export FOB prices did not even cover the cost of copper. Small differences in the supply chain costs, between MM Kembla's estimates and Hailiang's costs will not alter this fact. In fact, it is MM Kembla that has the largest scale position when it comes to domestic warehousing, distribution and freight costs with many multiples of Hailiang Australia's relative market share. MM Kembla costs are extremely competitive, and any argument otherwise is incorrect and cannot be substantiated. If export prices do not cover the cost of copper used in the Hailiang Australia pricing methodology regardless of the copper benchmark used, then the commissioner's assessment that the sales between the exporter and its related party importer is flawed.

Examples of the DEP calculations have been detailed in MM Kembla Response to Statement of Essential Facts - Confidential Attachment 1 & 3.

Hailiang also claims that costs which are "*immaterial for cooperating exporters, are significant costs for MMK".* The example of cleaning and capping is used, but Hailiang has stated during verification that they do not even know its costs to clean and cap tube and as such Hailiang has no data to support its statement that it is an immaterial cost.

MM Kembla has a fully absorbed product costing system with detailed costing at material level not based on average costs but on specific costs for labour based on machine manning levels and throughput rate, process and machine costs, manufacturing related overheads, product specific bill of materials and product specific yield rate. The commission has MM Kembla's detailed costing extract from MM Kembla's ERP – see - MM Kembla Response to Statement of Essential Facts - Confidential Attachment 7.

Hailiang does not measure the cost of cleaning, capping, labour or associated handling cost at this level so dismissed it as immaterial. Hence pricing does not truly reflect the real cost of these refrigeration capped products and are exported below the real cost of manufacture. MM Kembla has outlined to the commission the percentage increase in AS1571 refrigeration tube pricing in the domestic market over AS1432 plumbing tube as a direct result of these increased cost of manufacturing.

Hailiang further states that "*the degree of undercutting of MMKs prices by imports sourced from all Chinese, Korean and Vietnamese exporters confirms that it is not cost competitive, which immediately renders the deductive export price to be unreliable*".

The DEP calculation makes no reference to MM Kembla's prices or costs, other than relatively minor supply chain cost estimates. The DEP is a highly reliable indicator that something is absent from Hailiang's prices, as the calculated Export FOB price is lower than the cost of copper used as the copper benchmark in the pricing for Hailiang Australia. The extent of price undercutting of MMK's prices is evidence that there is widespread dumping in the Australian market.

8. Undercutting

Hailiang has made a reference under this sub-heading concerning the basis for copper pricing. Hailiang asserts ""*the copper price component of Zhejiang Hailiang's selling prices is determined by the customer's preference. That is the customer will request a particular copper benchmark price".*

The benchmarks have been redacted, however the redacted benchmarks will only differ in the timing basis of when the copper price is set. MM Kembla's submission on copper price volatility is aimed at normalising the timing basis of the copper price between export and domestic sales to enable a fair price comparison to be made.

9. Domestic products made to different standards

MM Kembla has demonstrated in detail the differences in the Australian copper tube standards AS1432 and AS1571 with those evident in the domestic standards applicable in China, Korea and Vietnam standards, and that these differences are material in nature.

The Commission's findings in the exporter verification report in Investigation 469 for Guilin International Wire and Cable Co Ltd in PVC Electrical Cables exported from China was referenced to highlight the Commission's previous findings on applicable standards, and to confirm that the locally produced goods differ from the exported goods due to the latter being manufactured to a different standard.

10. Capping costs and removal of the Capping Model Characteristics from the MCCs

Hailiang has not submitted evidence that capping costs are immaterial as they do not measure the costs of cleaning and capping. The cost of capping is treated as part of packaging cost.

Hailiang's comments on this issue in its EQR were:

> *"Zhejiang Hailiang recommends that the comparison between domestic and Australian sales should be made between the same specification's, including outside diameter, wall thickness and length, if required. Besides, Zhejiang Hailiang would like to make suggestion on the composition of MCC. When organizing the cost sheet G-3 and G-5, Zhejiang Hailiang noticed there is a difficulty in reporting MCC as required, for the category "Cap". As introduced before, Zhejiang Hailiang adopts SAP system in its financial accounting. In SAP, product is assigned with its exclusive material code, and cost is accounted based on material code. In preparing the G-3 and G-5, Zhejiang Hailiang relied on the cost reports exported from SAP, and used the material code to identify relevant MCC. The material code encompass detailed product characteristics which is used to prepare the MCC (for detailed explanation, please refer to section C-4 below),* ***but it does not include whether the cap is used. Including cap or not is a requirement from the customers. So, for a material code, it may have cap and it may not, based on what the customer requires****. Therefore, in sales table B-2 and D-2, Zhejiang Hailiang could organize the complete MCC, because technician staff would know for each transactions that whether the customer asks for using caps, but it is impossible to identify, in cost table, which material code uses cap. Zhejiang Hailiang believes the same situation would happen to other parties as well. Therefore, Zhejiang Hailiang would like to suggest that "cap or not" should not be taken as one of the components of MCC. The price differences regarding the usage of cap could be offset by reporting and adjusting cap's cost as packing materials in Attachment B-2 and D-2, as Zhejiang Hailiang has already done."*
> (para C3, page 11, Zhejiang Hailiang Exporter Questionnaire)

There are significant differences between cleaned and capped tube for the Refrigeration market compared to tube produced for the plumbing tube market. This has been demonstrated to the commission and as outlined above detailed costings have been provided from the MM Kembla ERP system.

The refrigeration and air-conditioning markets require copper tube to meet stringent specifications for internal cleanliness. Refrigeration tube must be capped securely immediately after cleaning.
MM Kembla's capping operations are highly automated where possible, with a dedicated automatic capping line. MM Kembla capping and cleaning costs are internationally competitive and well understood.

All cooperative exporters including Hailiang, Daejin and Nungwon say they are not capable of identifying this specific cost for cleaning and capping.

The commission has determined that it will accept the submissions from Hailiang that capping costs are insignificant, but at the same time the commission has ignored the fact that Hailiang does not even measure these costs in its costing system.
MM Kembla submits that capping and cleaning costs for Refrigeration tube are material and should be included in the applicable MCCs as an upward adjustment.

17. Laboratory testing

The issue with non-compliance with Australian standards is that there are significant cost savings to be made by the exporter selling non-compliant tube in Australia. MM Kembla has requested that the commission adjusts for the unfair cost advantages that Hailiang has gained by supplying tube that does not comply with Australian standards. The cost adjustments will be related to:

- drawing thin-walled tube which generates significant savings in the cost of copper, in some cases savings are equal to the total fabrication cost;
- non-compliance with internal cleanliness standards which generates savings from insufficient cleaning and testing;
- savings from having lax internal quality assurance systems;
- yield savings that are only possible due to the lax internal quality assurance systems.

18. Normal value adjustments

(a) Scrap

The following adjustments to normal value are therefore required:

> "Zhejiang Hailiang confirms that scrap was used in the production of copper billet which was then used in the production of both domestic and exported goods."

The commission has previously stated that it "*has observed that raw materials purchased on the domestic market have not been used in the manufacture of copper tube exported to Australia by Hailiang"*. That all export sales to Australia only use LME imported cathode.

The response by Zhejiang Hailiang is in clear conflict to the previous statement made by the commission above during verification.

A continuous biller caster production process is exactly that - continuous, which means you have no definitive start or finish to which raw materials end up in the finished billet. Raw materials are always blended in the furnace so for Hailiang to make the statement above that only imported LME imported cathode is used in the manufacturing of copper tube exported to Australia is misleading and incorrect.

The commission must establish with Hailiang the use of copper scrap in its manufacture of copper tube.

(c) Draw thin

Hailiang states: "All the product sold in domestic market are in accordance with the tolerance and copper content request" (Hailiang 15 Oct 21).

This statement confirms MM Kembla's submission that the wall thickness is determined as the copper content requested by the domestic Chinese customer. There is a very significant cost saving from drawing thin. This statement also validates the MM Kembla submission that the export and domestic tubes are not like products as they are made to different standards and cannot be compared without adjustment.

20. Subsidies

Zhejiang Hailiang states "*Regarding MMK'S assertion that 'the Zhejiang Hailiang 2020 Annual Report discloses a number of additional subsidy programs that the Commission has not identified at Section 7 of SEF 557'*,

Hailiang clarifies that these 'additional subsidy programs' were received subsequent to the period of investigation. The grant programs received by Zhejiang Hailiang during the period of investigation have already been reported in the questionnaire response and verified by the commission.
There are a number of subsidies listed in section 53 Other Income of the Zhejiang Hailiang 2020 Annual Report relating to the 2020 and 2019 reporting period that are not listed at Section 7 of SEF 557. Hailiang has made unsubstantiated assertions that these are outside the period of investigation and should be investigated by the commission. As a minimum the size and total value of the combined subsides disclosed in the annual report should be compared to that provided by Zhejiang Hailiang during the investigation.

Conclusion

We submit that Hailiang has further attempted to misrepresent the relevant considerations concerning copper cost and timing issues, the selection of purchase order date as the correct date for fair comparison purposes, the relevant standards by which the domestic and export goods are manufactured to, and the cleaning and capping costs, in the determination of dumping margins for Hailiang's exports to Australia.

These concerns apply equally to other Chinese exporters and exporters in Korea.

MM Kembla respectfully requests the commission to fully consider the matters included in this submission which address the shortcomings of the identified matters raised by Hailiang in its 15 October 2021 submission.

If you have any questions concerning this submission, please do not hesitate to contact me.

Your sincerely

Tony Bova
Executive General Manager