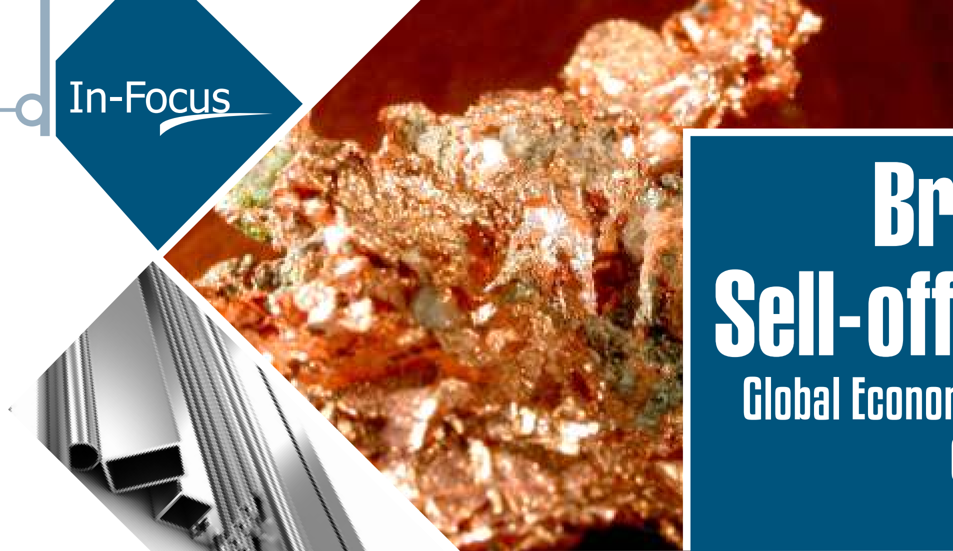

Broad Based Sell-off in Base Metals

Global Economic Uncertainty Hits Industrial Commodities Hard

- Metalworld Research Team

A broad based sell off seen for over three months in base metals amid dollar force against majors and Euro losses made on uncertain Greece debt conditions. Lack of China stimulus and slow demand in case of industrials had put more pressure in last month.

Base metals slipped to support zone on rising concern of global surplus and weak Chinese demand in the last month. Lack of China stimulus added more concerns to the market. Secondly, reduction in oil prices also caused selling pressure on metals. In the current month, metals are likely to show some rebound after sharp reduction witnessed in the last month. In ht metals complex, Aluminum and Lead likely to show higher pullback as compared with other metals, zinc upside move is limited as overvalued counter is likely to correct somewhere. Nickel prices are unlikely to go below $11800 levels on LME in the current month.

US employers ramped up hiring last month, signaling a rebound in overall growth after a bumpy start to the second quarter and nudging the Federal Reserve towards its first interest-rate increased in a decade approximately. The 280,000 payrolls in advance exceeded the median forecast, while the jobless rate ticked up slightly to 5.5%, as more people entered the labor force, whereas hourly earnings rose a year ago since August 2013. The dollar strengthened and Treasuries fell after payrolls rose more than forecast, bolstering the case for raising interest rates. The dollar rose to 13-year high of 125.84 against the yen and Euro by 1% on Greece debt worries. In May, dollar traded firm above 95 levels on Fed confirmation of rate hike and Greece struggling to reach to final deal to make payment to its creditors. Euro gained 3.2% in the last month above $1.1250, erasing two months losses a European Central Bank official said the bank will speed up its bond-buying program before an anticipated mid-year lull. ECB's Draghi said that investors should get used to higher debt market volatility, off late EURUS D retreated as Greece postponed 300 million euro IMF repayment.

Copper Under Pressure

In last month London copper slipped 5%, but remained under pressure with data stoking worries China the top metals user about demand. China's Copper imports dropped 5.3% to 360K in last month on year on year basis. Global stocks are also reduced on LME and COMEX by around 4.50% in last one month. Majorly, in last month dollar strength and European concerns was most influencing factor for Copper sell off after USA's weak housing and manufacturing data. After the long consolidation, copper breached below Rs 390 levels on MCX and $6000 on LME as Fed rate hike confirmed dollar rally against metals. Metals traded down on weak Chinese demand but any other stimulus from China will add gains to the picture. As per the earlier forecast copper likely to continue with its gains above Rs.400 if prices are not sustaining on lower side below $5800 levels or Rs 360-370 levels in short term thus there would be some correction in current month to Rs.375-380 on which buying could be suggested.

Meanwhile, the global copper agency, International Copper Study Group (ICSG) projections for 2015 indicates that the world refined copper production is expected to exceed apparent refined copper demand by 365,000 metric tonnes (t). According to ICSG projections for 2016, the copper market may show a second consecutive production surplus relative to demand. However this is expected to be lower at 230,000 (t) as the demand grow and also the outpaces production grows. In developing its projections, ICSG recognized that the global market balance could vary from those project owing to numerous factors that could reduce or enhance projections for both production and usage. In this context it can be noted that actual market balance outcomes have on recent occasions deviated significantly from ICSG market balance forecasts due to unforeseen developments.

After underperforming in 2014 with

growth of just 2.4%, world mine production is expected to increase by around 5% in both 2015 and 2016 to 19.5 Mt (million tonnes) and 20.5 Mt respectively after adjusting for historical disruption factors. The increases will reflect expansions at existing operations, ramp-up in production from mines that have recently come on stream and output from a few new mine projects. Most of the new production is expected to be in the form of copper in concentrate. After increasing by 7% in 2014, world refined copper production in 2015 is expected to increase by around 4% year-on-year to 23.4 Mt on the back of capacity expansions at electrolytic plants in China. Primary refined production is expected to grow by 6% this year benefiting from increased availability of concentrate while secondary production is forecast to decline by 2% on continued tightness in the scrap market. In 2016, world refined copper production is expected to grow further by around 2.5% to 24 Mt. Following growth of around 7% in apparent usage in 2014, ICSG expects world apparent refined usage in 2015 to increase by only 0.6% mainly because, although industrial demand growth in China is expected at around 4.5-5%, apparent demand in China is expected to increase by 1%. On the other hand, usage in the rest of the world is expected to remain essentially flat. For 2016, the growth in apparent refined usage is expected at around 3% with underlying Chinese industrial demand growth expected at 5%. Usage in the rest of the world is expected to increase by about 2%.

Record Stockpile Pulls Down Nickel

Nickel slumped 6.4% for the biggest drop among the six main metals on the London Metal Exchange to lowest drop since March 31 as LME Stockpiles tracked warehouses rose to a record 444,936 metric tons. Recently global nickel market fundamentals have been troubling analysts with the market, forecast to enter a significant deficit constantly. However, this outlook never seems to be materialize, leaving nickel prices drifting and failing to rally as expected on the back of tight market balance. The failure of the nickel market to enter a global deficit is highlighted by the large buildup of inventory in LME warehouses. Indeed, market participants feel that these stocks should be drawn down considerably before any meaningful improvement to be seen in the LME nickel price. Part of the increase in LME, warehouse inventories has been as a result of exports of Chinese refined metal was relocated from bonded warehouses, as well as slower demand from the global stainless steel sector that has been in a destocking phase since May of 2014. Stainless steel accounts for around two-thirds of global nickel consumption. Likewise, China's stocks of Indonesian nickel ore failed to decrease rapidly in the aftermath of Indonesia's ban on nickel ore exports in January 2014 due to increased exports from the Philippines and a blending of Indonesian and Filipino ore for China's nickel pig iron (NPI) production.

The world's largest nickel producer, Norilsk Nickel, said this week at its 2015 Strategy Update that LME nickel warehouse inventories were now at a turning point and are expected to decline. The producer also commented that China's inventories of nickel ore are down significantly, with only around two months of consumption left. The company also believes China's dependence on imported refined nickel is set to rise. It estimates that total nickel demand in China in 2015 will be made up of 42% imported refined nickel, 47% imported feed, and around 11% of domestic feed. In 2014, total nickel demand in China consisted of 28% imported refined nickel, 61% imported feed, and 11% domestic feed. In its 2014 full-year results, the company forecast a 20,000 mt global deficit this year down from a 93,000 mt surplus in 2014. While a number of analysts are also forecasting a revised deficit between 20,000-45,000 mt this year, it remains to be seen whether this shift will actually occur. And with now resting on the second half of 2015 for a change in nickel's fortunes, it remains to be seen if the forecast deficit scenario will really unfold, especially when taking into account the traditionally slacker period for metal demand over the summer months.

Zinc Retreats

Zinc prices retraced lower from its swing highs at Rs 154.35 levels to close at Rs 142.55 with a cut of 5%. Failure to trade above Rs 143 on pullbacks will see prices head lower and test major support areas around Rs 133 levels. Until prices hold on above Rs 133 chances of prices moving higher are quite high. A monthly close above Rs 145.50 will be positive for the counter. Lead prices closed down with a cut of 8.26% during the previous month. Areas around Rs 121 are strong support cluster for lead and sustenance, above this support will see prices rebound towards Rs 130 levels. A breakdown below Rs 121 will see prices correct towards Rs 115 levels. A monthly close above Rs 130 will see again prices move higher towards Rs 135 areas. LME Zinc touched the lowest since April, while Lead also posted weakest month in the year.

The International Lead and Zinc Study Group (ILZSG) has released the preliminary data for world lead supply and demand during the first quarter of 2015. The provisional data indicates that the lead mine supply has marginally declined by almost 0.9% year-on-year during the initial three month period of the year. According to ILZSG, the world supply of refined lead metal exceeded demand by 11kt during the first quarter of the year. The total reported stock levels dropped by 10 kt during the period. Meantime, LME stock levels rose during Jan-Mar,15. The overall lead mine supply during Q1 2015 totaled 1.146 million tons, in comparison with 1.156 million tons during Q1 last year. The falling mine output from Australia has contributed to the 0.9% year-on-year decline in global lead mine supply. On the other hand, the mine supply from Peru and the US increased during the quarter. The global refined lead metal production declined by 2.3% during Q1 this year. This was primarily on account of lowered production from China and disruption of operations at La Oroya plant in Peru during the month of June last year. The global demand for refined lead metal witnessed a decline of 2.7% during the quarter. The apparent usage of refined metal by China and the US fell by 4.6% and 6.2% respectively. The apparent lead usage by the European region too dropped by 2.5%. ILZSG statistics indicate that the lead mine supply during the month of March alone totaled 379,300 tonnes. The global refined lead metal production during the month totaled 859,100 tonnes. The apparent lead usage totaled 854,600 tonnes during March this year.

The latest statistics published by the International Lead and Zinc Study Group (ILZSG) indicates that global refined zinc market was in surplus of 140,000 tons during the initial quarter of the current year. The total reported zinc inventories at LME declined by 180,000 tons during the quarter. Meantime, inventories at Shanghai Futures Exchange increased by 57,000 tons. The stocks reported by producers reported a jump of 40,000 tons during Q1 this year.

The zinc mine output reported declines in China. However, the fall in output was covered with the increased mine output from other countries including Australia, India, Peru and Sweden. Overall, the zinc mine output grew by 4.3% during the quarter when compared with the corresponding quarter last year.

The refined zinc metal production during the three-month period totaled 3.414 million tons, 4.3% higher when compared with the 3.153 million tons output during corresponding three-month period in 2014. The Chinese refined zinc metal production surged higher in Canada, China, India and the Republic of Korea.

The global demand for refined zinc metal increased by 2.3% to 3.274 million tons during Q1 2015. The Chinese apparent usage increased by 3.9%. The US reported a demand rise of 13.9% during the quarter. The usage reported higher levels in the Republic of Korea, Africa and Thailand. The apparent consumption in the Europe region remained flat during the quarter. Interestingly, Chinese net imports of refined zinc metal plunged 78% during Q1 2015 in comparison with the first quarter of 2014.

The ILZSG preliminary data indicates that global zinc mine output totaled 1.08 million tons during the month of March alone. The global refined zinc metal production totaled 1.144 million tonnes, whereas global zinc demand totaled 1.107 million tons.

Aluminium Faces the Biggest Monthly Loss

In May, aluminum showed its biggest monthly loss in 2-1/2 years on supply glut. Global consultancy firm Goldman Sachs sees lower aluminum prices as world must offset China. Aluminium prices rallied to a high of $2,119 per tonne early in September from a low of $1,671.25 in February before dropping back to $1,778, thereby retracing 76 percent of the gains. Prices are now around the upper levels of the former sideways range that formed the 2013-2014 base. Last year in July report we thought the rally was premature and that prices were running ahead of the fundamentals - as well as being counter-productive because higher prices were encouraging idle capacity to be restarted. Lower energy prices (oil and coal) seem to be driving the deeper pullback, lowering producers costs of output, which is providing an incentive to raise production, as the latest International Aluminium Institute (IAI) data shows.

Global aluminium output in November averaged 151,700 tonnes per day (tpd) compared with 146,100 tpd in October and an average of 142,100 tpd in November 2013. In the first 11 months of 2014, production averaged 144,920 tpd, which means output in November on an annualised basis was running some 2.5 million tonnes above the average in the first 11 months of the year. Looking forward, producers now face some crosscurrents - some will be able to take advantage of lower energy prices to reactivate idle capacity but lower LME aluminium prices will start to squeeze operating margins at others. So in the short term lower oil prices are likely to remain a bearish influence, especially if it encourages more exports of Chinese aluminium semis. But if lower benchmark prices start to prompt talk of more output cuts, bargain-hunting may well reappear. As always with aluminium, the demand profile is second to none, so at the first sign of supply restraint consumers and investors are likely to return as buyers. This in turn could trigger shortcovering and restocking and another upward run in prices.

New LME Rules and its Impact

If the new LME warehousing rules are implemented this year, leading to a faster outflow of metal, it does not necessarily mean availability will increase - the metal leaving warehouse could simply just go into off-market financing deals. We do not think there will be much pick-up in availability in the market until interest rates rise to a level that makes financing metal economically unviable. Given concerns over slower global growth, the US Federal Reserve may indeed delay any rate rises or it may have a negligible impact on the financing model. The aluminium industry may therefore have more time to reduce the stock overhang but to do so it will need to limit production increases - this will require keeping aluminium prices sufficiently low.

Demand growth remains robust – aluminium continues to enjoy strong demand growth, especially for auto-sheet. With China growth slowing and with Europe trying to fight deflation, there are high expectations for more stimulus measures, which seem likely. In addition, lower oil prices should provide a worldwide boost to household and business spending, which should help to counter some of the other negative factors affecting growth such as tight credit in China. We still expect relatively strong growth overall while aluminium gains market share from copper and galvanized steel.