INSIDE METALS

Tuesday, December 10, 2013

CHART OF THE DAY

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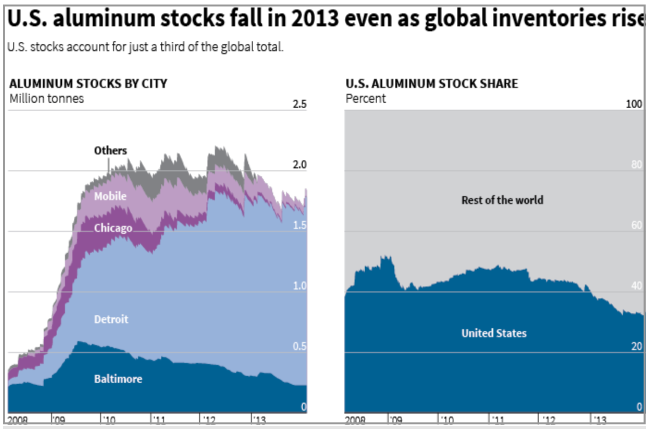

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FEATURE

With Washington watching, U.S. aluminum stocks dwindle

Aluminum stockpiles in U.S. cities such as Baltimore and Chicago are slowly vanishing as traders worry that U.S. regulators might step into a years-long dispute over the London Metal Exchange's warehousing policy.

LME-registered aluminum stocks in the United States have fallen 6 percent so far this year to around 1.8 million tonnes, the lowest since July 2009, even as global inventories have risen to new records with the market still awash in the metal.

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TODAY'S MARKETS

BASE METALS: London copper hit a one-month high as expectations the Federal Reserve could soon start tapering its economic stimulus undermined the dollar, while steady consumer buying from China put a floor under prices. "We are expecting demand conditions in the first quarter next year to be much more positive, not just in China ... but in the rest of the world as well," said analyst Matt Fusarelli of Sydney-based AME Group.

PRECIOUS METALS: Gold was steady after gaining 1.3 percent over the past two days, but trading volumes were thin as investors turned their attention to a U.S. Federal Reserve policy meeting next week. "The short-term bullishness is unlikely to last through next week as speculators are likely to trade with more caution closer to the last FOMC meeting of the year," said Joyce Liu, investment analyst at Phillip Futures Pte Ltd, referring to the Fed's Federal Open Market Committee.

FOREX: The euro stayed well-bid scaling a fresh five-year high on the yen and a six-week peak against the dollar as expectations for further stimulus from the European Central Bank continued to fade.

"That to me signals that when taper does happen it will be a token of faith to the markets," said Evan Lucas, a market strategist at IG in Melbourne. "I believe that any moves in the asset purchase programme will be a token affair as its second mandate of inflation is still well behind expectations."

FEATURE

ANALYSIS-With Washington watching, U.S. aluminum stocks dwindle

By Josephine Mason

NEW YORK, Dec 10 (Reuters) - Aluminum stockpiles in U.S. cities such as Baltimore and Chicago are slowly vanishing as traders worry that U.S. regulators might step into a years-long dispute over the London Metal Exchange's warehousing policy.

LME-registered aluminum stocks in the United States have fallen 6 percent so far this year to around 1.8 million tonnes, the lowest since July 2009, even as global inventories have risen to new records with the market still awash in the metal.

They had fallen by as much as 13 percent through mid-November, but recovered slightly in recent weeks.

About one-third of the 5.5 million tonnes in the LME system is now stored in the United States, the smallest share since before the world economic crisis hit five years ago, a Reuters analysis of exchange data shows.

Metal traders cite many potential causes for the stark reversal, principally an overhaul of the LME's warehousing rules that has curbed controversial incentive payments made by warehouses to attract metal, especially in the United States.

They also say a better U.S. economy and improved auto manufacturing, spurred demand, while new competition has emerged from the Dutch port city of Vlissingen, where Pacorini Metals, owned by Glencore Xstrata Plc, has built a network that now houses some 40 percent of the LME global stock.

But some in the industry also see the shift as a stark response to rising risks. Companies are removing metal from the LME's U.S.-based warehouses for fear that pending investigations could land them in hot water.

The aluminum in Detroit and other cities is not necessarily being shipped elsewhere, it is simply disappearing from the LME network and moved into non-exchange warehouses.

Among concerns is worry that regulators will intervene to further tighten the LME's warehousing policy, ratcheting up the minimum rate for "loading out," or removing metal, and increasing the risk of being caught holding loss-making metal.

"There are still concerns down the road about regulators enacting a faster pace of load-out," said Nicholas Snowdon, a base metals analyst at Barclays Capital.

"If you can get the metal off exchange now, you're better placed to liquidate holdings if premia come under more intense pressure."

Their focus is not on Britain, where the Financial Conduct Authority (FCA) oversees the exchange, but rather the U.S. Commodity Futures Trading Commission (CFTC), which took the lead during the summer in investigating alleged market manipulation.

Under pressure from angry end users and facing intense scrutiny from U.S. politicians and regulators, the LME has announced measures to cut wait times to 50 days at some of its biggest storage hubs, and increase oversight of the over 30 warehouse companies in its global system.

The measures are aimed at stemming the years-long criticism of the exchange's warehousing policy by end users, including MillerCoors, which uses the metal to make beverage cans and says long wait times and big incentives have inflated physical prices and distorted supplies.

DIMINISHED INCENTIVE

Warehouses in Baltimore, Chicago and Mobile - among the LME's nine U.S. locations - have seen the biggest drawdowns, taking stocks in the three big port cities to their lowest since 2008, when inventory started to build up as demand ebbed.

During the economic crisis, most of the metal landed in Detroit, the U.S. auto hub. Stocks there remain high, reaching a record of almost 1.6 million tonnes last week, but most of it is canceled, meaning it is waiting to be delivered.

At its peak in 2011, U.S. aluminum accounted for more than half of the LME total.

Much of that was fueled by financing deals in which banks or traders agreed to store metal in warehouses for months or years at a time and sold it forward at a profit due to the wide forward price structure known as the "contango" and low borrowing costs.

To bring in even more long-term financing customers, exchange-registered warehouses began offering ever-higher incentives to store metal at their facilities, sparking the biggest controversy in base metals trading in 20 years.

As aluminum piled up in Detroit, end users complained they had to compete with those payments to secure metal, paying out inflated physical premiums for their raw material.

Now, at least in the United States, that is reversing.

Incentive payments have not disappeared altogether, but warehouses have slashed them. Premiums paid on top of the LME benchmark for physical delivery have steadied around 9.50 cents per lb, still an historically high level, but down from over 12 cents per lb earlier this year.

And non-LME storage operators are now offering rental rates that can be as much as 80 percent lower than LME warehouse fees to lure material.

Combined with a big contango, storing metal in long-term financing deals off-exchange has never been more profitable, traders and analysts say.

Moving outside the LME system might also give consumers quicker access to the metal, avoiding the controversial long wait times end users say have distorted supplies.

In Detroit, where Goldman Sachs Group Inc's Metro warehouse dominates, it can take over a year to get metal.

FEATURE *(Continued)*

"It's definitely easier to get hold of off-warrant metal," said a U.S. trader. The LME stock data does not tell the whole story. Some metal never shows up in LME-registered storage and goes straight into off-exchange storage. There are no official estimates for the size of off-exchange stocks, but many analysts said they are as big, if not, bigger than LME stock.

As a result, storing metal outside the LME network will increase the perception of tightness, even as the market struggles under 5 million tonnes of surplus metal, and will likely temper the pressure on premiums, traders said.

BRITAIN VS UNITED STATES

For traders, the question now is whether action by U.S. regulators will deepen the reforms already laid out by the LME, and specifically what kind of pressure the CFTC, the agency that helped fuel the global investigations into interest rate benchmarks, might bring to bear. "The CFTC could extract a significant amount of leverage over the LME. They could certainly cause them some pain," said an industry source familiar with the CFTC.

The CFTC was the first to take action in investigating the warehouse issue, handing out subpoenas to warehousing companies and their owners, including Glencore and Wall Street's biggest banks in July. The Department of Justice continues to look into the matter. Traders and legal experts say the commission could claim some jurisdiction through a "no-action" letter it granted in 2001 allowing the LME to operate in the United States. The LME and CFTC both declined to comment.

That would be unprecedented, experts say.

The LME has already taken action of its own, proposing the most sweeping changes to its operations in its 136-year history, which is seen by Britain's FCA as a step towards improving transparency.

But end users in the United States say the changes do not go far enough, calling for wait times to be cut further, even though the LME has said it would not be practical.

Intense regulatory, legal and political scrutiny in the United States also shows no sign of abating. In the new year, an influential political committee will grill U.S. regulators on the role of Wall Street banks in physical commodity assets.

"The LME could not have done much more, but the concern is still the CFTC," said a senior executive at a ring-dealing member of the exchange.

GENERAL NEWS

Barclays favors nickel in 2014, bearish on gold and oil

NEW YORK, Dec 9 (Reuters) - Base metals, led by nickel, appear set to trend higher in 2014 due to tighter supplies, while unfavorable economics should keep pressure on gold and oil and prompt investors to avoid much of the commodity complex, Barclays said on Monday.

In another negative outlook on commodities from a major investment bank, London-based Barclays said that outflow of money from the sector will not end soon, at least not in the first quarter.

It cited a litany of reasons, including comfortable supply levels in most raw materials; a still-sluggish global economy and the likely scaling back of the Federal Reserve's stimulus that had supported commodities.

"It is unlikely investors will warm to commodities in the near term," said Barclays, which until a few years ago was one of the biggest proponents of the sector. Goldman Sachs, often regarded Wall Street's most authoritative voice on commodities, and Citigroup have issued similarly sanguine outlooks in recent weeks.

NICKEL MOST FAVORED PLAY

Smaller stockpiles has base metals better positioned for gains than other commodities when the new year begins, with nickel in particular due to a planned export ban by Indonesia, Barclays said.

"Most base metals have been stuck in structural surplus to a greater or lesser degree since 2007/08 after what was one of the strongest-ever periods of supply growth. However, 2014 is likely to mark the end of this phase."

Nickel hit a one-month high on the London Metal Exchange on Monday, closing up 1.4 percent at $13,955 a tonne.

Barclays said it expects the metal to average $14,750 in the first quarter and above $15,000 for the rest of the year as the Indonesian ban potentially deprives the Chinese nickel-pig iron sector of crucial raw material.

"There remains some uncertainty over how strictly this ban will be implemented. Even if it is not, nickel prices are so low," it said. Nickel is down 18 percent so far this year.

Barclays said it expected aluminum and lead supplies to turn into a deficit in 2014, and zinc's surplus inventories to shrink dramatically like nickel's. It forecast modest supply growth in copper, the most-widely traded base metal.

OPEC SUPPLY WEIGHS ON OIL

In crude oil, it said the need for OPEC oil was diminishing and global inventories will climb if members of the producer group do not cut output. A sluggish global economy weighed on the outlook for oil, as did a decline in geopolitical risks in oil produc-

GENERAL NEWS *(Continued)*

tion areas following the nuclear agreement between Tehran and the global powers, it said.

Barclays projected oil's benchmark Brent crude to average $101 per barrel in the first quarter, versus Monday's level of nearly $110. It forecast a high of $108 for the final quarter of 2014. Brent is down almost 2 percent this year.

For U.S. crude, the projection was $95 a barrel in the first quarter, versus current prices near $98, and a high of $99 by the year-end. U.S. crude is up about 6 percent this year, outperforming Brent.

"SHORT" GOLD

In the case of gold, Barclays advised investors to "short", or bet on a fall in prices, the precious metal after March, its target period for any reduction in the Fed stimulus.

In spite of that, the bank had a higher price expectation for gold in 2014 versus Monday's traded levels -- a discrepancy it did not explain.

Barclays said gold was likely to average $1,350 an ounce in the first quarter, although it forecast a drop to $1,270 by the end of 2014. The spot price of gold hovered at $1,240 on Monday, down 26 percent so far this year and heading for its first yearly loss since 2000.

Barclays did not provide price forecasts for the agricultural markets or "softs" commodities such as coffee, sugar, coffee and cocoa. But it cited supply gains in corn and wheat from larger harvests in 2013/2014.

Goldcorp says Mexican land group threatens Canada suit

TORONTO/MEXICO CITY, Dec 9 (Reuters) - Goldcorp Inc said on Monday a group challenging its use of lands around its Peñasquito mine in Mexico is threatening to sue the company in Canada.

The company and an organization of local landowners, the Cerro Gordo Ejido, have been locked in a tussle for months. Goldcorp in June won a temporary suspension of an agrarian court ruling that nullified Goldcorp's lease of the lands and ordered that the land be returned to the group.

Since then, Goldcorp and the Cerro Gordo Ejido have been in talks with a view to reaching a settlement.

However, Vancouver-based Goldcorp said on Monday it had received a notice from a Canadian law firm purporting to represent the Cerro Gordo Ejido group, threatening litigation against Goldcorp in Canada concerning the same lands.

Goldcorp said it believes the allegations are baseless. It said it will vigorously defend any claim if one is filed.

Alfonso Herrera, a lawyer representing the group, said the landowners had tired of getting hit with injunctions from Goldcorp in Mexico that stalled their case, arguing the company had shown little real desire to negotiate.

He also said the miner had been unwilling to address the group's complaints, which include backpayment on what the landowners say is the correct value of the land bought by Goldcorp and the construction of public works like a hospital.

Herrera said his client chose to take the case to Canada because the landowners believed the country's more rigid legal system would offer them more support than Mexican courts had.

"We're willing to dialogue with them," Herrera said. "But if this process doesn't lead to results, then we will sue them and we'll do it in Canada."

Peru silver mine strike ends after state intervention

LIMA, Dec 9 (Reuters) - Operations at Peru's Uchucchacua silver mine resumed over the weekend after the government ordered an end to a three-day strike, parent company Buenaventura said on Monday.

Buenaventura, Peru's largest publicly traded mining company, issued a statement saying "operations were immediately reinitiated" on Saturday after the labor ministry deemed the work stoppage illegal.

Metals production key to the Peruvian economy.

Workers at the Uchucchacua mine had been on strike since Wednesday demanding the restitution of 12 workers who were fired by Buenaventura.

Local labor union leader Segundino Romero said Uchucchacua miners went back to work not because their demands had been met but because the strike had been called off by the government.

"We have not reached a resolution to our demands, which included reinstating the fired workers," Romero said.

MARKET NEWS

BHP to pay 41 pct more to China copper smelters in H1 charges-sources

HONG KONG, Dec 9 (Reuters) - Miner BHP Billiton has agreed to pay a 41 percent rise in copper processing fees to China's large smelters for the first half of 2014, sources said, showing smelters are in a strong negotiating position as supply of concentrates rises.

The smelters and Anglo-Australian BHP have agreed to treatment and refining charges (TC/RC) of $99 per tonne and 9.9 cents per pound for term concentrate shipments in January to June 2014, two sources at smelters said on Monday.

That compares to the $70 and 7 cents the two sides negotiated for shipments in July to December 2013 and is more than the 2014 benchmark rate for full-year shipments.

The rise in the charges reflects an expected supply increase in the global copper concentrate market next year. More concentrate supply would encourage smelters to make more metal, which could pressure copper prices. The charges are higher than the 2014 benchmark of $92 and 9.2 cents agreed between Chinese smelters and other miners such as Freeport-McMoRan Copper & Gold Inc . But they are lower than the spot TC/RC of about $130 and 13 cents for clean, standard concentrates to China. Global miners pay TC/RC to smelters to convert concentrate into refined metal, with the charges deducted from the sale price, based on London Metal Exchange copper prices. Higher charges are typically seen when concentrate supply rises.

"We have settled with BHP at $99 and 9.9 cents for half-year shipments," said a source at a large copper smelter who had direct knowledge of the deal.

A manager at another large smelter said the firm had signed the same TC/RC with BHP and would continue to negotiate with the miner for full-year shipments. BHP had not given a new figure for full-year shipments to China after the smelters there rejected the miner's offer of $80 and 8 cents last month, he added.

"We don't comment on pricing," a BHP media relations manager in Australia said in an email to Reuters.

SUPPLY RISE

The deals with BHP were reflective of smelters regaining some negotiating power, said Michael Widmer, analyst at Bank of America Merrill Lynch. "It shows the current environment of having more concentrate supply coming through generally, but at the same time the smelters did not get the maximum that they wanted." Chinese smelters had planned to ask global miners to pay TC/RCs of about $105 and 10.5 cents for term shipments in 2014. A source at a miner said the jump between the initial offer by BHP to the Chinese smelters and the agreed TC/RC suggested the miner recognized its first offer might have been a bit ambitious. "I was surprised BHP is giving $99 and 9.9 cents. The strong charges reflect that miners are afraid they can't sell all production next year," a trader at a small Western miner said.

He added that TC/RCs for term shipments in July to December 2014 could be higher compared to the $99 and 9.9 cents for the first half as new projects were expected to come onstream and given that spot TC/RCs had risen more than 10 percent in the past month.

A deal for 30,000 tonnes of clean, standard African concentrate was sold at TC/RC of $130 and 13 cents last week to China, the trader said.

The bulk of the spot deals had changed hands at TC/RCs of about $115-$120 this month, compared to about $113-$115 in October and November, the sources at smelters said.

Kazakhmys sells power station stake as mine costs rise

LONDON, Dec 9 (Reuters) - Kazakhmys is selling its stake in Kazakhstan's largest power station for $1.3 billion, the copper miner said on Monday, boosting its finances as it also told investors that its Bozshakol mine would cost almost a fifth more than planned.

As well as a copper miner, Kazakhmys has been a major power supplier in Kazakhstan - accounting for over 20 percent of the country's power supply - but it has refocused on its core copper mining business in recent years, selling its stake in rival ENRC to the company's founders in October.

It said on Monday that Kazakhstan's sovereign wealth fund, Samruk-Kazyna, had agreed to buy the 50 percent stake in mammoth power station Ekibastuz GRES-1 that it does not already own - almost a year after talks over a sale were first disclosed. Press reports in February said the Ekibastuz deal could be struck for $1.6 billion, but analysts have since quoted a valuation of closer to $1 billion-$1.2 billion. Samruk bought the first 50 percent of the asset from Kazakhmys in 2009.

The deal also includes 100 percent of Kazhydro, a company established to develop hydropower plants in Kazakhstan.

Kazakhmys said in Monday's statement that the deal's net proceeds of about $1.25 billion would substantially strengthen its financial position during the development phase of its major copper growth projects, Bozshakol and Aktogay - key to turning the miner into a lower cost producer that will get the bulk of production from open-pit mines. But it also announced the budget at $1.9 billion Bozshakol had been raised by $350 million - the latest cost overrun in a mining industry that has frequently spent above planned amounts on growth projects, particularly mines built from scratch.

Kazakhmys, which has been running a cost review to cut back unnecessary spending, did not specify a reason for the budget overrun, but said it had appointed Non Ferrous China as a second principal contractor at Bozshakol. It said the development would keep it on track to begin production at the mine in 2015.

MARKET NEWS *(Continued)*

"We have been carrying the Ekibastuz asset at around $1 billion, so the sale value will be ... accretive," analysts at Nomura said in a morning note. "However the capex overrun at Bozshakol makes this pretty much a wash, net-net, on net present value." Shares in the miner were down 1.6 percent at 0900 GMT, lagging a 0.8 percent drop in the UK-listed sector.

China's daily steel output hits 2013 low in November

SHANGHAI, Dec 10 (Reuters) - China's average daily crude steel output fell for a second straight month to its lowest level in 2013 in November, as mills in the world's top producer trimmed production on softer demand ahead of winter.

Steel output fell to 60.88 million tonnes, falling 6.5 percent from October but still up 4.2 percent from a year earlier, data from the National Bureau of Statistics showed.

Daily production stood at 2.029 million tonnes, down 3.3 percent from October and the lowest level this year, according to Reuters' calculations. Steel demand usually falls away in November and December as cold weather slows construction activity in northern China, forcing mills to curb production.

"Tougher environmental measures and weak demand in the winter season will force mills to cut production further, though I still expect the average daily rate to stand around 2 million tonnes," said Jin Tao, an analyst with Guotai Junan Futures in Shanghai. Chinese steel futures rose less than 1 percent in November after falling more than 5 percent in the previous two months on limited growth in demand. Production reached 712.86 million tonnes in the 11 months from January to November, up 7.8 percent from a year ago, the data showed. China's crude steel output hit a record 716.5 million tonnes last year, up 3 percent from 2011. China's steel production is expected to rise to about 780 million tonnes this year and to increase further to 810 million tonnes in 2014, according to the China Metallurgical Industry Planning and Research Institute, citing improving economic conditions at home and abroad.

Indonesia trying to skirt its own ban on mineral exports

JAKARTA, Dec 9 (Reuters) - Indonesia's government is still seeking a way around a mineral ore export ban that the country's parliament insists remains in place, chief economic minister Hatta Rajasa said on Monday, as mining investors held out for a breakthrough.

The ban, which comes into effect next month, is designed to increase the value of the country's mineral exports. Indonesia, the world's top exporter of nickel ore, thermal coal and refined tin, has for decades and with limited success tried to create more value from its vast array of natural resources and hopes to develop processing industries to support its growing economy.

But a shortage of smelters in place threatens to cut output from mining companies in Indonesia such as Freeport-McMoRan Copper & Gold Inc and Newmont Mining Corp unless they find a way to meet or adjust the minimum processing requirements.

"We are trying to find a way, to find a solution. But that doesn't mean we are going to break the law ... We are going to talk again to parliament," Rajasa told reporters.

Freeport, the country's top exporter of copper and a major source of export revenue, is also seeking a way around the ban that could see its production cut by 60 percent or force it to stop operations completely. Newmont, which currently smelts less than a quarter of its ore domestically, has also warned it may have to halt operations at its Batu Hijau mine, which it operates in partnership with Japan's Sumitomo Corp.

The ore export ban has come at an unwelcome time for the government, as Indonesia scrambles to cut a large current account deficit that has been undermining confidence in its currency, Asia's weakest this year after falling around 20 percent to the dollar. Any cut in exports will only mean a bigger deficit. The authorities have been deliberately slowing growth in an attempt to cut imports and the current account deficit.

Late last week, lawmakers rejected a government bid to water down the ban by allowing mining companies to export unprocessed ore if they were able to show they were building smelters or were prepared to pay higher export taxes.

A complete ban would cost Indonesia billions in lost revenue from the mining sector, according to the Indonesian Mining Association (IMA). "Thousands of workers will be left unemployed ... I think the only ones who will survive will be Vale Indonesia and partly Antam," said IMA vice chairman Tony Wenas, referring to two companies that posses smelting facilities.

THRESHOLD

However, there is still room for the government to manoeuvre around parliament and the export ban, Wenas said, by adjusting its regulation that determines minimum purity thresholds for processing.

"The law only states that companies must process and refine their products domestically," Wenas told Reuters, pointing to a discrepancy between the minimum processing threshold for copper (99.9 percent) and nickel pig iron (6 percent) set out in a government regulation.

"To change the law, of course it's up to the parliament, but to change a regulation or a ministerial decree is the authority of the government," Wenas said.

Earlier, the Indonesian Mineral Entrepreneurs Association said it was also against the ban, which it said would destroy the domestic mining industry by cutting into profit margins.

The association said the law favours big international mining firms like Freeport-McMoran Copper & Gold Inc and Newmont Mining Corp that could afford to build smelters.

ANALYTIC CHARTS *(Click on the charts for full-size image)*

Daily LME Aluminium 3-months

Daily LME Copper 3-months

Daily LME Nickel 3-months

Daily LME Zinc 3-months

Daily LME Lead 3-months

Daily LME Tin 3-months

Daily LME Alloy 3-months

Daily LME Nasaac 3-months

THOMSON REUTERS

MARKET REVIEW

London copper hits one-month peak as dollar drops

SINGAPORE, Dec 10 (Reuters) - London copper hit a one-month high as expectations the Federal Reserve could soon start tapering its economic stimulus undermined the dollar, while steady consumer buying from China put a floor under prices.

Copper prices have begun to find traction in the past month as the global economy revives, but price prospects have been capped by expectations of a supply surplus next year.

"We are expecting demand conditions in the first quarter next year to be much more positive, not just in China ... but in the rest of the world as well," said analyst Matt Fusarelli of Sydney-based AME Group. Growth in China's factory output and investment eased slightly in November, while retail sales grew at their strongest rate this year, data showed on Tuesday, suggesting the economy is on track to achieve the government's growth target this year. AME has scaled back its expectations of a market surplus next year to 136,000 tonnes, with prices to average $7,300 in the first quarter. Actual copper supply typically falls short of forecasts given the technical hardships of accessing deeper ore deposits and prospects for unexpected events such as earthquakes in Chile, or more recently typhoon Haiyan's impact on Philippine smelter Pasar. Three-month copper on the London Metal Exchange was trading up 0.1 percent at $7,137 a tonne by 0703 GMT from the previous session. It earlier hit its highest since Nov. 12 at $7,155 a tonne. The most-traded February copper contract on the Shanghai Futures Exchange edged up 0.39 percent to 51,100 yuan ($8,400) a tonne, having also hit a one month peak at 51,220 yuan. The possibility that the Fed could start to temper its bond-buying policy as soon as next week continues to weigh on commodities, where climbing costs of capital could hit demand from industry and investors.

Conversely, a weaker dollar helps shore up demand for commodities which become less expensive for holders of other currencies. The euro was also supported by fading expectations of stimulus by the European Central Bank.

Chinese regulators will clamp down on banks' and companies' use of foreign currency for trade finance by ensuring that trade deals are authentic and by monitoring for unusual cross-border cash flows, state media reported.

"Right now, the impact is not severe but is becoming more pronounced. I don't think it will influence copper imports into China, it will only influence the arbitrage," said one trader in Singapore, adding his company is no longer able to issue letters of credit for some types of trade finance.

Physical demand for copper remains strong with bonded copper premiums trading up $5 at $195/$210 a tonne from month-ago levels, according to price provider Shmet.

"We might see some correction in the short term as the market has rallied $200, and Chinese banks are tightening on copper financing," said a broker in Hong Kong.

Elsewhere, base metals, led by nickel, appear set to trend higher in 2014 due to tighter supplies, while unfavourable economics should keep pressure on gold and oil and prompt investors to avoid much of the commodity complex, Barclays said on Monday. LME nickel CMNI3 prices have outperformed for the past two weeks, up around 3 percent, but the metal is by far the worst performer this year with losses of more than 18 percent.

Gold steady after 2-day gains, but taper worries linger

SINGAPORE, Dec 10 (Reuters) - Gold was steady after gaining 1.3 percent over the past two days, but trading volumes were thin as investors turned their attention to a U.S. Federal Reserve policy meeting next week.

Volumes on the futures market and the physical market were thin as investors waited on the sidelines for a clearer outlook on the U.S. central bank's commodities-friendly monetary stimulus measures. Spot gold had eased 0.1 percent to $1,239.39 an ounce by 0319 GMT. It had gained over the last two sessions on short-covering, technical-selling and some fund-buying.

"The short-term bullishness is unlikely to last through next week as speculators are likely to trade with more caution closer to the last FOMC meeting of the year," said Joyce Liu, investment analyst at Phillip Futures Pte Ltd, referring to the Fed's Federal Open Market Committee.

Markets worry the Fed could decide to begin cutting its $85 billion monthly in bond purchases at the Dec. 17-18 meeting due to recent strong economic data. The stimulus has supported gold prices as it boosts the metal's inflation-hedge appeal.

Gold has lost about a fourth of its value this year on fears the bond purchases would be scaled back. In comments made on Monday, two Fed officials also supported market views that the bank was close to tapering. St. Louis Fed President James Bullard said the Fed could slightly reduce its monthly bond purchases this month in reaction to signs of an improved labour market. Dallas Fed President Richard Fisher said he will urge his colleagues at the Fed's meeting next week to begin trimming their bond-buying program immediately.

DOLLAR WEAKNESS

The euro stayed well-bid on Tuesday, scaling a fresh five-year high on the yen and a six-week peak against the dollar as expectations for further stimulus from the European Central Bank continued to fade. A weaker greenback could support gold by making the dollar-denominated metal cheaper for holders of other currencies. "In the current environment, it appears further USD weakness is likely. This should provide some support for bullion," HSBC analysts said in a note. "Beyond that, we believe gold prices are more likely to stay in a tight trading range in the near-term, barring any major economic surprises."

MARKET REVIEW *(Continued)*

Euro advances as dollar, yen stay out of favour

SYDNEY/TOKYO, Dec 10 (Reuters) - The euro stayed well-bid , scaling a fresh five-year high on the yen and a six-week peak against the dollar as expectations for further stimulus from the European Central Bank continued to fade.

ECB Executive Board member Yves Mersch on Monday played down the prospect of following the Federal Reserve and Bank of Japan down the path of asset purchases, saying such action poses immense challenges for the central bank.

In fact, the ECB's balance sheet has been shrinking over the past year as the euro zone's financial system stabilises, in contrast to the Fed and the BOJ which continue to print money through asset purchases. That provides underlying support for the common currency, as does the euro zone's current account surplus, despite sluggish economic growth in the currency bloc.

The euro last traded at 141.95 yen after touching 142.085, a high not seen since October 2008. Against the dollar, the common currency bought $1.3755, up slightly from late U.S. levels and creeping ever closer to a two-year high of $1.3833 set in late October. The euro has been gaining ground since the ECB last week refrained from following up November's surprise rate cut and said it has yet to come up with a detailed plan of which policy tools to use and when. At the same time, there appears to be a general acceptance among investors that the Federal Reserve will soon scale back its bond-buying programme as the economy continues to improve. Indeed, Dallas Fed President Richard Fisher, seen as a hawk, said financial markets are in a "better position to accept" a reduction in stimulus than they have been before. More surprising for some traders were comments from centrist policymaker James Bullard, the St. Louis Fed president, who said the Fed could slightly reduce its monthly bond purchases this month in reaction to signs of an improved labour market. The Fed holds its policy meeting next week.

"That to me signals that when taper does happen it will be a token of faith to the markets," said Evan Lucas, a market strategist at IG in Melbourne. "I believe that any moves in the asset purchase programme will be a token affair as its second mandate of inflation is still well behind expectations."

TAPER TIMING

Economists polled by Reuters on Monday suspect the Fed will begin reducing its massive bond-buying programme in March, but some are warming up to the idea of a December or January taper. Traders said markets have pretty much priced in the risk of the Fed scaling back support soon, which might help explain why the dollar has not risen broadly in the past few sessions.

In fact, a robust euro has knocked the dollar index to its lowest level in six weeks.

Against the yen, though, the greenback held at 103.22 yen and was close to a five-year peak of 103.74 set in May.

The Japanese currency continues to be the funding currency of choice thanks to the BOJ's ultra-loose monetary policy and expectations of more easing next year when tax hikes kick in.

But one possible concern for yen bears is that support for Japanese Prime Minister Shinzo Abe dropped after he steamrolled through parliament a tough secrecy act that critics fear could muzzle media and allow officials to hide misdeeds.

"Given that investors have piled up huge yen-selling and Japanese share-buying positions solely on hopes of Abenomics, there is risk of reversal in these positions should Abe lose popularity," said Junya Tanase, chief FX strategist at JPMorgan Chase Bank in Tokyo. Another standout currency was sterling, which hit a two-year high against the dollar and a five-year peak against the yen, thanks to a brightening outlook for the UK economy. Bank of England Governor Mark Carney said on Monday the country's economic recovery is on its way to achieving self-sustaining momentum. Still, Carney said monetary policy will need to remain exceptionally loose for some time to come, although sterling bulls paid no heed to that.

The pound rose as high as $1.6468, surpassing a two-year high of $1.6443 set a week earlier It last traded at $1.6455, up 0.15 percent from late U.S. levels. Sterling also jumped to around 169.91 yen. The focus in Asia is likely to rest on China's industrial output and retail sales due around 0530 GMT.

Recent data has given hope the world's second-biggest economy is regaining some momentum since arresting a protracted slowdown in the middle of the year. Confirmation of that view will help underpin risk appetite.

(Inside Metals is compiled by Vikas Vasudeva in Bangalore)