INSIDE METALS

Thursday, May 23, 2013

CHART OF THE DAY

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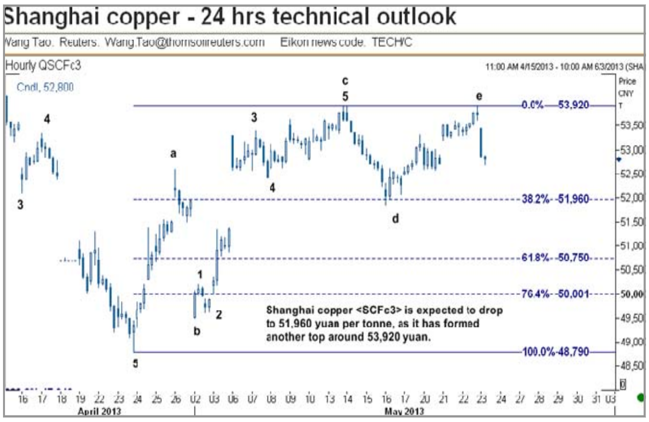

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FEATURE

COLUMN-China still favouring raw materials over metals

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Andy Home is a Reuters columnist. The opinions expressed are his own

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TODAY'S MARKETS

BASE METALS: London copper fell more than 2 percent after a preliminary survey showed China's factory sector contracted in May, hitting sentiment already soured by concerns the United States may pull back on its bond-buying program. "A reading under 50 is certainly not a good omen and weaker than what we would have expected," said Matt Fusarelli, analyst at consultancy AME Group in Sydney.

PRECIOUS METALS: Gold fell for a third straight session after U.S. Federal Reserve Chairman Ben Bernanke hinted at reducing an $85 billion bond-buying programme, which has increased the precious metal's appeal as a hedge against inflation. "It does not matter if the tapering off (of the bond buying) is in this quarter or next or delayed by six months," said Dominic Schnider, an analyst at UBS Wealth Management.

FOREX: The yen gained across the board bouncing sharply off a 4-1/2-year low against the dollar and notching up a two-week high against the euro after a whiplash move in stocks prompted investors to scramble for safety in Japanese bonds. "Bernanke didn't actually say they would give up on QE3 early, but market players decided to read it that way this morning ... the junior players were buying USDJPY before they realised the senior guys hadn't yet," said a trader at a major Japanese bank.

FEATURE

COLUMN-China still favouring raw materials over metals

By Andy Home

LONDON, May 22 (Reuters) - The world's largest buyer of industrial commodities is still favouring imports of raw materials over refined metals.

These were the twin themes of China's import appetite over the course of the first quarter of this year and the latest April figures show no significant change of pattern.

Good news for miners but less good news for refined markets that have, for now at least, lost a key bull driver.

Although each market has its own specific story when it comes to China's metal trade dynamic, the broad theme remains one of a country that is showing every sign of gradually shifting its import dependency upstream.

EXPORTS PICK UP

Imports of refined copper, aluminium, tin and lead were all soft last month.

Indeed, in the case of lead, China has returned to a marginal net exporter in the first part of this year. April's net exports were 2,456 tonnes, bringing the year-to-date outflow to 5,523 tonnes.

These are marginal tonnages, not much more than a drop in the global lead ocean. But you'd have to go back to the start of 2010 to find the last time China was a net exporter for five consecutive months.

It's all the more remarkable given the hefty 10 percent export tax on refined lead.

The underlying driver is the disconnect between an apparently well-supplied Chinese market and an international market characterised by a steady erosion of visible inventory.

There are signs that the Chinese market is tightening up again, most obviously in the form of a change of trend in stocks registered with the Shanghai Futures Exchange (SHFE) , but for now there is evidently sufficient availability for metal to seep out of the country.

There is also a possibility that more may be departing but in a form, such as lead plate, that doesn't make it into the headlines.

No danger yet that the world's biggest copper consumer is going to turn to net exporter.

But a steady counter-flow of refined metal, coupled with low imports, is damping China's call on the rest of the world's copper supply.

Exports came in at 29,000 tonnes last month, bringing the cumulative January-April total to 154,500 tonnes.

No surprise that the bulk of that material, 88,000 tonnes, has gone to Malaysia, given the well-documented incentives being offered by London Metal Exchange (LME) warehouses.

Whether the outflow is coming straight from those Chinese smelters qualified for preferential tax treatment or from Shanghai bonded warehouses is difficult to tell. Remember that what sits in Shanghai has already been counted as an import, which means that if it turns around and heads out again, it reappears as an export on the customs figures.

Less ambiguous is the 18,000-tonne export flow to Taiwan, a country with no registered LME warehouses.

Refined copper imports last month were 183,000 tonnes, the lowest monthly level since June 2011. Net imports of 154,000 tonnes were the lowest since May 2011.

China's net draw on refined copper from the international market has slumped by 570,000 tonnes this year relative to the same four months of 2012.

Quite evidently we are now in a major destock cycle as Chinese buyers draw down Shanghai bonded stocks, currently estimated at around 500,000 tonnes, compared with close to a million tonnes late last year.

IMPORTS WEAKEN (WITH TWO EXCEPTIONS)

Some sort of destock may also be taking place in the Chinese tin market, given that net imports of 801 tonnes last month were the lowest since May 2011.

It marks an acceleration of a trend that has been evident since February. At 5,500 tonnes net imports over the first four months of this year are already 3,700 tonnes lower than over the year-earlier period.

It's a similar picture for primary aluminium net imports, running 160,000 tonnes slower than last year at just 23,000 tonnes in January-April.

A figure that is dwarfed by the flow of metal out of the country in the form of semi-manufactured product. Exports have totalled 930,000 tonnes so far in 2013, a new record.

This component of China's trade dynamic in the light metal is starting to move on to analysts' collective radar and is worth watching closely over the coming months.

As ever when it comes to China's imports, there are exceptions to the rule, most notably zinc and nickel.

Net zinc imports of 45,000 tonnes in April were well off the pace of March's 73,000 tonnes but the cumulative year-to-date total of 187,000 tonnes is up 21 percent on last year.

This flow of metal largely reflects a combination of arbitrage and financing demand rather than Chinese physical shortfall.

Certainly, there is a stark contrast with the trend in imports of zinc alloy. This is firmly down with cumulative January-April imports of 36,000 tonnes the lowest since the first four months of 2009.

Nickel is another outlier with net imports of refined metal of 12,200 tonnes in April the strongest monthly flow since January. Cumulative imports are running 49 percent higher so far this year at 53,600 tonnes.

FEATURE *(Continued)*

It's fair to say there is a quite a lot of scratching of heads among analysts about these imports.

While there's no doubt that Chinese stainless steel output is strong, reflecting the broader strength in the country's crude steel production [ID:nL6N0E234N], there's also little doubt that China's own nickel pig iron production (NPI) is running equally strong.

RAW MATERIALS BOOM

Imports of Indonesian nickel ore, the key NPI input, may have eased slightly to 3 million tonnes in April but that shouldn't detract from the year-to-date trend.

Cumulative January-April imports totalled 14.5 million tonnes, up 32 percent on last year. And this time last year, remember, China was sucking in as much ore as it could from Indonesia ahead of that country's mid-year clampdown on exports of unprocessed minerals.

Another more comprehensive clampdown by the Indonesian authorities is planned for next January and it is possible that pre-emptive stock-building is already taking place.

It's noticeable that China's imports of Indonesian bauxite are also accelerating. April's total of 4.6 million tonnes was the highly monthly import level since May 2012, the month before last year's warning shot from the Indonesian authorities.

So too are imports of alumina from Australia, up 7 percent in the first four months of this year.

Again, importers may have one eye on Indonesian mineral policy but strong flows of both raw and intermediate materials in the aluminium-making process tally with continued strong production of the light metal in China. Also booming are China's imports of copper concentrates. Last months' tally of 839,000 tonnes (bulk weight) was the second highest ever inflow after December last year.

Cumulative imports are up a massive 37 percent on last year. Chinese smelters may be benefitting from increased supply resulting from the outage of India's Sterlite smelter.

But there is little doubting the broader message that China is pumping up its own primary smelting capacity.

Secondary production, meaning that from scrap copper, is suffering with Yunnan Copper Industry Company the latest to join a growing list of companies idling capacity due to poor scrap availability.

Copper scrap imports have fallen by almost 5 percent so far this year and April's total was again low at 337,000 tonnes.

But the cumulative drop in tonnage terms so far this year has been just 67,000 tonnes.

That in itself does not explain the crunch on scrap availability in China, suggesting that other drivers are at work, most likely the withholding of supply by scrap traders due to lower prices.

The scrap crunch will at some stage force import demand back into the refined segment of the refined copper market, but there remains the suspicion that domestic supply might miraculously recover on any price strength.

--Andy Home is a Reuters columnist. The opinions expressed are his own--

GENERAL NEWS

China factory activity shrinks for first time in 7 mths - flash PMI

By Aileen Wang and Koh Gui Qing

BEIJING, May 23 (Reuters) - China's factory activity shrank for the first time in seven months in May as new orders fell, a preliminary manufacturing survey showed, entrenching fears that its economic recovery has stalled and that a sharper cooldown may be imminent.

The flash HSBC Purchasing Managers' Index (PMI) for May fell to 49.6, slipping under the 50-point level demarcating expansion from contraction for the first since October. The final HSBC PMI stood at 50.4 in April.

The lack of vigour in the world's second-biggest economy implies its ability to meet the government's 7.5 percent growth target this year is increasingly difficult, analysts said, albeit it is still possible.

The soft data also sharpens Beijing's policy dilemma over whether to act to stabilise activity, or tolerate an orderly slowdown while focusing on reducing the country's dependence on exports and investment for growth, changes that would bring longer-term benefits.

Yao Wei, an economist at Societe Generale in Hong Kong, said the debate favours policy inaction from Beijing for now, as long as economic growth remains above 7 percent.

"We don't think it will trigger any cyclical policy move as long as the job market is fine," she said.

"China is really on a path of structural (growth) deceleration. It's possible (to meet the growth target) but it's becoming increasingly difficult."

The PMI survey suggested China is up against weakness both at home and abroad. A sub-index measuring overall new orders dropped to 49.5, the lowest reading since September, suggesting domestic consumption is not strong enough to offset soft global demand.

Asian stock markets extended early losses after the report. Oil, copper and rubber prices also retreated, while the Australian dollar skidded.

GENERAL NEWS *(Continued)*

Thursday's PMI revived investor worries about whether China can sustain an economic revival this year, after annual growth slumped to a 13-year trough in 2012. China's factory output and investment performance for April released earlier this month had already underwhelmed markets.

The run of dismal data reports have prompted economists to slash their growth forecasts for China.

UBS this week downgraded its 2013 growth target for China to 7.7 percent, from 8 percent, and Societe Generale is in the midst of lowering its estimates. Bank of America-Merrill Lynch cut its China 2013 growth forecast earlier this month to 7.6 percent from 8 percent.

If the economy meets the government's growth target and expands 7.5 percent this year, it would still be its worst performance in 23 years.

ALL ABOUT JOBS

The HSBC flash PMI comes about a week before the final reading and is the earliest indicator of how the Chinese economy is faring each month.

The PMI survey showed new export orders hovered below the 50-point level in May, though the rate of decline slowed from April.

Still, the weak showing implied foreign demand remained lethargic due to a patchy U.S. recovery and Europe's nagging debt crisis, and echoes weak export momentum seen in Taiwan and South Korea in May.

In a reflection of the cooldown in the vast factory sector, both indices for input and output prices stayed muted in May to be near troughs seen in the third quarter last year.

"A sequential slowdown is likely in the middle of the second quarter, casting downside risks to China's fragile growth recovery," said Qu Hongbin, an economist at HSBC.

Yet, barring a slump in the labour market, most analysts believe Beijing will opt to stay on the policy sidelines. Measures such as reducing corporate taxes may be enacted, but only as part of broader tax reforms, not to pump-prime growth.

A stable employment market ranks high among China's policy priorities as the Communist Party justifies its one-party rule with tacit promises of economic prosperity.

Although Chinese media has reported that a record 7 million graduates will join the labour force this year, there are few reports of widespread discontent among job hunters. Thursday's PMI also showed pointed to a stable employment market.

And Chinese leaders on their part appear to be comfortable for now with moderating economic growth.

Chinese Premier Li Keqiang said last week the country has limited room to rely on government spending or policy stimulus to spur its growth, dispelling market speculation that Beijing may act to pump-prime its economy.

At the depth of the global financial crisis in 2008/09, an estimated 20 million rural migrant workers lost their jobs, prompting Beijing to unveil a 4 trillion yuan stimulus package to shore up the economy and guarantee employment.

The latest sputter in China's growth engine is clearly taking a toll on its corporate sector, but there are no signs of major defaults on loans.

Among China-listed companies which have posted their first-quarter earnings, 67 percent missed market expectations, ThomsonReuters data showed.

Zoomlion Heavy Industry Science and Technology Co Ltd , China's second largest construction equipment maker, reported a 72 percent plunge in its first-quarter earnings from a year earlier.

Government data this week also showed that profit growth in China's giant state firms cooled in the first four months of the year.

Mexico says mine industry investment could rise a bit through 2018

By Gabriel Stargardter

MEXICO CITY, May 22 (Reuters) - Mexico sees total mining investment between 2013-2018 of at least $25 billion, holding steady or rising slightly from the previous six years despite the prospect of less favorable metals prices, Mexico's top government mining official told Reuters on Wednesday.

"We estimate total investment for the (president's) six year term could be above or around $25 billion or $26 billion," Mario Cantu Suarez, Mexico's chief mining official, told Reuters at the BNAmericas Mexico mining summit.

Over the six-year term of former president Felipe Calderon, when metals prices saw an unprecedented boom thanks to top commodity buyer China, total investment reached $25 billion, with foreign companies accounting for 40 percent.

Driven by Chinese demand, commodity prices soared in recent years, and Mexico's mining income grew 134 percent between 2009-2011. Mining is now Mexico's fourth largest industry in dollar income, behind automobiles, oil and electronics, according to official data.

"We saw an impressive boom," Cantu Suarez said.

He hoped that a national development plan recently unveiled by the government could spur investment and counter the drag of lower metals prices and a proposed 5 percent royalty scheme passed by Mexico's lower house of Congress.

Some foreign companies have said they will, or already have, decreased investment as a result of the proposed royalty.

"Where is the profitability?" Cantu Suarez said. "Many mines stop operating when profits are insufficient."

MARKET NEWS

Glencore, Trafigura deals with Iran may have skirted sanctions -UN

By Louis Charbonneau and Michelle Nichols

UNITED NATIONS, May 22 (Reuters) - Metals swap deals with Iran by Switzerland-based commodities giants Glencore Xstrata and Trafigura [TRAFG.UL] could have been a way of skirting international sanctions against Tehran over its nuclear program, according to a confidential U.N. Panel of Experts report seen by Reuters on Wednesday.

Reuters reported on March 1 that Glencore had supplied thousands of tons of alumina to an Iranian firm that has provided aluminum to Iran's nuclear program, an allegation Glencore confirmed as accurate. Afterward, Trafigura acknowledged it had also traded with the same Iranian firm.

Swiss authorities said at the time that they saw no evidence of U.N. or Swiss sanctions violations by Glencore, but the U.N. experts, who monitor compliance with the Iran sanctions regime, raised the possibility that the swap deals were a means of flouting restrictions on trade with Iran.

"If confirmed, such transactions may reflect an avenue for procurement of a raw material in a manner that circumvents sanctions," the 49-page report said in reference to the media reports on the swap deals. "The companies involved have stated that they have halted those transactions."

Reuters has sought comment from both companies regarding the report, which was delivered to the U.N. Security Council's Iran sanctions committee earlier this month.

Reuters reported on Tuesday that Glencore's head of aluminum, Gary Fegel, is set to leave the company, the first high-profile departure since the commodity trading giant closed its purchase of miner Xstrata this month. The timing and reason for his exit after 12 years at Glencore are unclear.

The experts' annual report said they have found evidence that Tehran routinely attempts to flout the sanctions applied against Iran over its nuclear program, which Western powers and their allies suspect is aimed at producing weapons but the Iranians say is for peaceful electricity generation.

"Iran continues to seek items for its prohibited activities from abroad by using multiple and increasingly complex procurement methods, including front companies, intermediaries, false documentation, and new routes," the experts said.

"These require additional vigilance and expertise on the part of states in order to identify suspicious transactions," it said.

The panel listed 11 violations by Iran since June 2012 and said it has at least six ongoing investigations into possible sanctions violations, including the export of machine tools reported by Spain and the export of technical equipment for use in satellite technology reported by Germany.

The United States reported transfers and attempted transfers of items linked to Iran's nuclear program, including vacuum equipment for test stands, pressure transducers, vacuum pumps and materials for fabrication of centrifuge machine components like magnetic tape, marching steel and aluminum alloys.

The United States also reported a violation involving the transfer of specialized metals to several entities in Iran associated with the ballistic missile program.

The experts said Iran had not demonstrated any significant new missile capabilities in the past year, but had continued to violate Security Council resolution by launching missiles.

"Despite at least the partial success in making its ballistic missile program indigenous, Iran remains reliant on foreign suppliers for technology, some components and raw materials," the panel said.

"Preventing supply of these items is critical for international efforts to slow Iran's prohibited ballistic missiles activities," it said, while noting that "no significant new missile capabilities" had been demonstrated by Iran.

Even top Europe steel firms at risk unless output cut

LONDON, May 22 (Reuters) - The European steel sector in under pressure to cut production quickly as overcapacity and weak global demand threaten even some of the most important plants, the chief executive of Italian steel manufacturer Marcegaglia said.

Italy, Europe's second-largest producer, has been hit particularly hard by the demand slowdown, and the future of some of its biggest steel operations including the Riva-owned Ilva plant, stainless steel plant Acciai Speciali Terni and steel producer Lucchini is at risk.

"We are probably on the eve of a redefinition of the whole outlook," Antonio Marcegaglia said in an interview on Wednesday. "If we think about Italy, for example, Riva, Terni and Lucchini are important pieces of the industry that are going through epochal changes."

Although state subsidies are "no longer conceivable", the government should consider using some public funds to cushion the impact of plant closures on their workers, the Italian entrepreneur said.

Difficulties in getting financing are an additional problem affecting many industry players.

Marcegaglia said banks were still supporting his company but that some of his customers were suffering from a lack of funding.

"Indirect financial restrictions dictate we have to pay more attention to who to work with and for what sort of volumes," he said.

"Obviously in this context we are paying attention to cash flow and are targeting a reduction of our debt."

MARKET NEWS *(Continued)*

In order to strengthen its cash position and be able to dedicate more time and resources to its main activities, Marcegaglia is selling some non-core assets.

The Italian company is in "advanced negotiations" with French industrial group Fivs over the sale of engineering firm Oto Mills, Marcegaglia said.

It has also sold luxury tourist complex Forte Village, in Sardinia, to a Russian group based in Chechnya, he added.

Another asset potentially up for sale is Euro Energy Group, a subsidiary that focuses on renewable energy.

Marcegaglia's core business, steel manufacturing, has been able to maintain similar sales volume levels compared with last year despite steady to slightly lower demand in Europe.

The group overall had a turnover of 4.2 billion euros ($5.4 billion) last year, little changed from the year before.

The near future does not appear bright, however.

"I am not particularly optimistic on the developments of the European market this year," Marcegaglia said.

"Margins for all products are under pressure. Overcapacity in Europe is now a structural issue that we all have to face."

Outokumpu plans daily alloy surcharge pricing

By Silvia Antonioli and Ritsuko Ando

LONDON/HELSINKI, May 22 (Reuters) - Finland's Outokumpu is proposing to price alloys in its stainless steel products on a daily rather than monthly basis to reflect cost volatility and to limit speculation over the materials which form most of the price of the high-end steel.

The European stainless steel price is currently composed of two elements, a base price, agreed between the mill and the customer on a monthly, quarterly or longer basis and a monthly alloy surcharge, which today represents the biggest part of the total price.

"We are going to pilot a daily alloy surcharge... A daily mechanism is well tested in other industries, for products such as aluminium," the company chief executive Mika Seitovirta said during an event organized by the producer for its customers.

"Customers will also get the flexibility to decide whether to fix the alloy surcharge on the day of the order or the day of the delivery."

The monthly alloy surcharge is calculated using a formula based on the average price of nickel and of other alloys present in stainless steel, for the month before the booking.

With the current pricing mechanism, stockholders and other buyers can guess how the alloy surcharge is going to move before the number is formally announced by the mills and can modify their buying behaviour accordingly.

This has annoyed some producers in the past and led to Luxemburg-based stainless steel producer Aperam to call for a change in the mechanism last year.

Many clients also seemed open to a change in the pricing structure.

"Without doubt the current mechanism leads to excessive speculation and deserves to be modified," Antonio Marcegaglia, chief executive of Italian steel manufacturer Marcegaglia, told Reuters.

"Today we all have to be speculators rather than industrial players and many clients take buying decisions based not on distribution capacity or customer demand but on the alloy surcharge level."

The daily system Outokumpu proposed is one way to improve the situation but a second solution would be to reduce the weight of the alloy surcharge on the total price of stainless steel, Marcegaglia said.

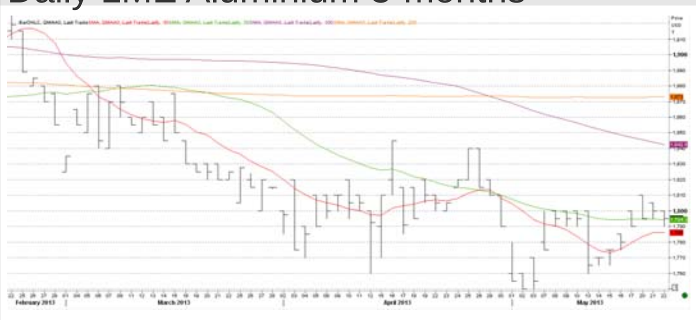
Asian producers already offer a daily alloy surcharge which more closely tracks the daily movement of the nickel price, a key element of the charge.

This allows foreign producers to lure more European buyers when nickel prices are falling.

"We believe it will reduce volatility that we have got now in the market, when nickel prices go up and down, and (will reduce the need for) imports, which offer daily surcharge, as we can do the same in Europe," Ulrich Albrecht-Fruh, president of the EMEA stainless steel coil department of Outokumpu told Reuters on the sidelines of the event.

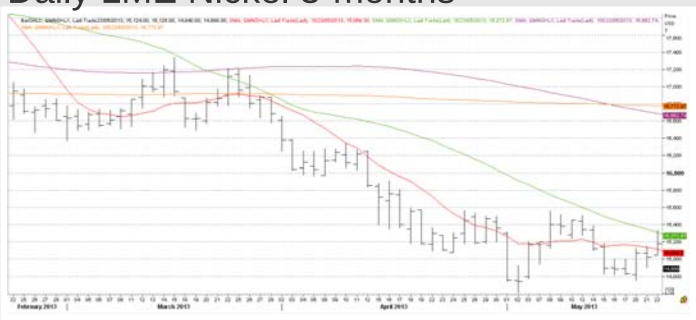
ANALYTIC CHARTS *(Click on the charts for full-size image)*

Daily LME Aluminium 3-months

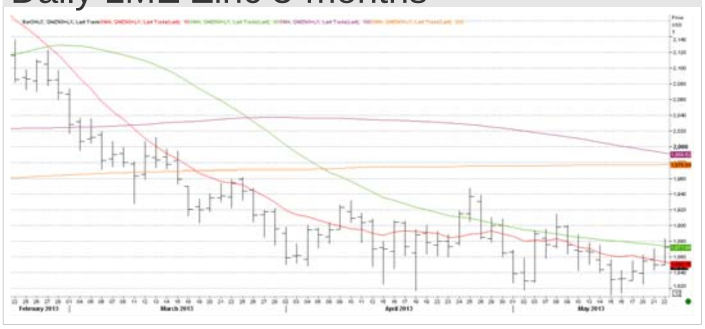


Daily LME Copper 3-months

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

MARKET REVIEW

METALS-Copper slides more than 2 pct as China factory data disappoints

By Melanie Burton

SINGAPORE, May 23 (Reuters) - London copper fell more than 2 percent after a preliminary survey showed China's factory sector contracted in May, hitting sentiment already soured by concerns the United States may pull back on its bond-buying program.

China's factory activity shrank for the first time in seven months in May as new orders fell, the survey of purchasing managers showed, adding to concerns that a recovery in the world's second-largest economy is sputtering.

"A reading under 50 is certainly not a good omen and weaker than what we would have expected," said Matt Fusarelli, analyst at consultancy AME Group in Sydney.

China is the world's top copper consumer, accounting for 40 percent of refined demand.

Also hurting sentiment were fears about the U.S. Federal Reserve tapering its bond-buying program earlier than expected, eroding liquidity and investment capital available for metals.

"For so long people have taken for granted that money will be free. But as soon as it's not free, then that's when we are going to see big ruction in metals markets," Fusarelli added.

Fed Chairman Ben Bernanke said on Wednesday a decision to scale back the $85 billion in bonds the central bank is buying each month could come at one of its "next few meetings" if the economy looked set to maintain momentum.

Three-month copper on the London Metal Exchange fell 2.4 percent to $7,296.50 a tonne by 0230 GMT, erasing gains from the previous session when it hit a six-week high of $7,533.75 and closed up 1.4 percent.

The most-traded September copper contract on the Shanghai Futures Exchange lost 1.76 percent to 52,540 yuan ($8,700) a tonne.

Still, a series of mining accidents and plant shutdowns this year have pushed copper's supply back under the spotlight, supporting prices. The global market for copper is expected to swing into a small surplus this year after several years of deficit.

Last week's shutdown at the world's second-largest copper mine run by Freeport McMoRan Copper and Gold Inc in Indonesia will extend until the company is convinced of the mine's safety, it said. A rockslide at Rio Tinto's mine in Utah had also cut production.

India's top copper smelter, run by Sterlite Industries , also remains shut as a court continues hearing into complaints of emissions.

PRECIOUS-Gold slips after Bernanke hints at slowing bond purchases

By A. Ananthalakshmi

SINGAPORE, May 23 (Reuters) - Gold fell for a third straight session after U.S. Federal Reserve Chairman Ben Bernanke hinted at reducing an $85 billion bond-buying programme, which has increased the precious metal's appeal as a hedge against inflation.

While Bernanke said the central bank needs to see further progress in the U.S. economy before the Fed scales back monetary stimulus, he also added that a decision to adjust it could come in the "next few meetings" if the economy looked set to maintain momentum.

Down nearly 20 percent this year, gold could come under more selling pressure as investors increasingly price in a stimulus cut ahead of the Fed's next policy meeting on June 18-19.

Spot gold fell 0.06 percent to $1,367.66 an ounce by 0327 GMT. It hit a low of $1,356.24 earlier in the session, near a two-year low of $1,321.35 plumbed in April.

"It does not matter if the tapering off (of the bond buying) is in this quarter or next or delayed by six months," said Dominic Schnider, an analyst at UBS Wealth Management.

"If you know it's tapering off anyhow in the next 12 months, people do not want to be in there anymore."

Sustained outflows from exchange-traded funds also point to more downside for gold prices.

Holdings in SPDR Gold Trust , the world's largest gold-backed exchange-traded fund, fell 0.3 percent to 1,020.07 tonnes on Wednesday, the lowest in more than four years. U.S. gold futures eased 0.06 percent to $1,366.60 an ounce. Spot silver , platinum and palladium tracked gold lower.

DEMAND CONCERNS

China's factory activity shrank for the first time in seven months in May as new orders fell, a preliminary survey of purchasing managers showed, adding to concerns that a recovery in the world's second-largest economy and No. 2 gold consumer is sputtering.

The contraction is an "alarming sign", said UBS' Schnider at a time when physical gold demand in Asia has been normalising.

Premiums for gold bars hit a record high in Asia on Wednesday as lower spot prices lured more buyers, mainly in China, amid tight physical supplies.

Top gold buyer India, which had seen gold imports jump 138 percent in April, is facing a slowdown as the peak wedding season comes to an end and its central bank imposes new rules to reduce a deficit.

MARKET REVIEW *(Continued)*

FOREX-Yen firms as China PMI sparks flight to debt; Aussie languishes

By Sophie Knight

TOKYO, May 23 (Reuters) - The yen gained across the board bouncing sharply off a 4-1/2-year low against the dollar and notching up a two-week high against the euro after a whiplash move in stocks prompted investors to scramble for safety in Japanese bonds.

The yen was squeezed 1.5 percent up to 101.62 yen after investors took weak Chinese factory data as an excuse to topple the Nikkei from a 5-1/2-year high, sending it plummeting 7.3 percent and prompting a rush for Japanese debt.

If the dollar fell to 101.14 yen, it would mark a 23.6 percent retracement of its rally between April 4 and May 22.

That was a sharp reversal from Wednesday, when the greenback raced to a fresh 4-1/2-year high of 103.74 yen after Fed chief Ben Bernanke told Congress that the central bank could "in the next few meetings take a step down" in its bond purchases. On Thursday, the market began to focus on Bernanke's caveats that any decision to reduce its buying would not mean the Fed would automatically push for a complete roll back of the stimulus, and that it could yet raise the pace of purchases depending on how the economy evolves.

"Bernanke didn't actually say they would give up on QE3 early, but market players decided to read it that way this morning ... the junior players were buying USDJPY before they realised the senior guys hadn't yet," said a trader at a major Japanese bank.

"The smart people who were long on the dollar-yen sold it at 103. On top of that, the Nikkei's fall meant people had to unwind their FX hedges on equities and sell dollars," he added.

The Nikkei's tumble helped the 10-year Japanese bond yield come down to 0.825 after it hit 1.000 percent earlier in the session, its highest in more than a year, after U.S. Treasury prices beat a hasty retreat overnight. The yen's gains were most dramatic against the Australian dollar , which tumbled 1.8 percent to 98.20 yen to a 7-week low after data showed factory activity in China shrank for the first time in seven months in May.

The flash HSBC Purchasing Manager's Index (PMI) for China, Australia's biggest export market, dropped to 49.6 in May, slipping under the 50-point level demarcating expansion from contraction for the first time since October.

That left the Aussie languishing 0.9 percent down at $0.9608 and fast approaching its June 2012 trough of $0.9581. The currency has shed 7 percent this month as the U.S. dollar has surged across the board and the central bank surprised with a rate cut.

The firmer yen took a stand against the euro too, racing up 2.1 percent to 130.40 yen , its highest since May 9. The euro was sluggish against the dollar, dropping 0.2 percent to $1.2836 to approach its 6-week low of 1.2796 hit on May 17.

The dollar index was off 0.2 percent from late U.S. levels on Wednesday, when it squeezed up to 84.498, a peak not seen since July 2010, on the prospect that the Federal Reserve might scale back its stimulus programme this year.

The dollar's recent resurgence has convinced some market participants that it could yet stretch as far as 105 yen in the near future.

"From the beginning of May, the yen's slide slowed down or stopped against a number of currencies, but the dollar's broad strength means it continues to slide against USD," said Minori Uchida, chief FX analyst at the Bank of Tokyo-Mitsubishi UFJ.

"Everyone said it would be hard for it to get over 95, 100, and 103, so I don't think there's much blocking it from 105...as long as the factors that have driven dollar strength don't change, putting a floor under the yen will be difficult."

The yen is still down 3.4 percent against the dollar since the beginning of May, compared to 1.6 percent against the euro . Against the Aussie, the yen has actually gained 3.2 percent this month.

"The Aussie is suffering because of the weak Chinese data that came out. So unfortunately for commodity currencies, it still looks pretty negative in the short term," said Mitul Kotecha, head of global FX strategy at Credit Agricole in Hong Kong.

(Inside Metals is compiled by Pradip Kakoti in Bangalore)