INSIDE METALS

Thursday, May 24, 2012

CHART OF THE DAY

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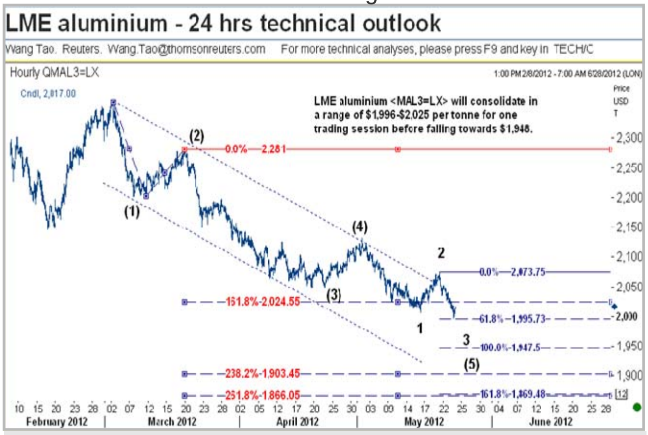

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COLUMN- Steel output up but price pressures build

Global steel production edged up to a new all-time high of 1.562 billion tonnes annualised in April, according to the latest estimate from the World Steel Association (WSA). But momentum is fading.

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

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TODAY'S MARKETS

BASE METALS: London copper rose 0.8 percent on Thursday as the market took a breather after sinking to a 4-1/2 month low in the previous session on risk aversion triggered by worries over Greece's possible exit from the euro zone. "Prices of copper have come off quite heavily in recent weeks so there might be some sense that maybe it was an overreaction," said Alexandra Knight, an economist with National Australia Bank. "From my perspective Greece will ultimately stay in the euro zone as there will be a lot of resistance to letting it exit."

PRECIOUS METALS: Gold hovered near $1,560 an ounce on Thursday, remaining on shaky ground as worries about Greece and the euro zone continued to dominate market sentiment after a European Union summit yielded few practical steps to manage the debt crisis. "Clients are not too interested in entering the market right now," said a Singapore-based dealer. "They are worried that if Greece eventually pulls out of the euro zone, the euro will fall and drag gold down with it."

FOREX: The euro hovered just above its 22-month low against the dollar on Thursday and remained vulnerable to further declines as the prospect of a Greek exit from the euro zone kept investors on tenterhooks. "It's still hard to see what the endgame will be like," a trader at a Japanese bank in Tokyo said.

FEATURE

COLUMN-Steel output up but price pressures build

By Andy Home

LONDON, May 23 (Reuters) - Global steel production edged up to a new all-time high of 1.562 billion tonnes annualised in April, according to the latest estimate from the World Steel Association (WSA).

But momentum is fading.

April's year-on-year growth rate was a meagre 1.2 percent and cumulative growth over the first four months of this year was just 0.8 percent, compared with 7 percent last year and 15 percent in 2010.

Moreover, steel prices just about everywhere are falling, a sign of spreading demand weakness and a warning that current production rates are unsustainable beyond the very short term.

Graphic on World steel production:

http://link.reuters.com/jec64s

Graphic on US and European HR coil price:

http://link.reuters.com/kem95s

Graphic on US PMI vs. steel price:

http://link.reuters.com/jem95s

Graphic on Shanghai steel price and iron ore price:

http://link.reuters.com/cep38s

CHINA...RUNNING ON EMPTY?

Nowhere is the disconnect between production and price so stark as in China.

National production hit a fresh annualised high of 737 million tonnes in April and the higher-frequency data provided by the China Iron and Steel Association (CISA) suggest run-rates only accelerated further in the first part of this month.

Yet Shanghai steel futures have been sliding since mid-April, the downtrend accelerating over the last 24 hours. The most active rebar contract on the Shanghai Futures Exchange slumped more than 2 percent to a seven-month low today.

Rebar steel is used in the construction sector and the Shanghai contract's precipitous slide is signalling weakness in what has been one of the pillars of Chinese steel demand.

Falling property prices may be a sign that the government's engineered cooling of the residential construction sector is working.

But the by-product has been a sharp slowdown in new construction activity.

Real estate investment growth fell to 19 percent in April from 28 percent in January-February. Analysts at China International Capital Corp estimate floor space under construction slumped 60 percent in March.

Against such a backdrop in such a key demand sector, Chinese steel production strength has simply fed accumulating inventories and accelerating exports.

Steel mills are operating at compressed margins, if they're achieving any margins at all.

Some sort of domestic market rebalancing looks overdue and the first tangible sign of pending reconnect between price and output may be the sliding iron ore price as Chinese mills defer raw material cargoes.

Since China has been the single-biggest driver of global steel production growth this year, the impact of an overdue slowdown in the country's run-rate is hard to overstate.

Production in the world outside of China was flat in April and marginally lower year-on-year in the first four months of the year.

PRICING TENSION IN THE US

That, though, masks very divergent production trends.

The stand-out performer so far this year has been North America, and the U.S. in particular, where annualised steel production in April of 94 million tonnes was the highest since September 2008.

Rising production has reflected robust demand from the automotive industry and from niche markets such as tube for the oil and gas sector.

But here too, there is a growing disconnect between production and price.

Hot-rolled coil prices, as assessed by The Steel Index, peaked above $700 per tonne in January and have been softening ever since to a current $652.

Moreover, the relationship between steel prices and the purchasing managers index has broken down in the last month or so, with the former falling and the latter still rising.

This pricing tension is signalling oversupply, a combination of strong domestic production and higher imports, even in what has so far been the strongest regional steel market.

And, in more muted form than in China, it also suggests some sort of rebalancing between local supply and demand is pending.

EUROPEAN WEAKNESS SPREADS

That rebalancing is already taking place in Europe and the result is a steady slowing of steel run-rates.

Year-on-year growth in April was negative at 5.2 percent in the EU-27 region, extending a trend that dates back to October of last year.

What is noticeable in the latest WSA figures is the spread of production weakness across the continent.

Previous stand-outs such as Italy and France last month joined the list of countries with negative steel output growth.

FEATURE *(Continued)*

Moreover, the trend of softening production is spreading to both CIS countries, where output fell by 5 percent in April, and to Turkey, where production growth has braked sharply from 14 percent in January to 5 percent in April.

Here the core price weakness is emanating from the Black Sea billet market, reflecting an absence of anticipated demand from the Middle East construction sector.

THE ONLY WAY IS DOWN?

Steel production is a lagging indicator of the state of the global manufacturing economy.

April's record output, therefore, says much about market expectations a few months ago.

Chinese steel mills were confident that it would be "business as usual" in the country's giant construction sector after the New Year holidays.

North American mills were capitalising on higher prices predicated on unexpectedly strong demand for their products.

And even in Europe the bigger steel-producing nations such as Germany, Italy and France were still riding buoyant export markets and steady if unexciting domestic demand.

Today recession in the euro zone is starting to look like a best-case scenario, relative to the likely fall-out from a Greek exit.

North American mills are now starting to feel the pinch from sliding steel prices.

And Chinese mills have started cancelling and deferring iron ore contracts, a sure sign of margin distress and a problematic outlook.

Steel prices are now reflecting this collective shift in market dynamics.

It's only a matter of time before production also readjusts.

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

GENERAL NEWS

Natixis bullish on metals hedging after unit shutdown

By Eric Onstad

LONDON, May 23 (Reuters) - Volatile markets and complex ore bodies are driving more mining firms to lock in prices for their output, said French bank Natixis, which is focusing on commodity hedging after deciding to shut its less lucrative commodities brokerage unit.

Natixis said earlier this month it would continue its over-the-counter (OTC) commodities business, but wind up the brokerage activities, including floor trading at the London Metal Exchange.

The OTC business largely consists of hedging and the bank is confident it can expand that area in conjunction with finance activities where companies take out loans and lock in commodity prices in one package, two executives told Reuters.

"The hedging business is picking up because of the increased volatility. You can't afford to ignore it," Henrik Wareborn, global head of commodities, said in an interview.

Mining offers more opportunities than the energy sector due to the fragmented state of the industry, he added.

"The mining industry is much less consolidated than the global oil sector so there is more need for mining projects to be hedged because there's higher leverage there."

Even though most major gold companies have renounced hedging under pressure from shareholders, Wareborn said hedging for precious metals has seen a revival because many new mines have mixed resources.

"Over the last two years, you are seeing more resources that are being developed where you have base metals and precious metals. Especially where you have precious metals as a by-product, they are tending to want to hedge all of that."

Natixis also has a good business on the other side of the market with consumers of metals and energy who want to insure against price rises, which nicely dovetails with producer hedging activities.

"Consumers come to us to hedge because they know we are strong with producers and we can offer aggressive prices," Wareborn said.

Clients include airlines, aircraft producers, automakers and even luxury goods companies that hedge precious metals exposure, he added.

LIQUIDITY CONSTRAINTS

Natixis decided to shut the brokerage and clearing activities because they consumed significant amounts of liquidity and capital while having limited profit potential compared with the OTC business, said Pierre-Henri Denain, UK country manager and head of capital markets.

Natixis has declined to give details of the turnover of its brokerage activities, but 2011 financial statements for UK unit Natixis Commodity Markets Ltd (NCM) show income from operations fell 10.6 percent from 2010 to $51.6 million.

The financial data, filed at UK Companies House, showed profit on ordinary activities before tax tumbled 45 percent to $11.1 million. The bulk of NCM's business is brokerage and clearing activities although some OTC business was also included.

GENERAL NEWS *(Continued)*

Denain said that while all European banks have constraints in accessing dollar financing in the current environment, Natixis benefits from its integration in the unlisted BPCE Group, France's second largest retail bank.

"The message is very much one of discipline and being very careful with how we use scare resources, but it is not a stressed environment for us, it might be for others," he said.

"In the new world, clearly liquidity is limited and more expensive and that's an issue and affects the profitability of the business, but how it affects you very much depends on the competitive landscape."

The European debt crisis has sparked a shake-up among French banks. In the past six months, Credit Agricole , BNP Paribas and Societe Generale have all taken steps to cut exposure to dollar financing, reduce debt and boost capital ratios.

Natixis competes with other French banks in commodity trade finance, where the country's financial institutions have traditionally been leaders.

Since the Natixis OTC commodity business does not include exchange traded funds and index products like many big banks, it has more room to expand hedging activities and is not in as much danger of coming up against regulatory limits.

"Up until recently it was unfashionable to be a medium-sized player, but now it's good because it's the big players who are coming up against these limits and it's very difficult for them to increase any business," said Wareborn

Indonesia exempts 2 miners from unprocessed ore export ban

JAKARTA, May 23 (Reuters) - Indonesia granted permission to miners PT Aneka Tambang (Antam) and PT Sebuku Lateritic Iron Ores to export unprocessed ore, despite a new regulation intended to stop raw mineral exports, the trade ministry said on Wednesday.

The two companies are the first to be approved from 20 that have applied for exemption from the regulation that was announced earlier this month, a senior trade ministry official said.

"The trade ministry has approved two companies as registered mineral exporters ie PT Antam and PT Sebuku Lateritic Iron Ores. The two companies can export mineral ores abroad," he said.

Miner Hochschild says YPF won't dull Argentina's shine

By Clara Ferreira-Marques

LONDON, May 23 (Reuters) - Argentina's soaring inflation is more likely to dent the country's appeal for miners eyeing its gold, silver and copper reserves than Buenos Aires' takeover last month of its biggest oil firm, YPF, the chief executive of miner Hochschild said.

Mid-sized precious metals miner Hochschild Mining gets the bulk of its production from its south Peruvian mines. But its San Jose mine in Argentina - where President Cristina Fernandez has seized control of energy company YPF from Repsol - accounts for almost a third of revenues and an even bigger slice of profit.

"We see YPF as an independent case," Hochschild Chief Executive Ignacio Bustamante told Reuters in an interview.

"The challenges that we face in Argentina are different from the challenges that we have operating elsewhere, and the biggest one is definitely inflation, mostly in labour costs."

Argentina, where the London-listed gold and silver miner expects costs to rise 25 to 30 percent this year, already has the highest operating cost of Hochschild's entire portfolio. Argentina's unit cost, excluding royalties, of just under $170 per tonne last year compares to a Peru average of $60.8 a tonne.

Miners eyeing Argentina's resources have complained it is dampening their enthusiasm not only with inflation - fuelled in part by strong state spending - but also with moves to stem outflows of cash and push companies to find equipment locally.

"What they are doing is raising the bar on what makes a profitable project - what makes a profitable project in Peru does not necessarily make a profitable project in Argentina," Bustamante said.

Argentina's geological potential is "outstanding", he said, though mining remains a smaller slice of the economy than in Peru, Mexico or Chile.

"Out of the countries we operate in, it is by far the one that has been explored the least and we have expectations that there are many good world-class deposits that can be found."

Hochschild, which has three of the 14 largest silver mines in the world, has prospects and drill targets in Argentina, beyond San Jose, though all its potential transformational projects are in Peru, Chile and Mexico.

Issues of national and community pressure are not unique to Argentina, with Peru a major concern for investors last year after leftist President Ollanta Humala's government was elected, promising to boost social spending.

Bustamante said the focus for miners in Peru now was on the need for an institutional framework for companies and communities to cooperate, in line with government hopes and requirements, and on speedier permitting.

He saw no readacross to Hochschild's own projects from Newmont Mining and Buenaventura's $4.8 billion Conga gold mine in Peru, currently stalled due to opposition from local community groups.

Conga would be the most expensive mine ever built in Peru and if it is abandoned, analysts fear it could scare off $50 billion in private investment destined for mining in Peru.

GENERAL NEWS *(Continued)*

"For the benefit of the country, it is very important that that materialises," Bustamante said.

But he said Hochschild's own most advanced projects, Inmaculada and Crespo, in its southern Peruvian "cluster", were on track, with the next stage of permitting due in the third and fourth quarter respectively, ahead of commissioning in 2013.

Inmaculada and Crespo, with a combined initial capital cost of just over $425 million, could boost Hochschild's current annual production - it is targetting 20 million attributable silver equivalent ounces in 2012 - by 50 percent.

"Conga should be seen as a particular case," Bustamante said. "We have already submitted environment impact studies, we have already had the public audiences with the participation of the community, the government and the company."

TRADING PLACES

U.S. copper user, trader attack JP Morgan ETF plan

By Josephine Mason

NEW YORK, May 23 (Reuters) - A major U.S. copper consumer and a trader have lodged the first public opposition to JPMorgan Chase & Co's plan to launch a exchange-traded fund (EFT) physically backed by copper, comparing its impact to the Sumitomo scandal in the 1990s.

Lawyers representing Southwire, one of the largest copper users in the United States, and Red Kite, a major metals hedge fund and physical trader, argued in a letter to the U.S. Securities and Exchange Commission (SEC) this month that such a fund would inflate prices and squeeze supply by removing as much as a third of the London Metal Exchange's copper stocks.

Inflating prices for an industrial commodity already in short supply would "wreak havoc on the U.S. and global economy", according to a letter from attorneys at Vandenberg & Feliu LLP, dated May 9.

While it is the first formal criticism of the JPM XF Physical Copper Trust, the letter reflects widespread industry concerns that have complicated the fund's regulatory review. It came just weeks after JP Morgan filed plans to list the fund on the NYSE Euronext exchange as early as June, almost two years after it first announced plans to create a copper fund.

The letter equated the fund to the Sumitomo trading scandal in 1995, saying that the exchange would be "facilitating the fixing of prices" by allowing investors to underwrite the costs of holding physical copper off-market and in storage to drive up prices. The letter was first reported by the Financial Times.

The Sumitomo affair, which was at the time the largest trader fraud ever, involved the firm's copper trader Yasuo Hamanaka who built up a dominant position in the copper market and cost the Japanese trading house and the market billions of dollars.

There is no suggestion that the ETF would be fraudulent.

Senior executives from the two firms met with the SEC last week to voice their opposition to the plan, according to a separate filing.

A JP Morgan spokesperson did not immediately respond to a request for comment on the letter and the planned fund launch.

STOCKPILES FEARED

Net short sellers on the London Metal Exchange (LME) who need the physical commodity to close out their positions would be forced to pay higher prices, while manufacturers and fabricators who rely on LME inventory for supply would also pay more and pass on the extra costs to consumers, the letter said.

JPM's first filing said the fund would store LME brand-approved copper valued at $499,761,150 - equivalent to roughly 62,000 tonnes based on a copper price of $8,000 a tonne.

That equates to more than 30 percent of LME stocks from global annual output of 18 million tonnes.

Removing that material from the market would squeeze supply hardest in the United States, where physical premiums - the payments made on top of the benchmark copper price for delivery of the metal in cathode form - are cheapest, the letter said.

As a result, the bank would likely acquire most, if not all of its supply from the U.S., which is a net importer of copper and therefore in greater need of material than other regions.

Market participants have said there are flaws in the plan, questioning whether investors would be willing to pay fees to buy into the fund. With the price of copper for immediate delivery higher than prices for future delivery, many have questioned whether investors would be willing to watch their investment lose value.

JPM is not the only company planning a copper ETF. ETF Securities launched a copper fund in October 2010, but it had only amassed investments representing just over 6,000 tonnes as of March, worth about $50 million at today's prices. BlackRock lodged its prospectus around the same time, with plans to use 120,000 tonnes of LME-grade copper as collateral.

Similar products in the precious metals market have not raised the same concerns because they are larger markets with a greater flow of metal.

Trafigura shifts trading centre to Singapore

GENEVA/SINGAPORE, May 23 (Reuters) - Swiss-based commodities trading firm Trafigura said on Wednesday that Singapore would become its main trading centre as it seeks to tap booming demand for resources in the region.

TRADING PLACES *(Continued)*

Asian economic growth led by China is causing a shift in the global demand centre from West to East, prompting a hiring spree among the city state's commodity houses.

"Trafigura Pte Ltd, the Group's long established Singaporean entity, will ... become the main booking entity for the group's trading activities," the firm told Reuters in a statement.

As part of the expansion, Trafigura's chief financial officer Pierre Lorinet will move from Geneva to Singapore later this year and take on the additional role as Asia Pacific Managing Director, the firm added.

The move will not affect staff in other offices globally, Trafigura said. Previously, Trafigura's main centre for trade flows was in Amsterdam, where the company is legally registered.

Trafigura, which says it is the world's third biggest trader of raw materials, told Reuters earlier this month it was seeking further acquisitions in the region after buying a stake in Nagarjuna Oil Corp Ltd's planned Indian refinery.

Geneva, with its low corporate taxes and proximity to major banks, vies with London, Dubai and Singapore to be the world's top commodities trading hub and is the base for major traders like Vitol, Gunvor and Mercuria.

Typically trading companies in Geneva are categorised as "auxiliary companies" and pay around 12 percent corporate tax.

Taxes can be even more favourable in Singapore, which allows commodity firms with qualifying income under 'The Global Trader Programme' to benefit from a concessionary tax rate of 10 percent, according to a government website.

Proximity to China is also a major lure.

"People want to be close to their clients, and they want Mandarin-speaking traders," said a Swiss-based oil broker.

Rival Swiss-based trading house Gunvor said it planned to expand its activities further in Singapore.

"There are no current plans to move the headquarters to Singapore, but Gunvor is increasing its emphasis on Asia constantly, and it is its fastest growing operation," said Gunvor spokesman Stuart Leasor.

MARKET NEWS

China's top aluminium province idles plants as demand slows

By Polly Yam

HONG KONG, May 24 (Reuters) - China's top aluminium-producing province has idled about 700,000 tonnes of capacity in recent months, a senior industry official said, further evidence that slower growth in the world's No. 2 economy is denting the country's appetite for commodities.

The total reduction could rise to 1.2 million tonnes by the end of the year, Henan Nonferrous Metals Industry Association deputy chairman Liu Libin said, more than a quarter of the province's total capacity.

Slowing growth, along with a recent slump in prices, has sparked a string of deferrals and defaults on coal and iron ore deliveries to China and seen stocks of the minerals pile up in the country's ports.

Aluminium prices have joined a general slump for commodities, with London Metal Exchange metal down 15 percent from the year high hit in early March.

"Smelters that are still producing in Henan are big ones," Liu told Reuters.

"They are still able to maintain normal cash flows and are hoping the market will improve soon," he said, adding that local governments will support smelters as they want to maintain tax contributions and employment.

China is the world's largest producer of aluminium - used in the building, transport and packaging sectors - with a production capacity of more than 23 million tonnes a year.

Most of its smelting capacity sits at the high end of the global production cost curve, but many smelters have so far resisted closure, even though global producers Rio Tinto , Norsk Hydro and UC RUSAL have shaved output since the start of the year.

Norsk Hydro became the latest to announce a closure, saying on Wednesday it would shut its 180,000 tonnes a year Australian smelter.

Henan's move to shut plants illustrates how a combination of challenges, including sputtering demand at home and abroad, a production surplus and sliding prices are forcing smelters to bow to cost pressures.

State-backed research firm Antaike has estimated that less than one million tonnes of aluminium capacity in the country is currently shut, with capacity set to exceed real consumption by more than 2 million tonnes by the end of the year.

The supply glut has seen Shanghai exchange stocks of the metal reach a near one-year high of 369,247 tonnes in April, before falling to 335,301 tonnes last week.

Graphic on global output: http://link.reuters.com/vav27s

China suite: http://link.reuters.com/fut96s

OTHER PROVINCES MAY JOIN

Henan, located in eastern central China, has 4.6 million tonnes of annual aluminium production capacity. Smelters there are among the most costly to run in China due to high electricity tariffs in the land-locked province.

MARKET NEWS *(Continued)*

Liu said some 700,000 to 800,000 tonnes of capacity in Henan was most vulnerable to production cuts as these smelters do not have their own power plants.

The price of front-month aluminium on the Shanghai Futures Exchange , which typically reflects spot prices in China, has fallen from a peak of over 24,000 yuan ($3,800) a tonne in 2008 to 15,950 yuan on Wednesday.

Smelters in other provinces may also join the production cull if domestic prices fall to 15,000 yuan a tonne for a prolonged period, Liu said.

For now, production cuts in Henan are being compensated by new smelters coming onstream, including some 600,000 tonnes of new capacity in the remote northwestern Xinjiang region.

However, sustained low prices could help balance China's supply, as more smelters idle capacity or delay the start of new production lines.

"The production cuts should peak at the end of the year. Imports may rise after that," said a source at large Henan smelter, which was also thinking of idling some capacity.

Chile Codelco Q1 output falls, 2012 on track

By Alexandra Ulmer and Fabian Cambero

SANTIAGO, May 23 (Reuters) - The world's top copper producer, Chile's Codelco, said on Wednesday its output fell 10 percent in the first quarter from a year earlier to 373,000 tonnes, but said it was on target to produce 1.708 million tonnes this year.

Codelco produced 414,000 tonnes of copper in the first quarter of 2011, but output was hit during the first three months of this year by dwindling ore grades -- which the state mining giant sees improving in the second half of the year.

The century-old, massive Chuquicamata mine's production fell sharply to 60,000 tonnes from 100,000 tonnes during the same quarter last year, though output at the promising Andina mine improved to 62,000 tonnes.

"We are confident we will reach our (annual output) target of 1.708 million tonnes," CEO Diego Hernandez told a news conference, as lower ore grades had already been factored into annual production forecasts.

Hernandez said he sees market supply and demand fundamentals remaining tight and does not see copper prices dropping much, despite volatility in global markets amid Europe's swirling crisis.

Copper fell on Wednesday in London to a 4-1/2-month low, hit hard by a frenzy of risk-averse selling tied to global growth concerns, but miners point to brisk long-term growth forecasts for Asian giants China and India and curtailed metal supply as supporting prices in the long-term.

Hernandez said Codelco would push ahead with investment projects as planned, and that copper price fluctuations and rising operational costs would not trigger delays in the miner's ambitious $22 billion portfolio of projects planned by 2020.

Codelco's cash costs in the first quarter of the year were $1.30 per pound of copper, rising from 2011's average $1.16 per pound due to higher energy costs, exchange rate fluctuations and inflation.

Miners in world No.1 copper producer Chile have been hit by soaring energy prices, labor unrest triggered by high metal prices and unusual, extreme weather in the mineral-rich Atacama, the world's driest desert.

Codelco said earlier on Wednesday its profits before tax and extraordinary items fell 38 percent during the January-March period from a year earlier to $1.445 billion, due to lower prices for copper, Chile's top export.

The miner, which produces roughly 11 percent of the world's copper, also produced 4,000 tonnes of molybdenum in the first quarter of the year, down from 6,000 tonnes in the same period of 2011.

Codelco produced a record 1.735 million tonnes of copper last year, but the firm forecasts its 2012 output will dip before rising to 2.1 million tonnes by 2020 as its ambitious expansion plans come on line.

ANGLO NEGOTIATIONS

A month-long break from bitter legal proceedings is a final opportunity for Codelco and global miner Anglo American to head off a lengthy court battle over a multibillion dollar contract dispute, Hernandez said.

The two miners agreed on Tuesday to go back to the negotiating table in a push to end a damaging and increasingly acrimonious dispute over Anglo American's operations in the country's central-south region.

Hernandez did not provide further details on the reactivation of the confidential talks over Codelco's option to buy up to 49 percent of Anglo's flagship south-central Chile properties.

China iron ore market "steady as it goes" - Rio

By James Regan

SYDNEY, May 24 (Reuters) - Rio Tinto , the world's No.2 producer of iron ore, sees no signs of a slowdown in demand from top consumer China and still plans to almost double its output of the steel-making ingredient by 2016.

Slowing growth in China has rattled commodity markets in recent weeks, prompting sharp falls in some raw materials prices on fears demand will slump.

MARKET NEWS *(Continued)*

Some Chinese buyers have defaulted on coal and iron ore contracts and others are deferring deliveries following a drop in prices, traders said this week. But Sam Walsh, the head of Rio Tinto's iron ore division, said the company was seeing little evidence of such turmoil.

"We're not physically seeing it on the ground," he said, describing the China market as "steady as it goes" in the short-term.

China's factories faltered in May as export orders fell to two month lows, a private sector survey showed on Thursday, suggesting surprise weakness in April's hard economic data persists even as policymakers seek to shore up growth.

GRAPHIC: China suite: http://link.reuters.com/fut96s

Shares in Rio traded down 0.5 percent, having tumbled to a near three-year low last week amid concerns about the growth outlook and spending plans.

Rio, along with other big diversified miners including BHP Billiton , Vale and AngloAmerican , are beefing up iron ore divisions in anticipation of long-term demand despite the short-term set-backs in China.

Rio is already committed to lifting yearly output capacity at its main Pilbara mines by 23 percent to 283 million tonnes. It has a proposal before its board to increase that to 353 million tonnes by the first half of 2015.

"At current estimates, we have options to expand to a global annual capacity approaching 450 million tonnes by 2016, when Canada and our new project in Guinea are added in," Walsh told a business luncheon in Sydney.

PILBARA EXPANSION

Walsh reiterated that a decision on the Pilbara expansion was on course to be made within months.

BHP also has plans to expand its Australian iron ore mines. The company's chairman, Jac Nasser, said last week BHP would not meet its five-year, $80 billion capital expenditure plan, but did not mention which areas may be pushed back.

Analysts say big iron ore expansion and infrastructure projects in the Pilbara, where margins are among the industry's fattest, are less likely to be affected.

However, smaller iron ore players are struggling to raise funds for development projects, with access to credit more difficult and investors more wary.

Also on Thursday, China's Hanlong Mining put back its $1.3 billion takeover of Australian-listed Sundance Resources by six months amid delays over funding and consents.

Sundance is developing a $4.7 billion project on the border of Congo and Cameroon in western Africa.

China nerves delay $1.3 bln Australian iron ore bid

By Sonali Paul and Narayanan Somasundaram

MELBOURNE/SYDNEY, May 24 (Reuters) - China's Hanlong Mining has put back by six months a target date to seal a A$1.34 billion ($1.3 billion) takeover of Australian iron ore group Sundance Resources , as Chinese investment in Australian resource projects cools this year.

The firms said they had agreed to delay the takeover until November after Hanlong struggled to line up funding from China.

The long delay on the deal, first announced last July, points to China's reluctance to make big bets on risky resources projects offshore amid uncertainty over economic growth at home.

Global markets have been rattled by signs of slowing growth in the world's No.2 economy, which is casting a shadow over demand for commodities and led Premier Wen Jiabao to push forward key investment projects in a bid to revive growth.

Hanlong is targeting Sundance for its $4.7 billion Mbalam iron ore project on the border of Congo and Cameroon in western Africa, seen as a major new source of iron ore that could diversify China's dependence on Australia and Brazil.

The project, which includes building a 510 km (320 mile) rail line and a deep water port, has yet to secure key approvals from the two governments and backing from the Chinese Development Bank, all expected months ago.

Chinese interest in snapping up Australian assets has dropped sharply since last year, when Chinese takeovers of Australian metals and mining assets peaked at 40 deals worth $6.5 billion, according to Thomson Reuters data.

Nearly half way into 2012, Chinese bids have shrunk to $522 million, less than a tenth of last year's figure.

"The past urgency is missing," said a banker who had advised Chinese firms on several large deals in the last two years.

"Barely a year ago they would have stepped in, looked at the asset and if they saw potential, the Chinese would make the first bid which almost always looked compelling."

GRAPHIC: China suite: http://link.reuters.com/fut96s

Sundance Chairman George Jones said the two main factors holding up Chinese funding were slow decisions from Cameroon and Congo setting licence conditions for Sundance and delayed approval from Australia's Foreign Investment Review Board.

Jones said the mining licence terms should be agreed next week, or early June at the latest, and expects Hanlong to win Foreign Investment Review Board approval by the end of June.

Speaking by phone from Perth, he said the firm's close work with Hanlong has "given us a lot of confidence that they do have the ability to deliver on this transaction."

MARKET NEWS *(Continued)*

MID-NOVEMBER TARGET

Hanlong, which owns 18.6 percent of Sundance, had hoped to line up backing for the takeover from the China Development Bank last November, but has now pushed the deadline for that funding out to August 31.

Jones said Sundance now hopes to complete a deal by mid-November, having now established "a clearer understanding of the needs of China's National Development and Reform Commission and Hanlong's financiers, the China Development Bank."

Sundance's shares jumped 7.5 percent to A$0.43 as investors gained comfort the deal may still go ahead. But the shares were still 14 percent below Hanlong's offer price of A$0.50 a share.

Mbalam is expected to produce 35 million tonnes a year of iron ore. This compares with a forecast 55 million tonnes this year from Australia's Fortescue Metals Group , the world's number four iron producer.

The difficulties in getting big projects up and running in a rising cost environment have made Chinese firms and their lenders hesitant to make big new investments, China's ambassador to Australia, Chen Yuming, told Reuters in an interview this month.

Jones said the Chinese were just being prudent and he did not see the broader global uncertainty weighing on the deal or undermining China Development Bank's lending for deals in general.

Hanlong's bid for Sundance last year followed a string of Chinese bids for emerging Australian iron ore producers, as China's steel mills try to trim their dependence on the big three iron ore producers, Brazil's Vale and Anglo Australian giants BHP Billiton and Rio Tinto .

Rio Tinto and BHP, both in the midst of rapid expansions at their Australian iron ore operations, have recently flagged they remain bullish on the outlook for iron ore, despite slowing demand growth from China's steel mills.

However, BHP said the window for producers to tap into that demand growth had narrowed to 2025.

Severstal Q1 profit $427 mln, beats estimates

MOSCOW, May 24 (Reuters) - Russia's second largest steel producer, Severstal , said on Thursday that its first quarter net profit reached $427 million, beating forecasts thanks to the stronger rouble.

Analysts polled by Reuters had expected the company to post a first quarter net profit of $318 million, down from $531 million in the year-earlier period.

The company, controlled by billionaire Alexei Mordashov, also said results at its core Russian steel unit will improve in the second quarter, although the export market remains volatile.

"The outlook for the global steel industry remains challenging, however we see improving fundamentals for Russian steel in Q2 due to more stable steel prices and firm domestic demand," the company said in a statement.

The company said its first quarter earnings before interest, taxes, depreciation and amortisation (EBITDA) reached $562 million, below the $630 million forecast and also less than the $934 million year-earlier result.

It also said revenues were $3.68 billion , matching the $3.68 billion poll forecast and slightly below t he $3.73 billion 2011 first quarter result.

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 rises from 4-1/2 month low, EU crisis weighs

By Naveen Thukral

SINGAPORE, May 24 (Reuters) - London copper rose 0.8 percent on Thursday as the market took a breather after sinking to a 4-1/2 month low in the previous session on risk aversion triggered by worries over Greece's possible exit from the euro zone.

Copper, which has lost almost 10 percent this month, may find support from positive U.S. housing data, although gains were capped as the market remains vulnerable to the implications for the global economy after European leaders were unable to deliver meaningful measures to resolve the region's debt crisis.

"Prices of copper have come off quite heavily in recent weeks so there might be some sense that maybe it was an overreaction," said Alexandra Knight, an economist with National Australia Bank. "From my perspective Greece will ultimately stay in the euro zone as there will be a lot of resistance to letting it exit."

Three-month copper on the London Metal Exchange was up 0.8 percent to $7,594.25 per tonne by 0323 GMT, after falling to $7,503 per tonne on Wednesday - the lowest since early January.

LME copper dropped about 3 percent on Wednesday, triggering a broad-based decline across the base metals complex with lead and zinc each losing nearly 2 percent.

The most-active September copper contract on the Shanghai Futures Exchange slipped 0.5 percent to 54,740 yuan per tonne, tracking Wednesday's LME decline.

EUROPEAN CRISIS VERSUS U.S. DATA

European Union leaders, advised by senior officials to prepare contingency plans in case Greece decides to quit the single currency, urged the country to stay the course on austerity and complete the reforms demanded under its bailout programme.

After nearly six hours of talks held during an informal dinner, leaders said they were committed to Greece remaining in the euro zone, but it had to stick to its side of the bargain too, a commitment that will mean a heavy cost for Greeks.

Still, there was positive news from U.S. housing data, which could support industrial metals, particularly copper.

"U.S. housing data was a little bit better than expected," said Knight. "It has gone under the radar because of the focus on Europe, but it will help - particularly copper, which is used in construction."

The U.S. spring home-selling season got off to a strong start in April, with rising sales and prices providing evidence that a housing market recovery was gaining some traction.

The housing sector has been the Achilles' heel of the U.S. economy ever since the home-price bubble burst. Data this week, however, has painted a relatively upbeat picture for the market and underscored the economy's resilience.

The world's top copper producer, Chile's Codelco, said its output fell 10 percent in the first quarter from a year earlier to 373,000 tonnes, but added that it was on target to produce 1.708 million tonnes this year.

The latest data showed copper stocks in LME-registered warehouses rose by 1,725 tonnes to 225,700 tonnes, with net inflows mostly into warehouses in South Korea, where traders suspect Chinese merchants have booked around 110,000 tonnes for delivery.

Metals warehouses in China are said to be so full that workers are starting to stockpile iron ore in granaries and copper in car parks.

PRECIOUS-Gold hovers near $1,560/oz; Greece woes feed caution

By Rujun Shen

SINGAPORE, May 24 (Reuters) - Gold hovered near $1,560 an ounce on Thursday, remaining on shaky ground as worries about Greece and the euro zone continued to dominate market sentiment after a European Union summit yielded few practical steps to manage the debt crisis.

Gold, typically a safe-haven option, has been moving in tandem with riskier assets as the euro zone debt problem grinds on. Senior officials have advised European leaders to prepare contingency plans in case Greece quits the single currency, although the EU urged Athens to stay the course on austerity.

Light buying in the physical market emerged when prices dropped near a key support level near $1,530 in the previous session, but that has eased with selling trickling in as prices rebounded.

"Clients are not too interested in entering the market right now," said a Singapore-based dealer. "They are worried that if Greece eventually pulls out of the euro zone, the euro will fall and drag gold down with it."

Spot gold was nearly flat at $1,559.60 an ounce by 0327 GMT, after dropping to $1,533.41 in the previous session.

U.S. gold gained 0.7 percent to $1,559.50.

Gold's room on the downside might be limited, as investors with faith in bullion for longer term will likely return if prices weaken, some analysts argued.

"We'll see buy-on-dip type of purchases from investors and even central bank buying if prices fall below $1,530 an ounce," said Li Ning, an analyst at Shanghai CIFCO Futures.

"But on the upside gold is still facing a lot of pressure from a stronger dollar."

MARKET REVIEW *(Continued)*

The dollar index stayed near its highest level since September 2010, as the euro wallowed near a two-year low against the greenback. China's factories took a hit in May as export orders fell sharply, said the HSBC Flash Purchasing Managers Index, adding to concerns of global growth, which is already under threat from the deepening euro zone crisis.

Worries about Greece outweighed concerns about potential supply shortage in platinum caused by a shutdown of the world's biggest platinum mine Rustenburg. Spot platinum edged down 0.2 percent to $1,415.75, up from a four-month low of $1,400.9 hit on Wednesday.

Spot palladium dropped to $583.18 in the previous session, its lowest in nearly six months, before recovering some lost ground to $590.70 on Thursday.

FOREX-Euro shaky on Greece exit fear, near 22-month low

By Masayuki Kitano and Ian Chua

SINGAPORE/SYDNEY, May 24 (Reuters) - The euro hovered just above its 22-month low against the dollar on Thursday and remained vulnerable to further declines as the prospect of a Greek exit from the euro zone kept investors on tenterhooks.

The euro eased 0.1 percent to $1.2574 . It fell to about $1.2545 the previous day, its lowest level since July 2010. That level should provide initial support, followed by $1.2500.

The euro drew little comfort from an informal summit of European Union leaders that shed no new light on how the euro zone nations intend to tackle its debt crisis, including the threat of Greece's exit from euro.

"It's still hard to see what the endgame will be like," a trader at a Japanese bank in Tokyo said.

European Union leaders urged Greece to stay the course on austerity and complete the reforms demanded under its bailout programme. Three officials told Reuters that members of the currency bloc have been warned to prepare contingency plans in case Greece quits the euro, an eventuality that the German central bank said would be testing, but "manageable".

"With a Greek exit once again being discussed, the pressure on the euro should continue especially with the lack of clarity on any of the pressing issues," analysts at BNP Paribas wrote in a client note.

"EUR weakness is likely to be amplified against the USD and the JPY as the market seeks refuge (in the safe-haven pair) as negative risk sentiment persists."

The next major support level for the euro is seen at $1.2500, although some market players say the single currency is at risk of an even steeper drop.

Daisuke Karakama, market economist at Mizuho Corporate Bank in Tokyo, said the euro may drop to $1.20 by the end of June. The $1.20 level is key for the euro because the $1.20 to $1.22 range is seen as being roughly consistent with purchasing power parity, Karakama said.

In the past, there have been cases where the euro's drop versus the dollar have stalled near levels consistent with purchasing power parity, he added.

"One point to watch will be whether the euro can break below such levels," Karakama said.

With the euro under pressure, the safe-haven dollar held its ground. Against a basket of major currencies, the dollar stood at 82.086 . That was close to a peak of 82.221 hit on Wednesday, the dollar's highest level since September 2010.

The dollar held steady against the yen at 79.50 yen .

Data showing that China's factories faltered in May had limited impact on major currencies, as market players had been expecting a weak reading.

The Australian dollar inched up 0.1 percent to $0.9759 , staying above a six-month low of $0.9690 hit on Wednesday.

In the wake of its recent sharp falls, the Aussie dollar faces a further test over Thursday and Friday, when around A$600 million of uridashi bonds are due to be redeemed. Uridashi bonds are foreign currency debt sold in Japan primarily to households. The risk is that Japanese holders of such bonds may convert some proceeds from the bond redemptions back into the yen, although they might also roll their funds into other Australian dollar assets.

(Inside Metals is compiled by Shashwat Sharma in Bangalore)

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