

BASE METALS Q2 2011

(APRIL - JUNE)

RECOMMENDATIONS (Click on the name of the commodity to view complete details)

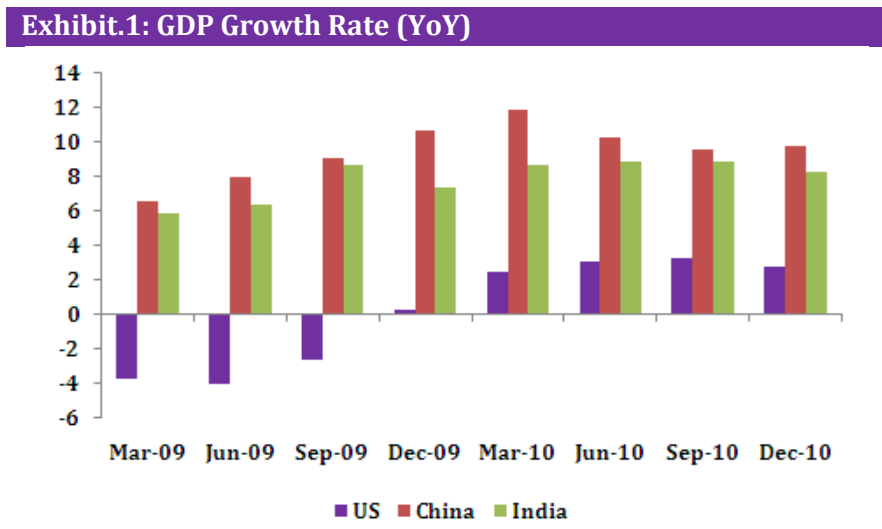
COMMODITY	RECOMMENDATIONS
ALUMINIUM	LME 3M Fwd: Buy at 2500-560 TP 2885 SL 2360 MCX: Buy at 110-113 TP 125 SL 107
COPPER	LME 3M Fwd: Buy at 9100-9200 TP 10200 SL 8900 MCX: Buy at 400-410 TP 465 SL 380
LEAD	LME 3M Fwd: Buy at 2550-2600 TP 3000 SL 2350 MCX: Buy at 115-119 TP 129 then 140 SL 108
NICKEL	LME 3M Fwd: Buy at 23800-24200 TP 29000 then 31000 SL 21000 MCX: Buy at 1130-1140 TP 1240 then 1300 SL 1050
ZINC	LME 3M Fwd: Buy at 2200-2225 TP 2600 then 2730 SL 2050 MCX: Buy at 97-100 TP 115 then 124 SL 93
INVESTMENT STRATEGIES	
ALUMINIUM MINI	MCX: Buy X lot at 114-116, Y lots at 108-110 TP 130,135 SL below 95
LEAD MINI	MCX: Buy X lot at 122-124, Y lots at 115-116 TP 140, 150 SL below 100
ZINC MINI	MCX: Buy X lot at 104-106, Y lots at 101-103 TP 120,125 SL below 90

***Note:** Calls mentioned above carry a long term view and we would insist to hold onto the actual technical levels for initiation. The levels of initiation might be applicable for couple of active contracts. Majorly these are tentative figures which give an indication of broad trend.*

ECONOMIC OUTLOOK: The Year 2011 started on a strong note for the global economy as major nations witnessed revival in growth. However growth ahead might face downward pressures in certain countries like Japan and in peripheral European nations. Japanese economy might witness decline in output, in the near term, given the recent catastrophe and peripheral Europe would remain under pressure from higher borrowing costs and weak economic prospects.

Global economy as a whole seems to be rebounding. IMF has revised its global growth estimate upwards to 4.4 percent in 2011. Advanced countries would grow at a rate of 2.5 percent lead by 3 percent growth in World’s largest economy, US. Growth projections of China have been left unchanged at 9.6 percent.

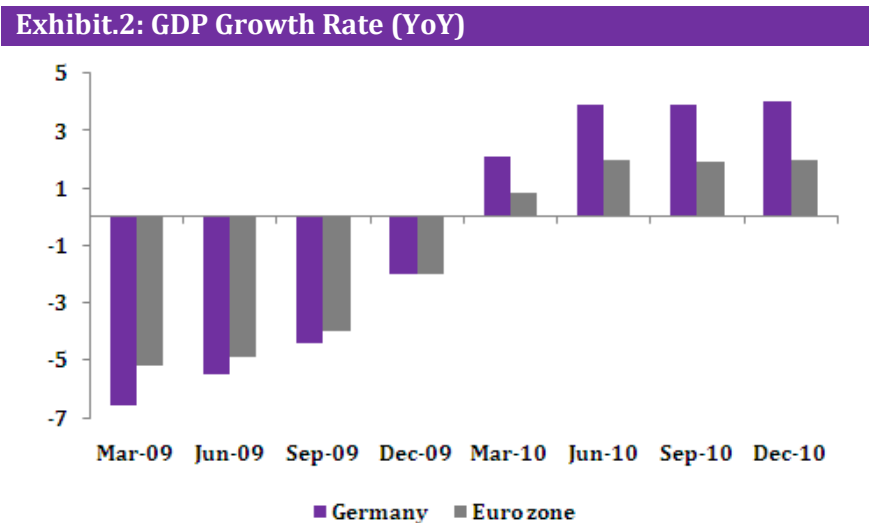
Divergence continues to remain between emerging economies and developed nations though in the opposite direction this time. Developed nations like US and Germany are expected to continue growing strongly as the fiscal and monetary measures to support economy takes hold. Emerging economies however are indicating a sign of moderation in growth this year as the central banks raises interest rates to combat inflation. On a relative basis however they continue to remain strong and same is with the prospects of demand.



Source: Bloomberg, KCTL Research

US economy grew by 3.1 percent in the fourth quarter of 2010 supported by personal consumption growth of 4.1 percent. Given the fiscal measures like extension of tax cuts, hiring seem to have picked in the economy thereby sending the unemployment rate down to 8.9 percent by the end of February. Federal Reserve is continuing with its bond buying program and maintained policy rate at 0.25 percent.

Peripheral European nations continue to face pressures and Moody’s downgrading credit rating of countries like Greece, Spain and Portugal indicates that tough conditions would continue to prevail. However larger countries in the region like Germany continue to do well and thereby the economy grew at an annualized rate of 4 percent in the fourth quarter of 2010 despite when the Euro zone reported a growth figure of 2 percent.

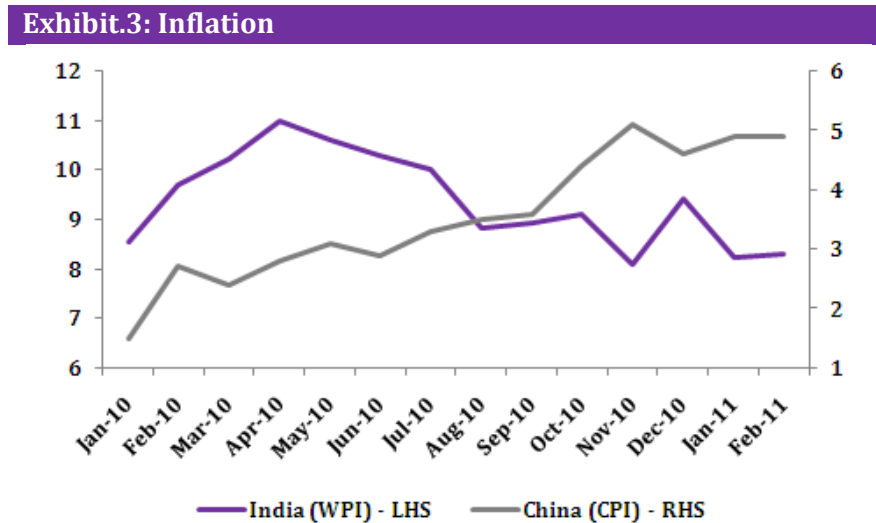


Source: Bloomberg, KCTL Research

Inflation in the euro zone has also picked up and is at 2.4 percent, which remains above the target rate of 2 percent thereby propelling the European Central Bank to signal increase in interest rates. So in April, interest rates might be hiked by 25 bps but that does not mean that the central bank has started on a tightening cycle. The conditions in the weaker European nations along with inflation trajectory, would determine the policy moves ahead and given the economic conditions, it seems unlikely that a series of rate hikes will follow.

Just when the Japanese economy was showing signs of stable recovery, it is hit by double blow of earthquake and Tsunami. This will hit the growth prospects at least for two quarters but once the reconstruction begins the economy might pick-up and demand for commodities might get a boost. However this time, it might take more time and the economy might not bounce back as strongly many expect it to. The countries debt to GDP ratio is nearing the 200 percent of GDP and thereby the government would be constrained in its spending.

Emerging economies like China and India continued to raise interest rates to combat inflation. Despite this, Chinese economy continues to remain strong and the GDP grew by 9.8 percent in the fourth quarter of 2010. However, given the various measures taken to cool the economy, growth might moderate ahead but that would be positive as it might prevent the economy from hard landing. Also a sustainable growth rate would be more desirable than above potential growth rate in short term. Reserve Bank of India also raised interest rates as inflation remained above 8 percent as against the central banks projection of 7 percent.



Source: Bloomberg, KCTL Research

Overall, developed economies might continue to witness strong growth, with emerging economies witnessing slight moderation in growth. Both this would support the demand for the industrial metals to remain strong.

BASE METALS: After starting the year on a strong note, base metal prices could not sustain all the gains and ended the first quarter with lower single digit percentage gains in case of nickel, lead and aluminium, while modest losses were witnessed in copper and zinc price. Initially prices got a boost from prospect of increasing demand along with supply constraints. Later however tensions in Middle East and North Africa (MENA) region along with prospects of decline in demand from World’s third largest economy, Japan sent prices lower.

Last year’s top performer nickel continued to lead the pack with gains of more than 8 percent on the back of balanced market while oversupplied market made zinc to underperform as prices ended lower by 5.2 percent on London Metal Exchange and nearly 4 percent on MCX.

Inventory has increased for all the metals in the first quarter of 2011 except for nickel. This also capped the price rise and raised fears that demand might be trimming at higher levels. Concerns about decline in demand from Japan might also keep the prices under pressure initially. However downside for prices from here might be limited as Chinese buyers might have only deferred buying and any major decline in prices would find buying support. Second quarter is also considered to be peak season for demand, especially in China, as restocking starts before construction activity picks up in the third quarter. Supply constraints continue to remain as catastrophes along with bad weather conditions hinder production.

Also given that growth across the major economies is expected to remain strong, base metal prices might find support.

RISK FACTORS: *Higher oil prices*; Global economy is just recovering from the financial crisis and thereby might not be ready to take the burden of higher oil prices. It might leave less amount of money with consumers to be spent on other items. Given the unrest in the Middle East region, any substantial increase in oil prices could even lead to risk aversion thereby sending base metal prices lower.

Japan, World's third largest economy, is the hub for many companies' production units and thereby extended period of disruption of activity there might disrupt the supply chain. Consumer durables like automobiles and electronics would be worst impacted and thereby could lead to decline in output.

EQUITY MARKETS

Equity markets also benefited from rebound in economic activity as it boosted corporate profitability and thereby stock prices. However they trimmed most of the gains and ended lower as rising crude oil prices along with natural calamities in Japan hit sentiment.

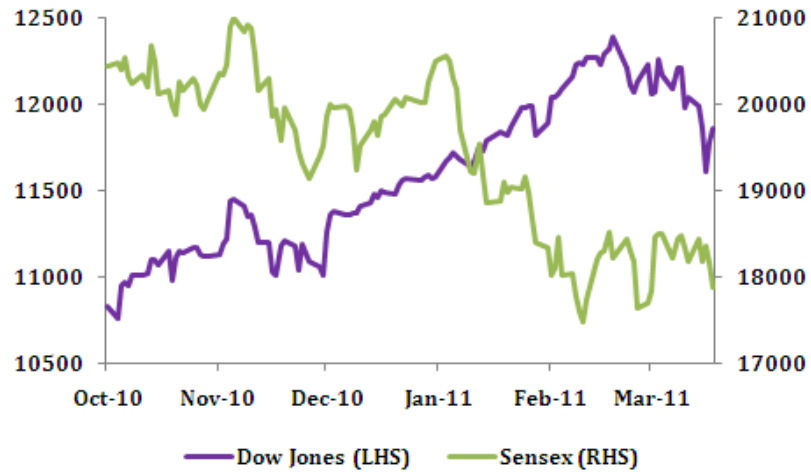
REGION	EQUITY INDEX	Q1 2011	Q4 2010
	MSCI - World Index	0.8%	8.3%
US & Latin America	US - Dow Jones	2.5%	7.3%
	US - S&P 500	1.7%	10.2%
	Brazil - BOSVEPA	-3.5%	-0.2%
EURO ZONE	London - FTSE-100	-4.2%	7.6%
	Germany - DAX	-3.6%	11.0%
	France - CAC	-1.1%	3.7%
ASIA	Hong Kong - Hang Seng	-3.0%	2.9%
	Australia - ASX 200	-3.4%	4.5%
	India - Sensex	-12.3%	1.6%
	India - Nifty	-11.9%	1.2%
	Japan - NIKKEI	-10.0%	9.2%

Divergence in the equity market performance was also witnessed. Among the major markets, US equity indices were the only one to end the quarter in green. Rest all ended lower with losses ranging from one to twelve percent.

Last year's top performer- Indian markets underperformed most of the other global majors and ended with double digit percentage losses. Japanese market also declined substantially on the back of after shocks of natural calamity.

In fact, emerging nations as a pack underperformed the developed nations. This is largely owing to relatively cheaper valuation amid improving economic prospects propelling investors to move money from emerging economies to developed nations. ***However this might only be a short term phenomenon and in the long term, emerging economies continue to have brighter prospects than the developed world.***

Exhibit.4: Dow Jones Vs Sensex



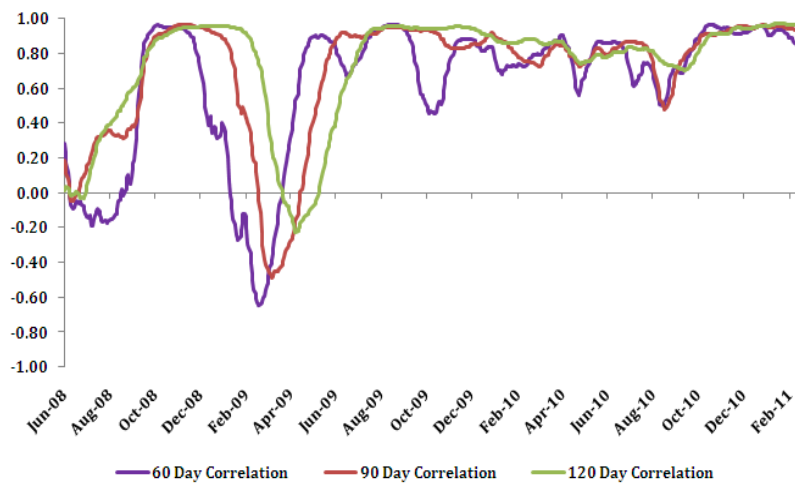
Source: Bloomberg, KCTL Research

CORRELATION BETWEEN DOW JONES AND COPPER:

Equity markets and industrial metal prices both share a very good correlation. Strong economic prospects would boost demand for the industrial metals and would also be reflected in strong equity markets. To check this out, we calculated the correlation between Dow Jones and Copper across various time frames.

Looking at the data from 2008, the correlation was actually strongly negative in March 2009. This was the time, when most of the equity markets and commodity prices bottomed out and started to rally.

Exhibit.5: Correlation between Dow Jones and Copper



Source: Bloomberg, KCTL Research

Currently, both Dow Jones and copper prices are strongly correlated. Over a 120 day period, which is more stable, the correlation is at 0.94, which means that most of the time, both Dow Jones and Copper move in the same direction. Even if one looks at shorter time frame say 90 days, even then the correlation holds strongly at 0.89 and over 60 day, the correlation is at 0.62. In total, we may conclude there holds a strong positive correlation between Dow Jones and Copper prices.

Reasons for this correlation to remain strongly positive are mainly two; **first**, low interest rates which along with quantitative easing measures have sent risky assets prices higher thereby building a strong correlation. **Second** is the **RORO trade i.e., Risk ON and Risk OFF** trade going on all over the globe that is moving risky assets like industrial metals and equities in the same direction.

CURRENCIES

Dollar remained under pressure as Federal Reserve might not raise interest rates this year, while other central banks like the European Central Bank and the Bank of England are expected to increase rates. This sent these currencies i.e., Euro and Pound higher while led to decline in dollar. Dollar index ended with quarter with losses of 4.2 percent thereby providing further boost to commodity prices.

From India markets, foreign investors pulled out money in the first quarter of 2011, amounting to nearly \$2 billion as concerns about higher inflation along with slower pace of policy reforms propelled some profit booking. This sent the Indian rupee depreciating by 0.9 percent.

CURRENCY PAIR	Q1 2011	Q4 2010
USD INR	0.9%	-4.4%
EUR USD	5.9%	-6.6%
GBP USD	3.9%	-2.9%
USD JPY	-0.6%	-12.2%
AUD USD	-2.6%	14.4%
SGD USD	-0.8%	-8.6%
Dollar Index	-4.2%	1.4%

Exhibit.6: Dollar Index



Source: Bloomberg, KCTL Research

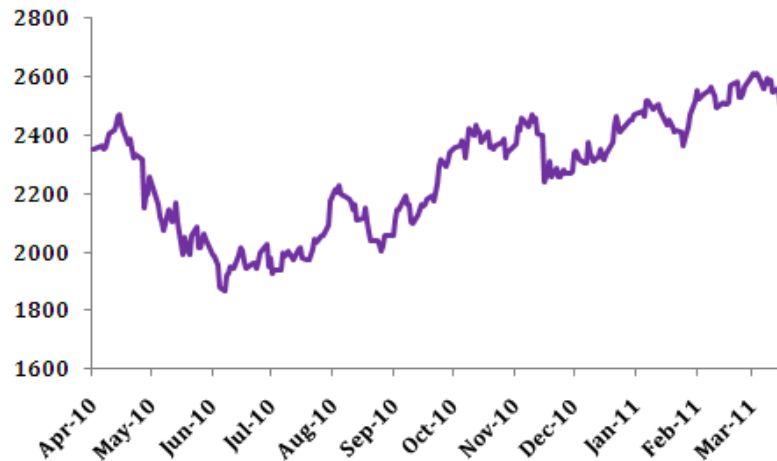
ALUMINIUM

PRICE PERFORMANCE: In the first quarter of 2011, aluminium prices moved higher by 3.6 percent on LME and by a similar percentage on MCX on the back of strong demand. During the quarter, prices made a high of \$2,628/tonne on LME and a low of \$2,360/tonne, before ending at \$2,560/tonne. In Indian markets, aluminium prices ended at ₹115/Kg.

Period	LME	MCX
Q1 2011	3.6%	3.7%
Q4 2010	5.5%	6.8%
Q3 2010	18.4%	15.0%
Q2 2010	-14.9%	-13.0%
Q1 2010	4.2%	0.4%

Aluminium, though providing lower returns, has been largely consistent given its stable fundamentals. Rebounding economy boosted demand for consumer durables thereby supporting aluminium price. However stock levels on London Metal Exchange warehouses increased indicating that supply continue to outpace demand. This limited the gains of the metal.

Exhibit.7: LME Aluminium Prices (\$/tonne)



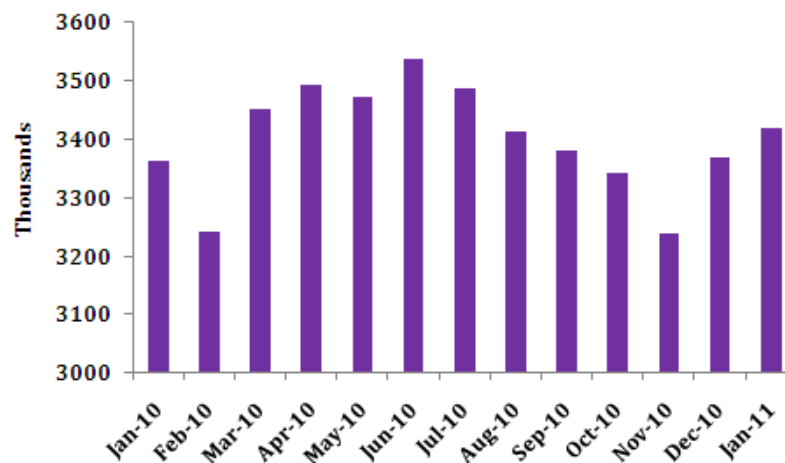
Source: Bloomberg, KCTL Research

FUNDAMENTALS:

Globally aluminium production in the month of January amounted to 3.42 million tonnes thereby registering a growth of 1.5 percent as against growth of 4 percent in the previous month. Higher production might largely be owing to increased utilization of capacity given the rebound in the economic activity thereby propelling companies to produce more.

In China, aluminium production in the first couple of months of 2011 has declined by 1.6 percent year-on-year to 2.6 million tonnes. The decline largely owes to cut in production in some provinces owing to short supply of power. However reports indicated that most of the smelters in Henan province, the top producing region in China, have restarted some of the idle capacity and thereby production might witness increase in the months ahead. This is also commensurate with the fact that the non-ferrous metal association expects the production to rise to nearly 20 million tonnes this year and the economy thereby still leaving a spare capacity of 5 million tonnes.

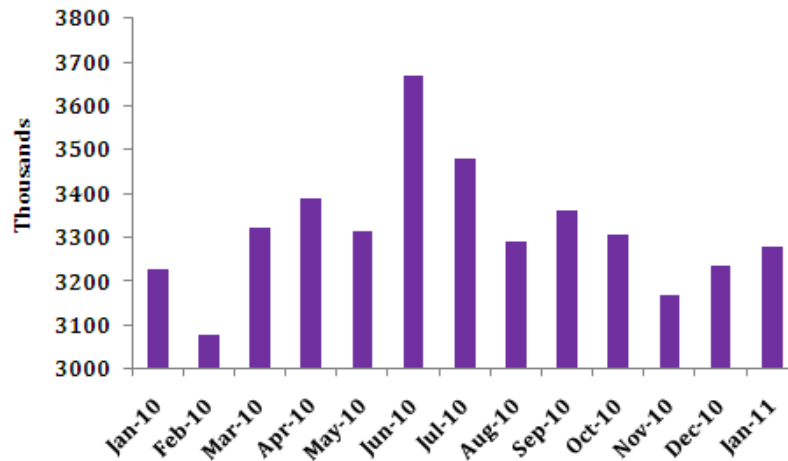
Exhibit.8: World Aluminium Production



Source: Bloomberg, KCTL Research

CONSUMPTION: According to the World Bureau of Metal Statistics, aluminium consumption increased by 1.2 percent to 3.27 million tonnes in the month of January. Increased consumption came in from higher demand from sectors like packaging. Demand of consumer durables like electronics was on the higher side in emerging economies and also picked up in developed nations thereby boosting demand for aluminium. For instance, consumption of processed aluminium products rose by nearly 18 percent in January as per the Brazil aluminium association.

Exhibit.9: World Aluminium Consumption

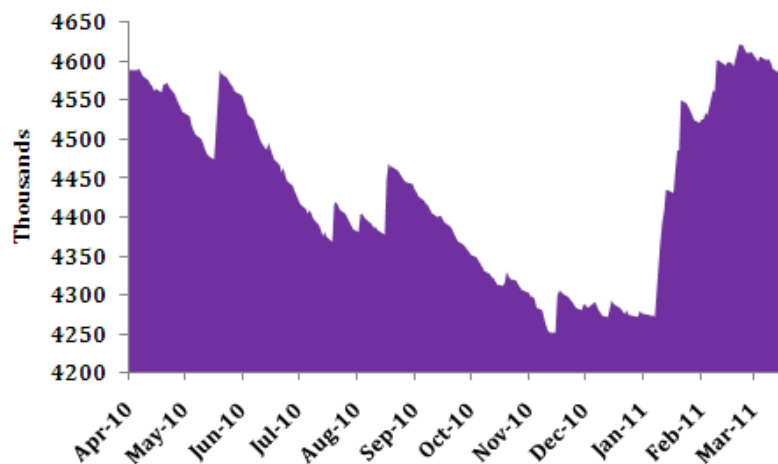


Source: Bloomberg, KCTL Research

INVENTORY: London Metal Exchange warehouses witnessed net build-up of stocks of aluminium, though financing deals might be attributed to some increase in the metal stocks. Increase in inventory limited the price appreciation of the metal.

In the first quarter of 2011, aluminium stocks on London Metal Exchange increased by 7.85 percent or 335,775 tonnes, thereby taking the total stock to 4.61 million tonnes.

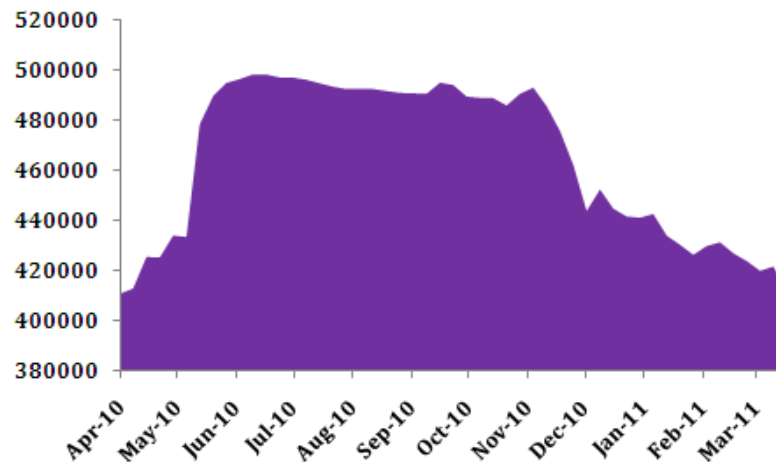
Exhibit.10: LME Inventory – Aluminium



Source: Bloomberg, KCTL Research

Stocks in Chinese warehouses however witnessed decline of 6.7 percent or 29,580 tonnes thereby taking the total stock to 411,589 tonnes. Though the decline may seem modest, it has been substantial from higher levels witnessed in first quarter of 2010. Also aluminium stocks held at Japanese ports declined by 5.7 percent from a month earlier to 208,100 tonnes, reflecting lower import volumes.

Exhibit .11: Aluminium Stocks at Chinese Warehouses



Source: Bloomberg, KCTL Research

OUTLOOK: Catastrophe in Japan might lead to decline in demand in the near term as the nation is Asia’s largest importer. However the demand continues to remain strong in countries like China. Also the term premiums for primary aluminium shipment to Japan for second quarter were mostly set at \$113/tonne which is largely unchanged from the first quarter of the current year thereby marking to an end of decline for the past four quarters. A cut in premium indicates sluggish demand and a higher premium indicates strong demand.

Premiums in Europe also continue to remain high indicating that large portion of the LME stocks are held up in financing deals. Deutsche Bank’s financing deal is reported to hold around 2 million tonnes of the metal, which constitutes nearly 43 percent of the total stocks. Given that aluminium market is in contango it makes this deal financially viable and profitable by leaving the metal in the warehouses which charges a lower storage cost.

Aluminium prices are also expected to find support from the fact that given the clouds over nuclear power, energy costs are expected to remain high and thereby cost of production of the energy intensive metal would also increase. This might even send capacity out of stream.

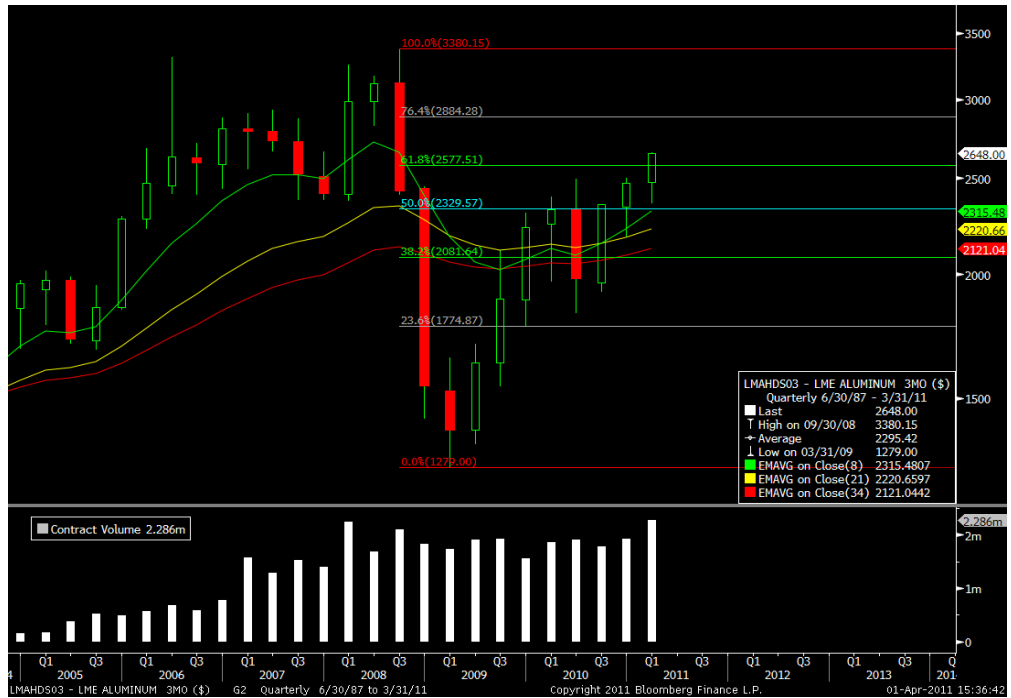
TECHNICALS:

View: Upside; **Strategy:** Buy

Outlook: The price action from the low of 2185 is considered as intermediate wave 3 in which minor wave structure with unfolding nature is in progress. However, market has breached the resistance at 2500 levels, which is top of intermediate wave (1) and currently trading above the same is suggesting further upside movements could be there. The upside potential is seen till 2816 levels (100% extension of the range 1279-2394). Trend line support is seen at 2550 levels sustain above the same it is possible to move higher. Overall, we carry a bullish view for aluminium prices and recommend buying.



Aluminium traded higher for the third consecutive quarter. It made a low of 2360 then 2656 and settled higher at 2648 levels. Closing of the candle renders bullish trend is still intact. The principle of Fibonacci retracement states that prices are witnessing support at 2330 levels which is 50% retracement of the range (1279-3380). On sustained trade above is likely to remain higher. Prices have breached the resistance at 2578 levels which is 61.8% retracement of the above mentioned range suggesting further bullish trend. The moving average principle suggesting bullish trend as prices are trading well above the short and medium term EMA's of (8, 21&34). The Volume indicator analysis also suggesting upside movements as volumes have increases from 1.925M contracts to 2.286M contracts. However a mild correction on the lower side may be expected before resuming its uptrend.



RECOMMENDATION:

LME 3M Fwd: Buy at 2500-560 TP 2885 SL 2360

MCX: Buy at 110-113 TP 125 SL 107

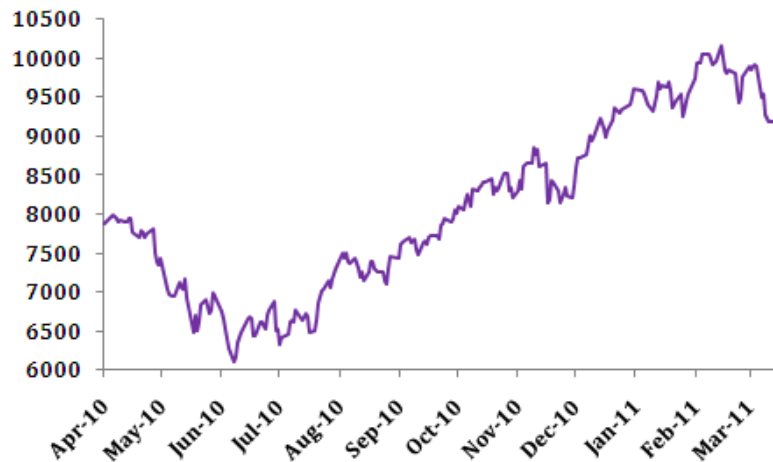
COPPER

PRICE PERFORMANCE: Copper prices ended the first quarter of 2011 with modest losses of 1 percent. On LME, prices made a high of \$10,190/tonne and a low of \$8,944/tonne before ending at \$9,510/tonne. In Indian markets, prices retraced from high of ₹466/Kg to end at ₹435/Kg.

Period	LME	MCX
Q1 2011	-0.9%	-1.2%
Q4 2010	19.1%	21.3%
Q3 2010	23.8%	20.1%
Q2 2010	-16.4%	-14.2%
Q1 2010	5.6%	2.1%

Copper started the year on a strong note on the prospect of strong demand and decline in supply but could not sustain the gains as tensions in Middle East along with prospect of near term decline in demand from Japan weighed on prices. Stocks on London Metal Exchange also increased thereby further adding to the pressure.

Exhibit.12: LME Copper Prices (\$/tonne)



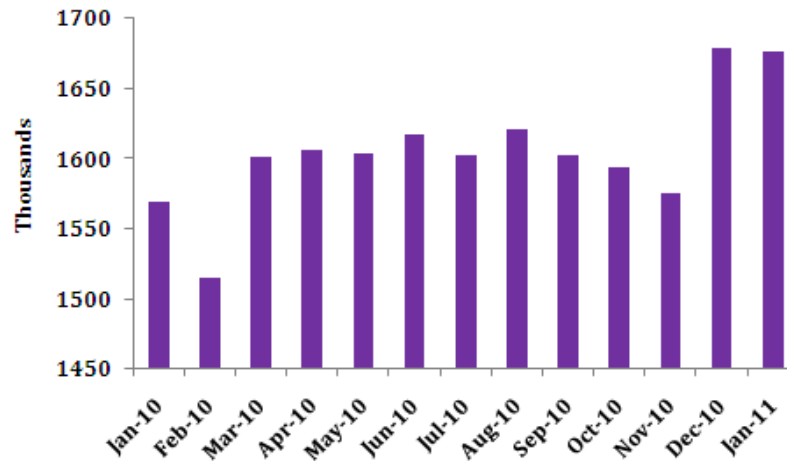
Source: Bloomberg, KCTL Research

FUNDAMENTALS:

Report by International Copper Study Group showed the total production in January to November 2010 amounted to 17.37 million tonnes while consumption outpaced with a total of 17.77 million tonnes indicating that copper market was in deficit of 400,000 tonnes as against surplus of 90,000 tonnes over the same period in the previous year.

In the more recent month of January, World Bureau of Metal Statistics data showed that refined copper production increased to 1.67 million tonnes from largely stable 1.6 million tonnes over the past few months.

Exhibit.13: World Refined Copper Production



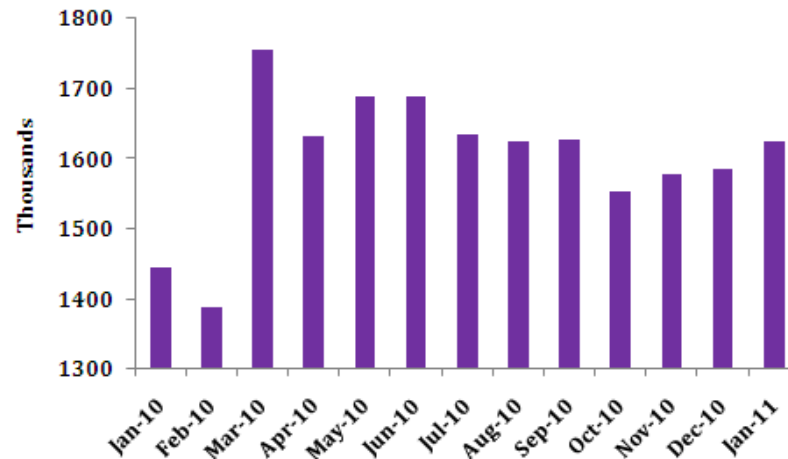
Source: Bloomberg, KCTL Research

World copper consumption has largely been stable at near about 1.6 million tonnes. In the month of January, consumption increased by 2.5 percent to 1.62 million tonnes and might further pick up ahead.

For the whole year, refined-copper output is expected to increase by 1 percent to about 19.3 million tonnes in 2011, while consumption may grow at about 4.5 percent to 19.7 million tonnes. This would result in a net deficit of 435,000 and thereby would support copper prices to move higher.

CHINA: Copper imports by China in the month of February tumbled by 35 percent to 235,469 tonnes, the lowest level in two years. Copper prices largely traded at a discount to London prices thereby have discouraged imports. On the other hand, domestic production increased by 8 percent to 795,000 tonnes and thereby catering to the demand. Output of copper products also jumped by 15 percent indicating that demand for end-products is also higher.

Exhibit.14: World Refined Copper Consumption



Source: Bloomberg, KCTL Research

DEMAND –SUPPLY MISMATCH EXPECTED: Leaving apart the recent increase in production, overall mine capacity is expected grow at a slower pace. Even if one looks at 5 years, copper mine capacity may increase by only 4.9 percent from 2011 to 2014 to reach 24.1 million tonnes, as per the study group. Mines continue to face issues like lower ore grades and shortage of workers and thereby are not able to boost output. But given the strong growth in emerging economies consumption might actually grow at a much accelerated pace thereby keeping the overall market tight.

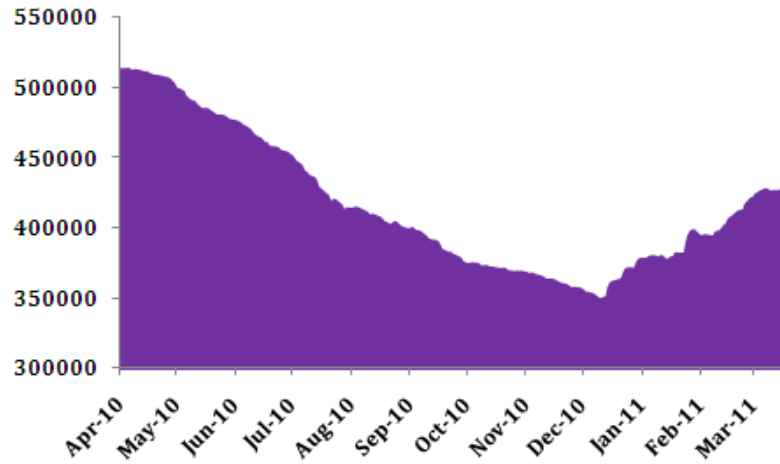
TC/RC CHARGES: Treatment and Refining Charges (TC/RC) are the amount charged by smelters and paid by miners to refine concentrate into metal. Higher TC/RC charges indicate that there is enough supply of the metal and thereby smelters might not compete for the supply. On the other hand, lower TC/RC charges indicate dearth of supply and thereby smelters would have to lower their margin to ensure adequate material.

The TC/RC charges are expected to rise as some capacity is expected to go off stream in Japan. Given the strong earthquake witnessed in Japan, many smelters like Mitsubishi Materials Corp have halted production. So the mined ore would now have to be sold elsewhere. Japan is second largest ore buyer after China and in 2010, Japanese smelters produced about 1.35 million tonnes of copper. Also the nation supplied 253,157 tonnes of metal to China, World’s largest consumer.

Spot TC/RCs moved higher to even \$120 a tonne up after the Japan earthquake as against average range of \$90-\$110/tonne.

INVENTORY: After decline in stocks by more than a 100 thousand tonnes in 2010 from the London Metal Exchange warehouses, copper stocks in the first quarter of 2011 rose by 13.8 percent or 52,100 tonnes thereby taking the total stock to 429,650 tonnes. Though this may seem higher it just amounts to around 2 percent to total global consumption as against nearly 10 percent for aluminium.

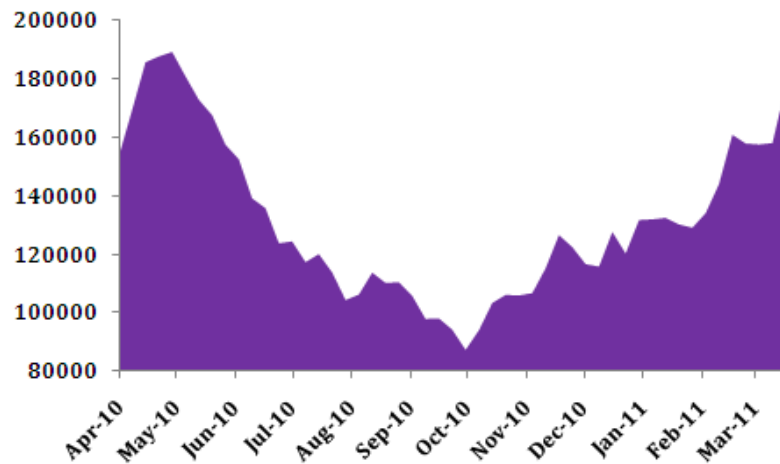
Exhibit.15: LME Inventory – Copper



Source: Bloomberg, KCTL Research

Warehouses in China also witnessed net build-up of stocks to the extent of 34.5 percent, but in absolute terms this amounted to just 45,474 tonnes thereby taking the total stock to 177,365 tonnes.

Exhibit.16: Copper Inventory in Chinese warehouses



Source: Bloomberg, KCTL Research

OUTLOOK: Japan’s demand for copper might decline in the near term as it might take some months before reconstruction activity starts. At the same time, supply might also decline as the country is World’s third largest producer of refined copper.

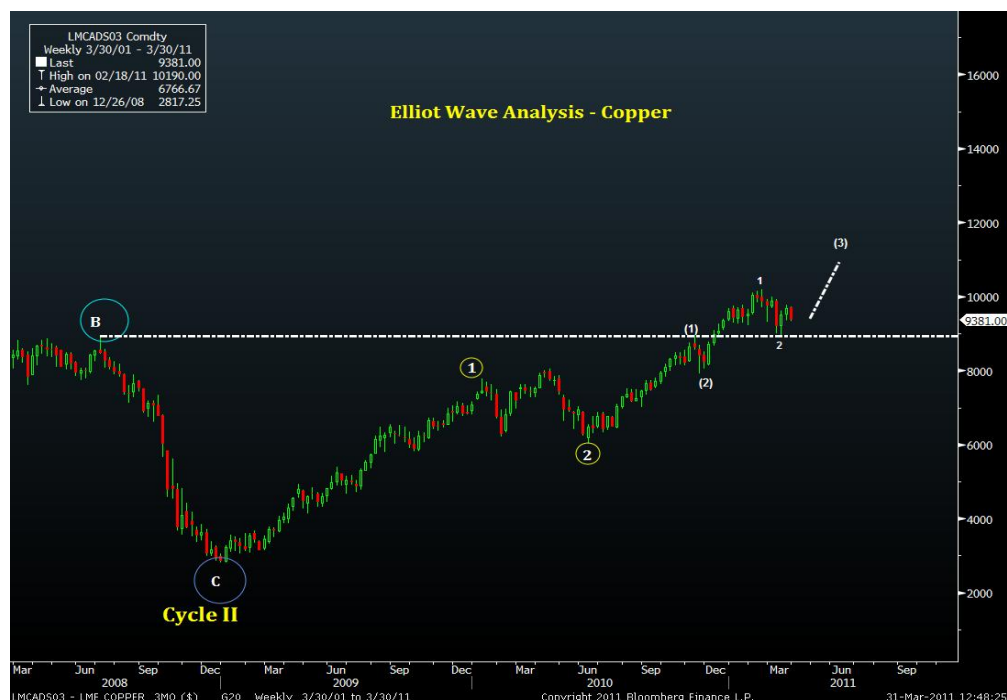
Chinese consumption would continue to remain crucial as it constitutes nearly 40 percent of World copper consumption. In 2010, its total consumption amounted to 7.9 million tonnes, an increase of 5.2 percent.

Second quarter is also considered to be peak season for demand especially in China as traders start to restock before construction activity picks up in the third quarter. Given that prices have declined from peaks, demand might pick up in the second quarter. So demand would remain strong unless strong measures are taken by the government, which seems unlikely, to cool the economy.

TECHNICALS:

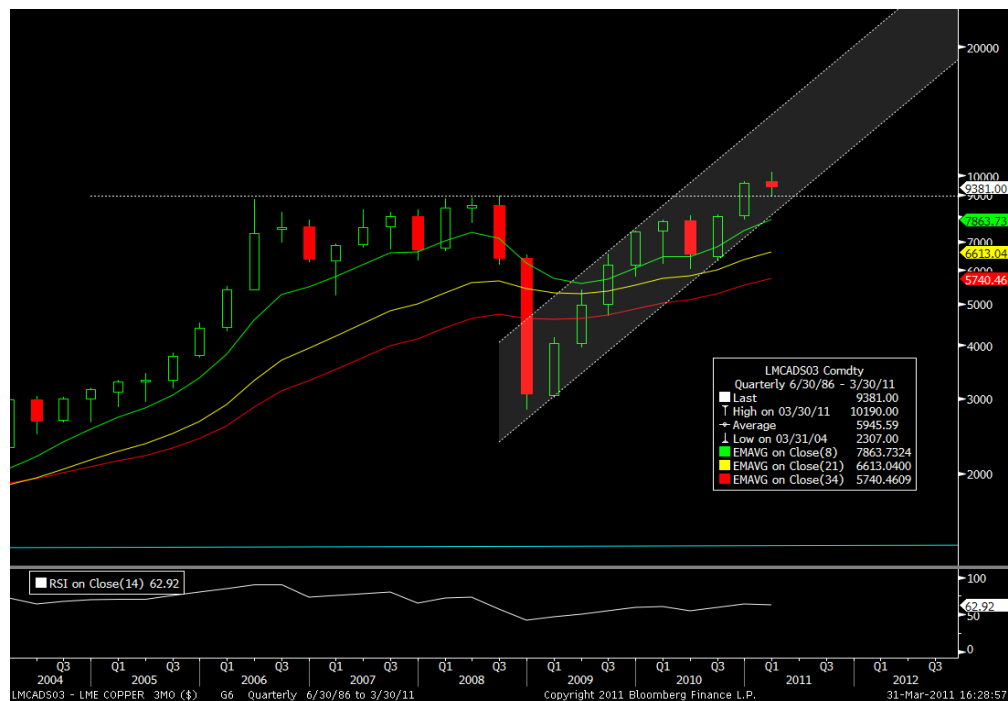
View: Upside; **Strategy:** Buy

Outlook: As per the analysis market took a minor correction till 8944 levels (minor wave 2 of intermediate wave (3)) and having a strong support near 8940 (previous swing high), which may help the prices to remain higher if it holds. A minor trend line resistance is seen at 9780 levels any significant break above the same confirms the price action of minor wave 3 having upside potential till 10800 initially. As long as market holds the support at 8940 it is expected to remain higher.



Copper traded initially higher and recovered all the gains then closed flat on last quarter. It made a high of 10190 then low of 8944.50 and settled at 9585 levels. Closing of the candle renders indecisive movements for the next quarter. Prices are witnessing support at 8940 levels (previous swing highs). On sustained trade above is likely to trade higher. Prices are witnessing trend channel formation on the higher and prices are hovering within the trend channel from the past couple of quarters. The momentum indicator RSI 14 quarterly is trading at 0.629 levels and suggesting higher potential. However, a mild correction on the lower side may be expected before resuming its uptrend.

CONCLUSION: We expect prices to trade higher and recommend buying at the support levels.



RECOMMENDATION:

LME 3M Fwd: Buy at 9100-9200 TP 10200 SL 8900

MCX: Buy at 400-410 TP 465 SL 380

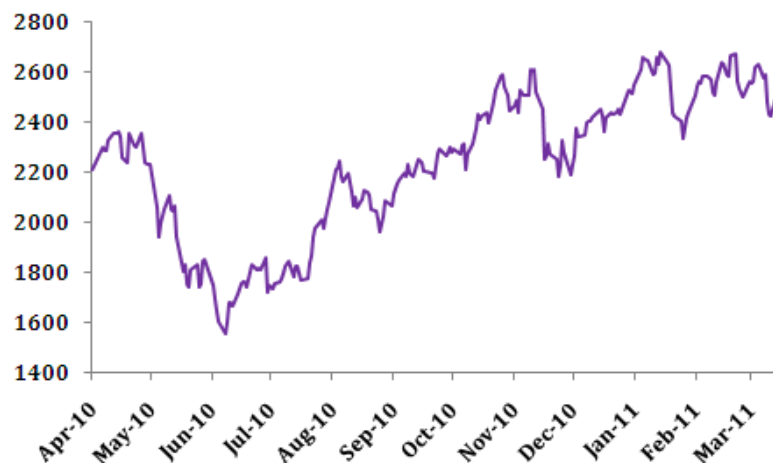
LEAD

PRICE PERFORMANCE: Lead prices ended the first quarter of 2011 on a strong note as they ended with 5 percent gains on LME and MCX. Except for nickel, it outperformed most of the other base metals on the back of strong demand. During the quarter prices made a high of \$2,740/tonne and a low of \$2,325/tonne before ending at \$2,677/tonne on London Metal Exchange. In Indian markets also prices recovered from low of ₹108/Kg to end at ₹123/Kg.

Period	LME	MCX
Q1 2011	5.0%	4.9%
Q4 2010	10.8%	13.8%
Q3 2010	31.4%	28.8%
Q2 2010	-18.5%	-17.6%
Q1 2010	-11.7%	-14.2%

Lead prices started the year on a weak note on the back of expectation that given the ongoing monetary tightening phase in emerging markets like China and India, automobile sales might decline. Also stocks on London Metal Exchange increased to the highest level since 1995, thereby further supporting the view. However automobile sales continued to hit record highs and expectation of increase in demand from Japan, owing to power outages sent prices higher. Shanghai Future Exchange has also started lead Futures contract for trading from March 24 onwards.

Exhibit.17: LME Lead Prices (\$/tonne)



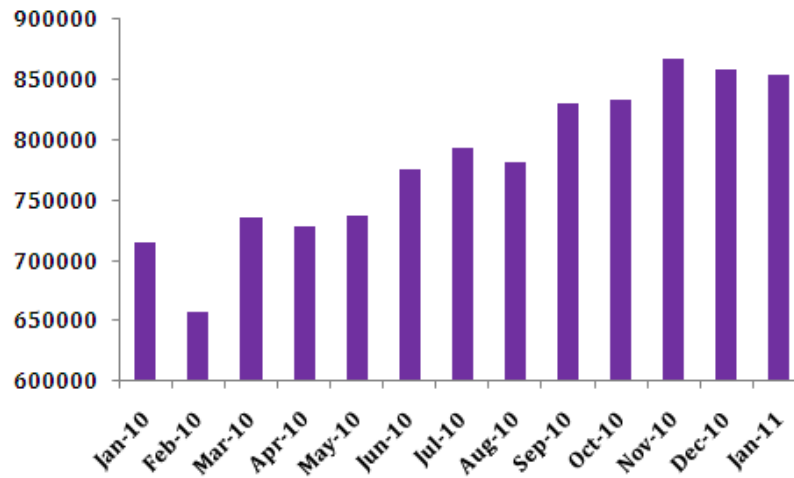
Source: Bloomberg, KCTL Research

FUNDAMENTALS:

According to International Lead and Zinc Study Group, global lead production declined by 5 percent to 0.814 million tonnes in the first month of 2011. However on a year-on-year basis, this was higher by 13.4 percent. The increased production was largely owing to increasing production in China as smelters in some of provinces which were previously closed owing to cut in power supplies would have restarted production on the back of regular power supplies.

World’s largest consumer of the metal, China, has been ramping up production as the demand for batteries, the major user industry of the metal, has been escalating.

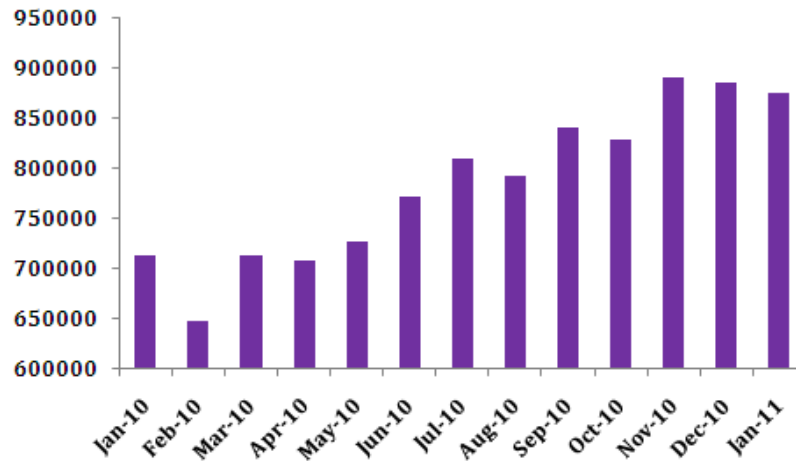
Exhibit.18: World Refined Lead Production



Source: Bloomberg, KCTL Research

Usage of the metal has also increased on a year-on- year basis by 13.2 percent while on a month-on-month basis it has declined by nearly 7 percent to 0.813 million tonnes. The usage growth got a boost from nearly 33 percent growth in demand from China. Overall, in the month of January, demand exceeded supply by 1,000 tonnes as against balanced market in the same month of previous year. For the whole of 2010 global lead market was in surplus of 37,000 tonnes.

Exhibit.19: World Refined Lead Consumption

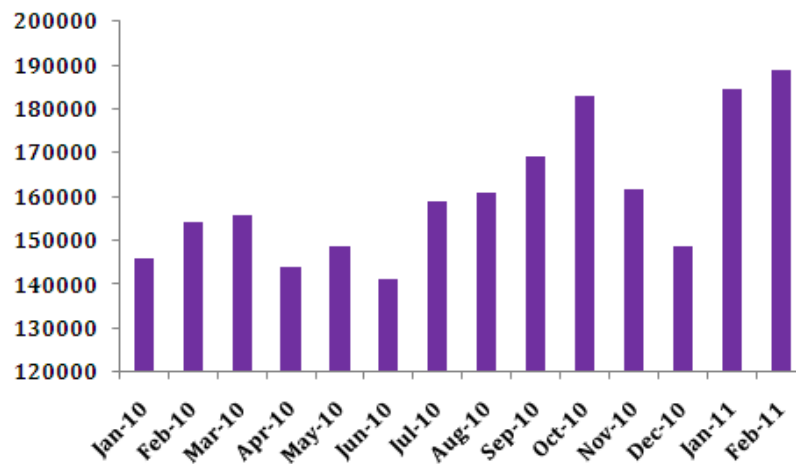


Source: Bloomberg, KCTL Research

AUTOMOBILE MARKET: In the automobile market, China continues to remain on the top with annual production of nearly 130 million cars. Sales continue to remain strong, despite recent measures by the government to cool down the economy. Same is the case in India as well.

India is the seventh largest car maker and despite recent interest rate hikes demand continues to remain strong. After increase in sales by 31 percent to 14.8 million units in 2010, this year might witness moderation in growth but that might be largely owing to higher base and a reasonable level of anywhere between 12-15 percent growth might be witnessed. Talking about the more recent month of February, automobile sales in India hit a record high of 189 thousand units, representing a growth of 23 percent year-on-year basis.

Exhibit.20: Passenger Car Sales – India



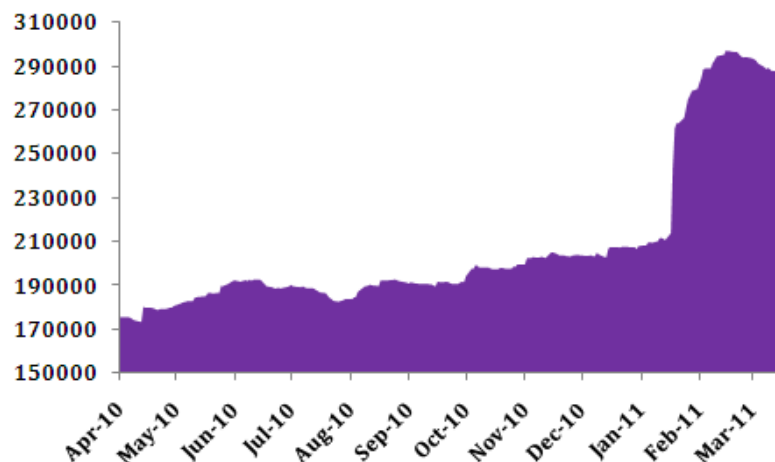
Source: Bloomberg, KCTL Research

Developed nations are also witnessing pick-up in sales. US sales grew by 11 percent to 1.16 Crore units in 2010, thereby ending four consecutive years of de-growth, though some might be attributed to government incentives like Cash for Clunkers.

On the industry front, Ivernia, the company which accounts for roughly 2 percent of global production, suspended operations for a brief period in the start of January after government order forced it to cut output. However by the end of February it re-called the workers as the ban was lifted.

INVENTORY: Increase in inventory has been one of the areas of contention, thereby leading to underperformance of lead prices. Stocks increased by a massive 38.5 percent or 80,375 tonnes there taking the total stock to 288,650 tonnes. Total stocks stands at the highest level since 1995.

Exhibit.21: LME Inventory - Lead



Source: Bloomberg, KCTL Research

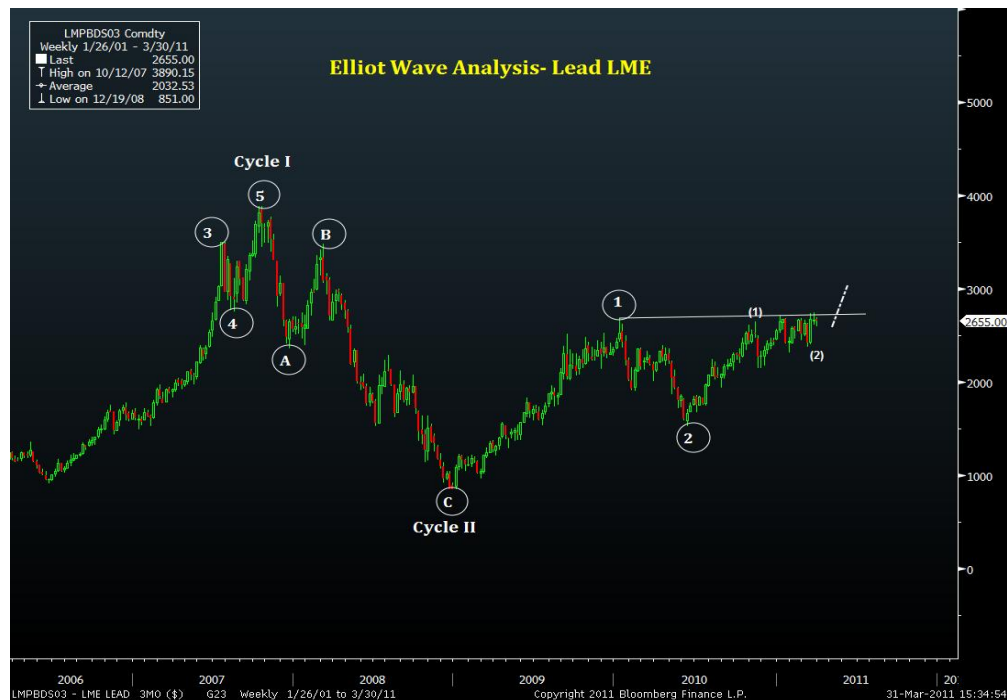
OUTLOOK: Japan witnessed strong catastrophe thereby sending leading massive destruction of companies and thereby power outages also followed. This might lead to incremental demand for lead as batteries might be the best alternative in the short term. Even a lot of cars and automobiles have been destroyed thereby raising prospect for long term demand for the metal. Other markets also continue to witness increase in demand and thereby would support prices to trade higher.

TECHNICALS:

View: Sideways to higher;

Strategy: Buy near support levels.

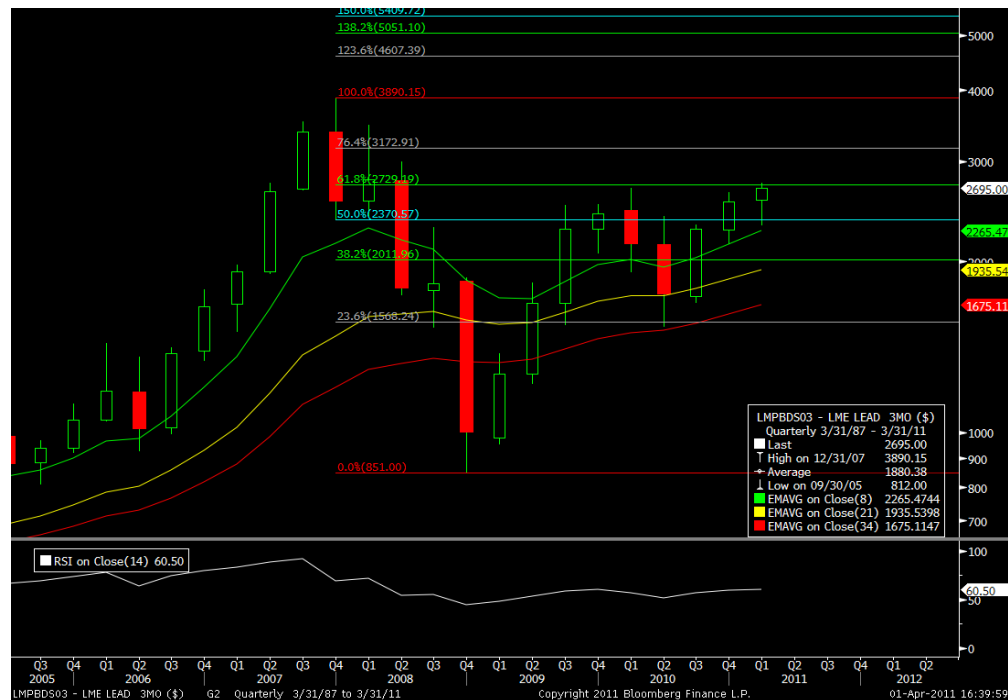
Outlook: Lead 3M forward prices moved in a range of 2320-2760 levels for the past three months. Market is moving near the resistance level at 2750 levels. A convincing break above the same it is possible to extend its gains further in near term and the upside potential is seen till 3000 levels. If market fails to breach the resistance at 2750 levels it is possible to continue the sideways movements. Downside strong support is seen at 2300 levels, which could help the prices to remain higher. Overall, analysis suggests prices to move sideways with higher bias.



Lead prices traded higher on last quarter by continuing the previous trend. It made a low of 2325 then high of 2747 and before settling higher at 2695 levels. Closing of the candle renders upside movements for the coming quarter. Prices have breached the key resistances at 2690 levels (previous swing highs). On sustained trade above is likely to trade higher.

The principle of Fibonacci retracement states that prices are witnessing immediate resistance at 2730 levels which is 61.8% retracement of the range (851-3890) levels. On breach and sustained trade above is likely to remain higher. However on the lower side key support level is seen at 2370 levels which is 50% retracement of the above mentioned range. On sustained trade above is likely to remain higher. The moving average principle suggesting bullish trend as prices are trading well above the short and medium term EMA's of (8, 21&34).

CONCLUSION: We expect the prices to trade higher and recommend buying at the support levels.



RECOMMENDATION:

LME 3M Fwd: Buy at 2550-2600 TP 3000 SL 2350

MCX: Buy at 115-119 TP 129 then 140 SL 108

NICKEL

PRICE PERFORMANCE: Nickel, the base metal that outperformed most of the other base metals in the year 2010, continues its strong run in 2011 as well. In the first quarter of 2011, nickel prices ended with gains of more than 8 percent on both LME and MCX. During the quarter they made a high of \$29,425/tonne and a low of \$23,822/tonne before ending at \$26,750/tonne. In Indian markets, prices ended at ₹1,200/Kg.

Period	LME	MCX
Q1 2011	8.1%	8.4%
Q4 2010	6.0%	6.5%
Q3 2010	18.2%	16.1%
Q2 2010	-21.0%	-20.0%
Q1 2010	34.9%	30.4%

Demand for steel continues to remain strong in countries like India and China thereby boosting demand for nickel, the metal used in making steel. Largely balanced market along with draw-downs of stocks from exchange warehouses supported prices to trade higher. Supply disruption at major producing companies further raised fears that market might even turn to deficit. However tensions in Middle-East along with catastrophe in Japan, lead to decline in prices by nearly 10 percent from highs.

Exhibit.22: LME Nickel Prices (\$/tonne)



Source: Bloomberg, KCTL Research

FUNDAMENTALS:

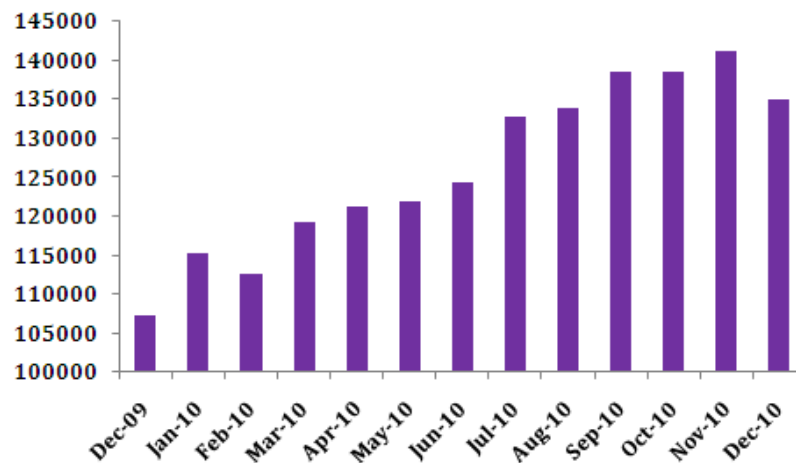
World, nickel ores and concentrate production declined by 4.2 percent to 135,061 tonnes in the month of December. Over the past few months, production has largely been stable. In China, after increasing to record high of 22,015 tonnes in the month of January, nickel output in month of February declined to 16,871 tonnes. However in 2011, instances of production disruption have increased.

Vale, Brazil based miner and one of the largest producer of Nickel, said that it would lose around 5 percent of the total 2011 nickel production. This is largely owing to 16-week shutdown of a smelter furnace in Canada thereby resulting in production loss of 15,000 tonnes.

Caledonia, the region lying between Tahiti and Australia, witnessed cyclone in January. Five nickel mines in the Island, which contributes roughly 4 percent of the global production were impacted. All this is indicating how the supply side continued to face disruption and thereby production numbers ahead might decline.

The only silver lining in all these has been the restart of production at Kwinana nickel refinery whose production was hit in December due to a shortage of nitrogen gas. The company alone accounts for roughly 5 percent of global production and thereby restarting of production was able to put a cap on prices.

Exhibit.23: World Nickel Ores and Concentrate Production

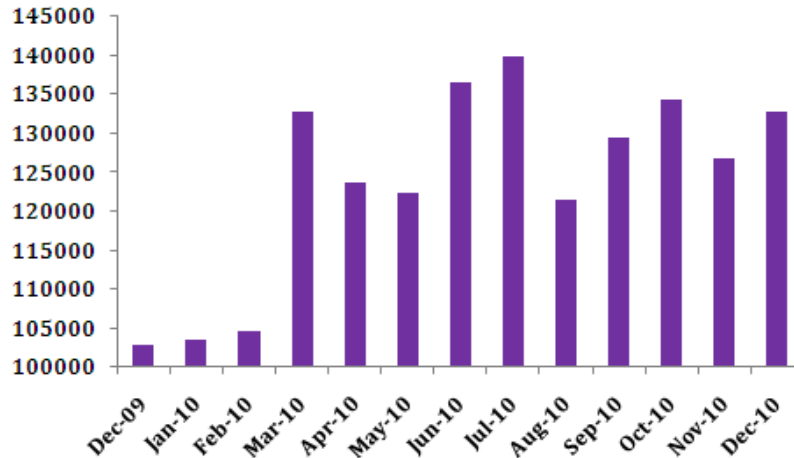


Source: Bloomberg, KCTL Research

On the other hand, consumption continues to remain on the higher side given the strong demand from nations like China. In the month of December, consumption increased by 4.6 percent to 132,628 tonnes.

In the month of January, the nickel study group reported surplus of a meager 5 tonnes. For the whole year, the market might even turn to deficit. In fact, even the decline in inventory is also pointing towards a tight market in 2011.

Exhibit.24: World Semi-Refined Nickel Consumption

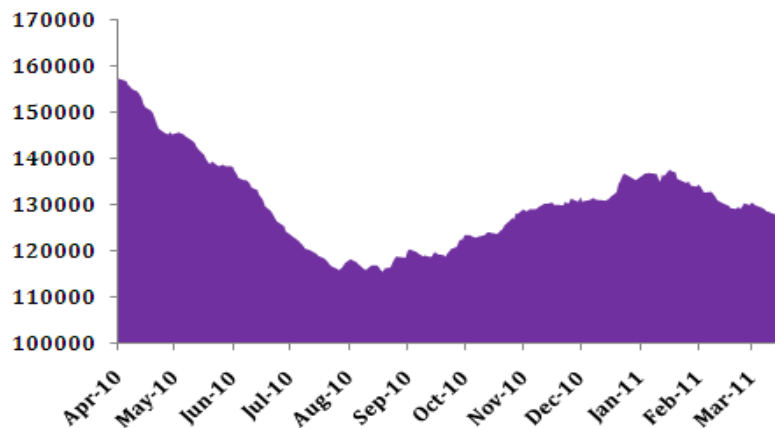


Source: Bloomberg, KCTL Research

On the industry front, Lundin Mining said that operations at its mine in Spain will not resume till 2012. Heavy rains caused landslide at the mine in December and operations have remain halted since then. Though for short durations, there were other production disruptions as well like the Yabulu nickel refinery in Australia.

INVENTORY: Nickel stocks on London Metal Exchange declined by 7.8 percent or 10,572 tonnes thereby taking the total stock to 125,100 tonnes. In fact, nickel was the only base metal to witness net draw-down of inventory thereby indicating strong demand for the metal.

Exhibit.25: LME Inventory - Nickel



Source: Bloomberg, KCTL Research

OUTLOOK:

On the one hand, disruptions continue to constraint the supply growth of the metal while on the other, demand continues to remain strong from large producing countries like China. Inventory has been witnessing net draw-downs from London Metal Exchange the decline has been the most consistent among all the base metals. Premium of the metal in the spot market has been increasing indicating good demand for the metal. All this is expected to support nickel prices to trade higher.

TECHNICALS:

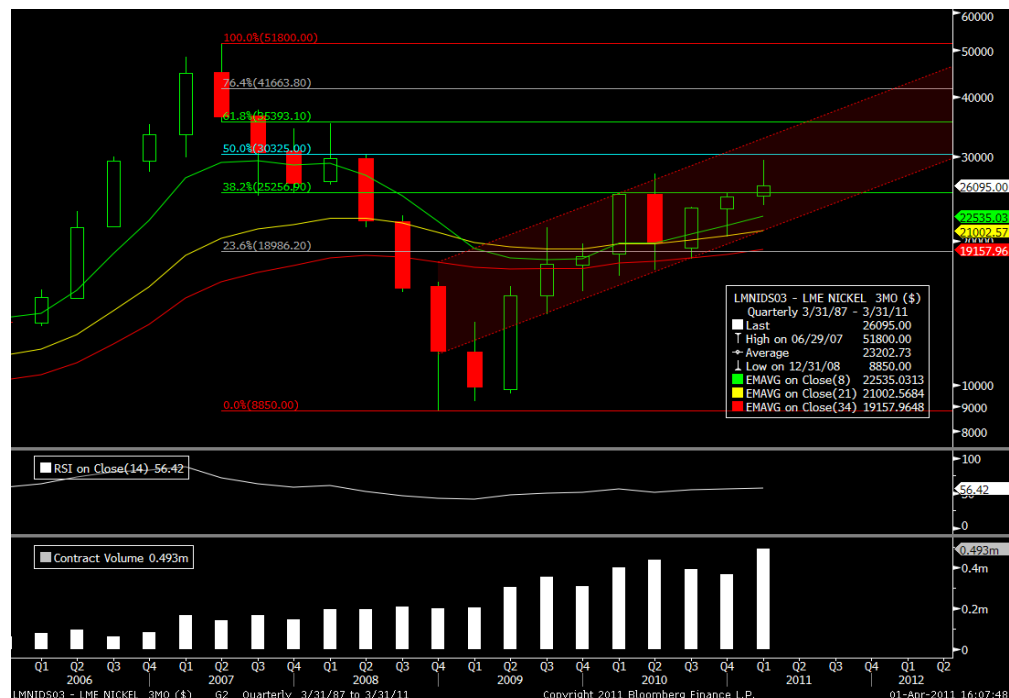
View: Upside

Strategy: Buy

Outlook: Nickel 3M LME forward prices made as high as 29425, which is considered as minor wave 3 of intermediate wave (3) and recently it tested the low of 24675 levels. However, if market fails to breach the support at 24675, thus conclude the end of minor wave 4 followed by minor wave 5 having upside potential further. The strong support to watch is at 23700 levels, those who would like to go for long position can keep stop loss below the same. Overall, we are having a sideways view with upside movement in the range of 23000-29500 levels.



Nickel prices traded higher on previous quarter and it was up by as much as 5.54% on last quarter. It made a low of 23822 then high of 29425 and settled at 26095 levels. Closing of the candle renders upside movements for the coming quarter. The principle of Fibonacci retracement states that prices are witnessing resistance at 30325 levels which is 50% retracement of the range 8850-51800 levels. On sustained trade above is likely to trade higher. Prices are witnessing trend channel formation on the higher side and allowing the markets to trade higher. The momentum indicator RSI 14 quarterly is trading at 0.564 levels and suggesting upside movements. The Volume indicator analysis also signifying upside movements as volumes have increase from 0.365M contracts to 0.493M contracts. A mild correction on the lower side may be expected before resuming its uptrend.



RECOMMENDATION:

LME 3M Fwd: Buy at 23800-24200 TP 29000 then 31000 SL 21000

MCX: Buy at 1130-1140 TP 1240 then 1300 SL 1050

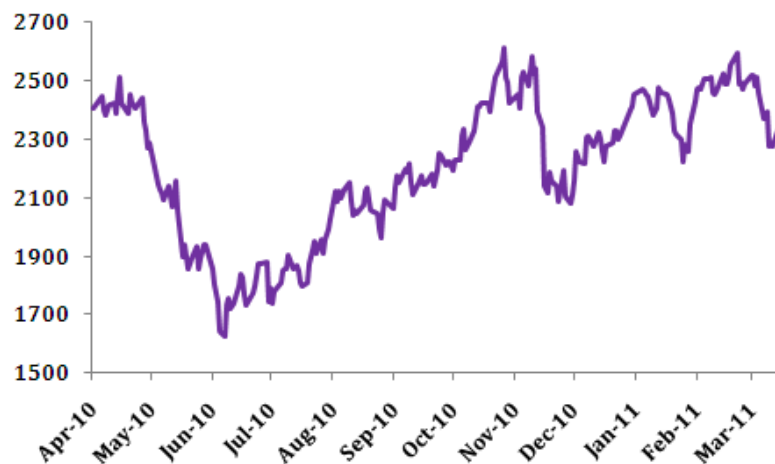
ZINC

PRICE PERFORMANCE: Zinc prices ended the first quarter of 2011 down by 5 percent on LME and nearly 4 percent on MCX thereby underperforming the entire base metal pack. During the quarter zinc price made of high of \$2,600/tonne and low of \$2,220/tonne before ending at \$2,325/tonne on London Metal Exchange. In Indian markets, zinc price ended at ₹105/Kg.

Period	LME	MCX
Q1 2011	-5.2%	-3.9%
Q4 2010	10.3%	10.6%
Q3 2010	24.1%	22.1%
Q2 2010	-24.5%	-24.3%
Q1 2010	-7.2%	-11.3%

Prices though started the year on a strong note on the back of improving economic outlook could not sustain the gains and ended the quarter lower. Fundamentals of the zinc continue to remain weak as supply continues to outstrip demand thereby keeping enough availability of material in the market. Stocks on London Metal Exchange warehouses also continue to witness net build-up thereby adding to the pressure on prices.

Exhibit.26: LME Zinc Prices (\$/tonne)



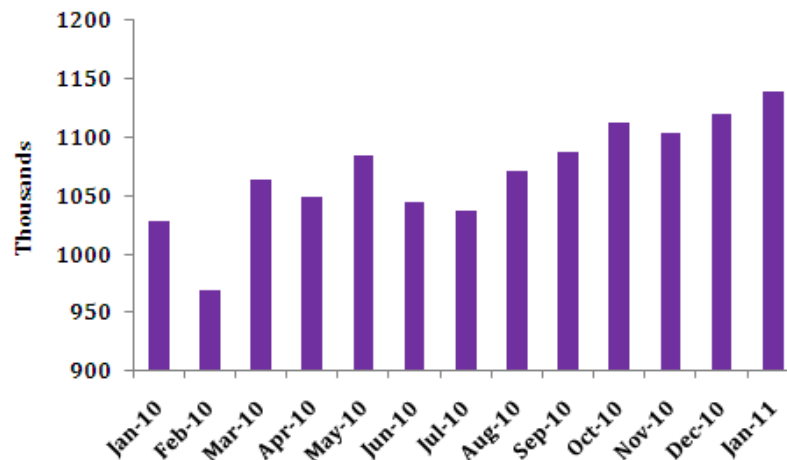
Source: Bloomberg, KCTL Research

FUNDAMENTALS:

Global zinc slab production rose by 1.6 percent in the month of January to 1.13 million tonnes. Production on a monthly basis has largely been increasing though at a stable of 1 to 2 percent.

In China, zinc output in the first two months of 2011 fell by nearly 13 percent to 799,000 tonnes. Decline in production largely owed to cut in power supplies thereby impacting production. For instance, a zinc smelter in Henan with capacity of 200,000 tonnes a year cut production in January on reduced power supply. However going forward, production might normalize as reports indicated that power supply might increase in the months ahead.

Exhibit.27: World Zinc Slab Production

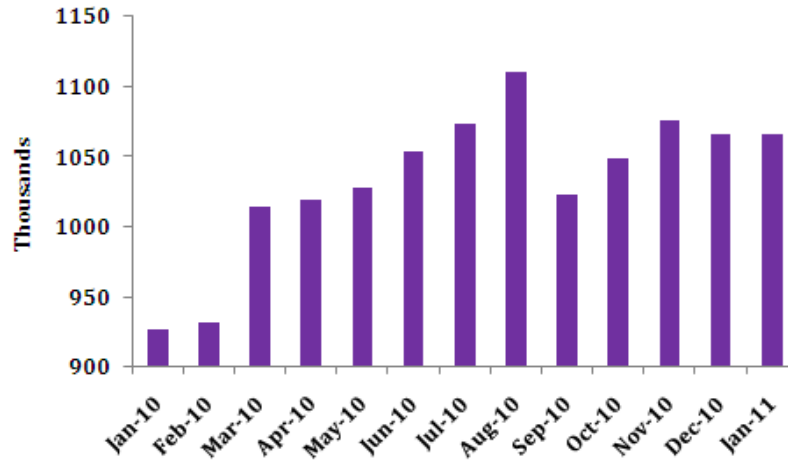


Source: Bloomberg, KCTL Research

Consumption on the other hand, has largely remained flat at 1.06 million tonnes, for almost couple of quarters now. So increase in production along with largely stable supply does not bode well for zinc price. Overall market continues to remain surplus and as per the international lead and zinc study group this surplus was 36,000 tonnes in the month of January.

On the industry front, Japan’s top zinc smelter, Mitsui Mining and Smelting Company, would remain shut for a while as a devastating earthquake and Tsunami damaged the facilities. So the company would import the bare metal. The company has a capacity of 110,000 tonnes a year.

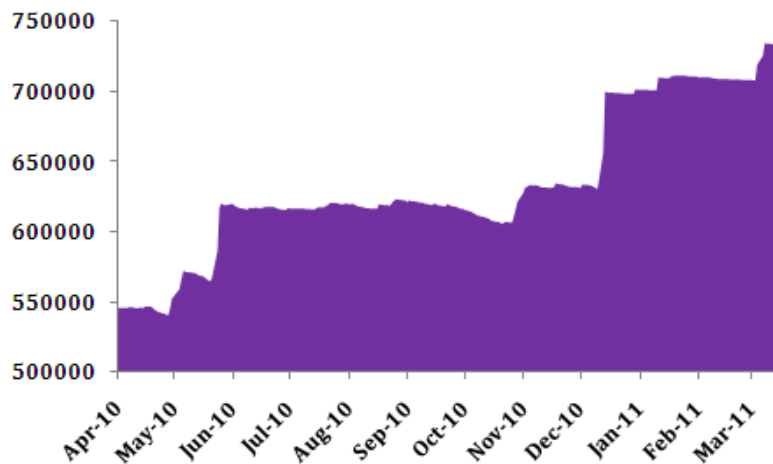
Exhibit.28: World Zinc Slab Consumption



Source: Bloomberg, KCTL Research

INVENTORY: Given the oversupplied market, zinc stocks on London Metal Exchange witnessed net build-up. In the first quarter of 2011, stocks increased by 5 percent or 34,775 tonnes thereby taking the total stocks to 736,200 tonnes. Though this may seem minute, it comes on the back of 215,150 tonnes increase in the year 2010.

Exhibit.29: LME Inventory – Zinc

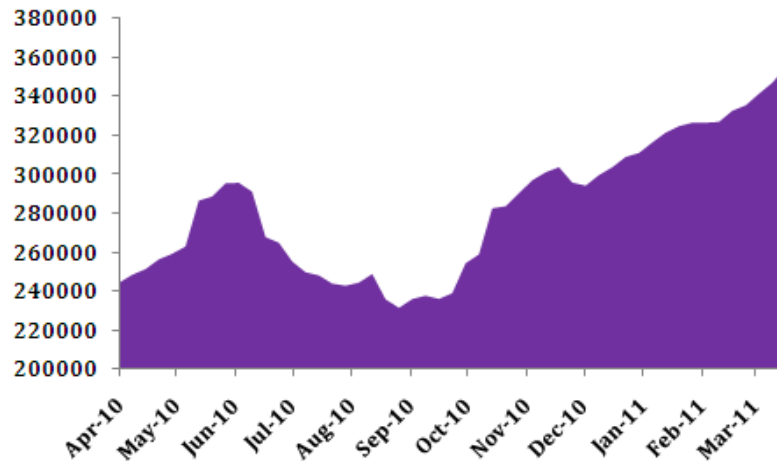


Source: Bloomberg, KCTL Research

Warehouses in China also witnessed net build-up of stocks. Stocks increased by 15 percent or 43,801 tonnes thereby bringing the total stock to 354,536 tonnes.

So the total stocks on both LME and Chinese warehouses come to more than a million tonnes which is almost equal to the one months World consumption and one of the highest among all the base metals. If one adds the inventory off the warehouses, of which there is no clear estimate, it would be much higher.

Exhibit.30: Zinc Stocks In Chinese Warehouses



Source: Bloomberg, KCTL Research

OUTLOOK:

Reports indicated that nearly 60 percent of the Japan’s production capacity of zinc was closed. In 2010, the country accounted for 271,000 tonnes of production. Closure of smelters along with anticipation of pick-up in demand, pushed the premiums in the spot market slightly higher. This along with improving economic outlook may support zinc prices to trade higher. However higher inventory levels along with overall surplus market might cap the gains of the metal.

TECHNICALS:

View: Upside

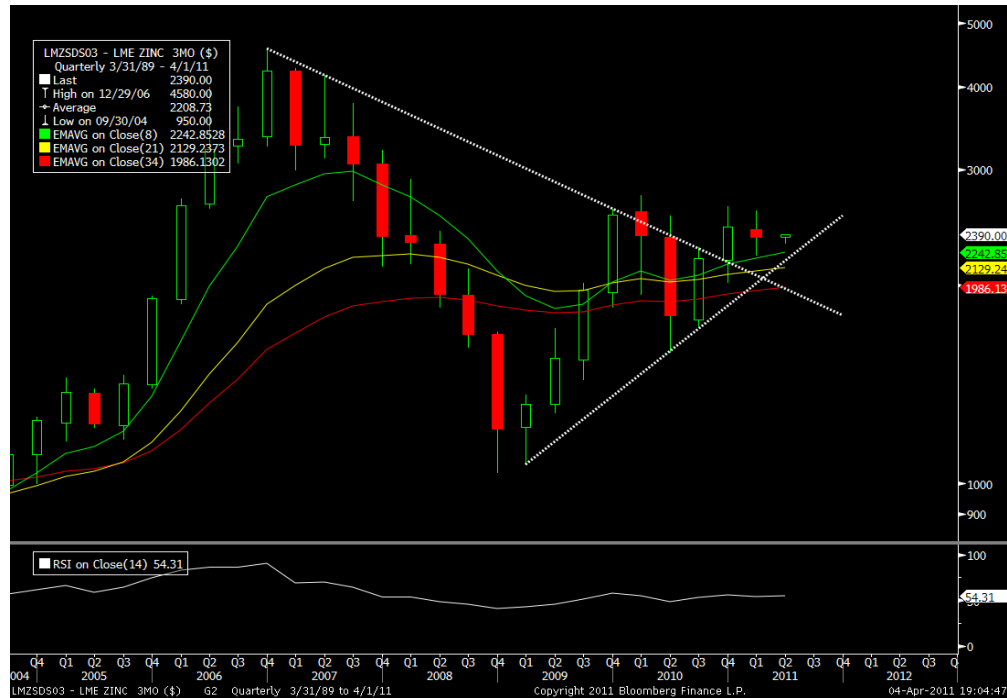
Strategy: Buy

Outlook: Zinc 3M LME forward prices took a lower correction from as high as 2599.75 and currently trading at 2338 levels. Currently prices are trading in a corrective intermediate wave (2) with unfolding nature. However, on the downside market is witnessing a strong trend line support at 2230 levels. Sustained trade above it is expected to bounce back. Conversely, on the higher side resistance is at 2600 levels. Only on breach of the same it is expected to confirm bullish trend for short to medium term. Overall, we expect prices to move in the range of 2100-2600 levels.



Zinc prices traded lower on last quarter by reversing the previous trend. It made a high of 2599.75 then low of 2220 and settled at 2362 levels. Closing of the candle renders indecisive movements for the coming quarter. Prices are witnessing trend line support at 2200 levels. On sustained trade above is likely to trade higher.

Prices are witnessing resistance at 2736 levels (previous swing highs). On breach and sustained trade above is likely to trade higher. The momentum indicator RSI 14 quarterly is trading at 0.543 levels and suggesting upside movements for the coming quarter. The moving average principle also suggesting upside movements as prices are trading well above the short and medium term EMA's of (8,21&34) levels. However a mild correction on the lower side may be expected before resuming its uptrend.



RECOMMENDATION:

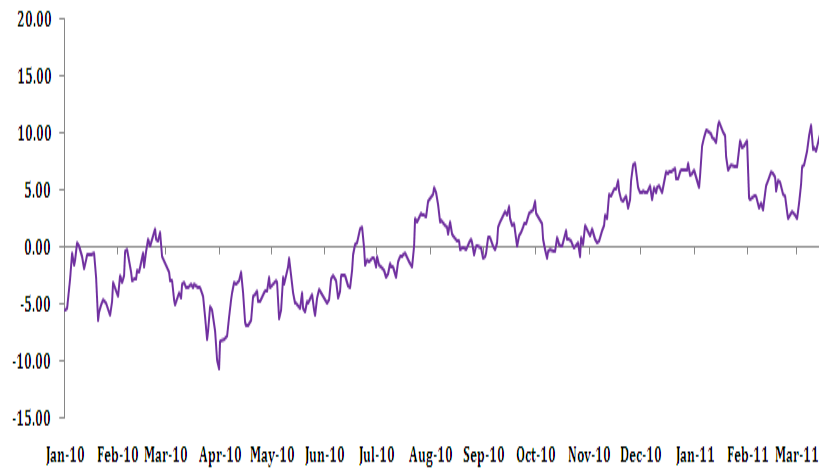
LME 3M Fwd: Buy at 2200-2225 TP 2600 then 2730 SL 2050

MCX: Buy at 97-100 TP 115 then 124 SL 93

LEAD –ZINC SPREAD STRATEGY

At the start of the first quarter of 2011, lead price underperformed zinc on the back of rising stocks thereby sending the difference between the prices of both the metals to 2.5. However later, as lead prices recovered, with the key reason being the strong demand from automobile sector, this spread moved higher. It ended at 16.7, the highest level in one and half year.

Exhibit.31: Lead –Zinc Spread (Lead Price – Zinc Price)



Source: Bloomberg, KCTL Research

Purely on fundamental basis, zinc market continues to remain oversupplied and the demand prospects for lead continue to remain strong. Given the strong run-up in both lead prices and the spread, a lower correction is expected. However given the relatively strong fundamentals of lead, the bias for the spread continues to remain on the higher side.

NOTE: We have assumed Mar 18, 2011 as the end of quarter for the preparation of this report.

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