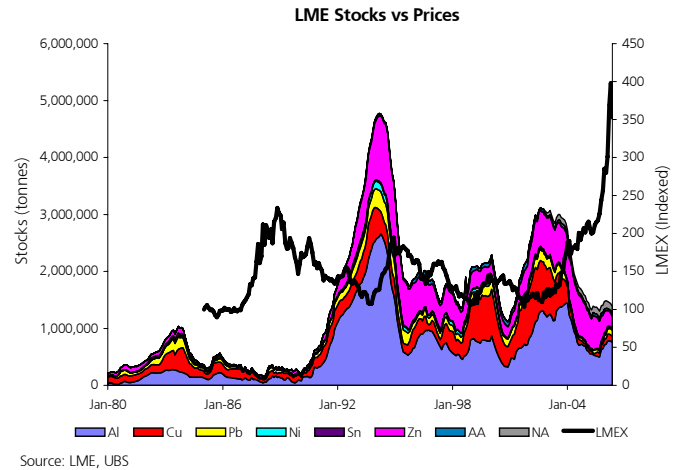


Base metals underpinned by low LME stocks

Inventories of base metals held in storage in LME warehouses have been steadily declining this year, the combined total of the eight metals traded on the exchange is currently at 1.38Mt compared to 1.41Mt at the end of 2005 and sharply down on the October 2002 peak of 3.12Mt. However, this masks the fact that inventories of some metals such as copper, nickel and zinc are at or are approaching critically low levels. Whereas, for metals such as aluminium and lead, the situation is much more comfortable and consumers are not scrambling around to secure physical metal in tight markets. LME stocks are likely to remain relatively low in the short to medium-term, with refined production growth limited in most cases and demand remaining robust on the back of strong global economic growth. With LME stocks low and the situation throughout the supply pipeline not that much different, prices will be well supported, albeit at not such elevated levels as before.



▪ **Base metals seeking direction**

Most base metals ended higher with the exception of aluminium and tin in thin and dull trading conditions ahead of the FOMC meeting which concludes today. A 25 bp rise in US interest rates has been discounted by the markets but the tone of the accompanying FOMC statement will be of much more importance with it being scrutinised to see whether interest rates are close to their peak. Copper is seen in a wide \$6,400-7,200/t range with trade interest evident at both ends of the range. A close above \$7,250/t is needed to see upward momentum generated. If this is the case then, the other metals will be dragged higher as well. The approach of the month/quarter/half-year end is likely to see some window dressing by traders and erratic price moves as a result. We remain friendly to the metals complex but expect them to be vulnerable to any broader asset market weakness with the resumption of Fed comments and data flow. Better buying opportunities should present themselves over the slow summer period. Nickel remains our favourite based on strong fundamentals.

▪ **Strikes at Grupo Mexico closer to being resolved**

Crippling strikes at two giant copper mines owned by Grupo Mexico will continue at least until after the July 2 presidential election, a source at the company said on Wednesday. The strikes at the La Caridad and Cananea copper mines would be more easily resolved after Mexico had chosen a new president. La Caridad and Cananea accounted for close to half Grupo Mexico's total 2005 output of 689,928 tonnes of copper. Grupo Mexico is waiting for a labor tribunal ruling to allow it to close La Caridad and fire the strikers (Reuters). A new president could find it politically easier to resolve the strikes especially as Napoleon Gomez, the ousted union leader, is no longer part of the problem.

▪ **Unions at Inco and Falconbridge worried over job losses if Phelps Dodge bid succeeds**

Unions representing thousands of workers at Inco and Falconbridge said on Wednesday that jobs will be lost if U.S.-based Phelps Dodge plan to buy the two Canadian mining companies for \$40 billion succeeds. The Canadian Auto Workers union, which represents 1,600 workers at the miners in Canada, sent Prime Minister Stephen Harper a letter saying there is a "threat of long term job losses for hundreds of workers in Northern Ontario regions." "The consolidation of Canadian facilities may result in a reallocation of capital toward foreign projects, with negative impacts on Ontario investment," said the CAW, Canada's largest private-sector union. Meanwhile, the United Steelworkers union, which represents more than 7,500 workers at Inco and Falconbridge, called for the resignation of Canada's finance minister, Jim Flaherty, a day after he joked, "I haven't heard any suggestions that they would move the mines." Phelps has promised not to lay off any workers at Canadian operations for three years after the deal closed. Both unions have said that the Phelps offer should be challenged and are calling on the federal government to back a "made-in-Canada" deal instead (Reuters).

▪ **Start-up of new Chinese copper smelter delayed until mid-2007**

A new 200,000-tonne-a-year Chinese copper smelter expected to be up and running in July will miss the target date, industry officials said on Thursday. An official for Fambros Group, which is also known as Shandong Fengxiang Group, said in April the plant could begin production in July this year. But now the start-up is expected between May and June 2007, said an executive for Xiangguang Copper Co. Ltd., a Fambros subsidiary that will operate the plant. He gave no reason for the delay. Xiangguang is a newcomer in China's copper industry and has approval from Beijing to build the plant, which is intended to have an annual capacity of 400,000 tonnes. It was trying to bring in Norddeutsche Affinerie, Europe's largest copper producer, to jointly operate the plant in the Shandong province but talks between the two parties ended without success earlier this year. An industry official who recently visited the plant site said Xiangguang had nearly finished the refining system at the plant but would take months to complete the flash furnace, used

to smelt raw material concentrate. The plant could use about 140,000 tonnes of concentrate this year if it began production in July, according to traders' estimate. Traders said Xiangguang's delay was adding to concentrate supply because its suppliers were reselling its contracted cargoes to other Chinese smelters, driving up processing fees. Overseas suppliers were offering the fees of more than \$80 a tonne for treating and 8 cents a pound for refining their spot concentrate, up from \$60 to \$70 and 6 cents to 7 cents in early June. But China Smelters Purchase Team, which is made up China's eight largest copper smelters, is demanding \$100 and 10 cents. The smelters buy about 80 percent of China's imported concentrate to jointly import spot concentrate. "By July to August, we will adjust our output if the fees do not meet that level," a team official said of production cuts. The team was asking Beijing not to issue import permits to its members for spot concentrates that were concluded at fees below that level, after July 10 (Reuters).

▪ **Little to stop wide ranges continuing in metals but near term direction is lacking**

With global markets narrowly focussed on today's Fed decision and many precious metals participants slouching back from Montreux precious metals remained quiet over the past twenty-four hours. Gold trading around \$580/oz, silver around \$10.30/oz, palladium just above \$300/oz and platinum just below \$1200/oz. It is interesting that the only metal we have had to update our support and resistance levels for is platinum, which has made ground recently while the other metals have traded broadly sideways. In light of our fundamental view and the snippets of information contained in the paragraph below this is not surprising. But with the exception of palladium we see no need to hurry back into metals at the moment; there is considerable risk from US inflation / growth / interest rate expectations and implied volatility is high for all metals indicating that the market is not swamped with short dated option sellers; this should keep daily trading ranges wide and perhaps biased to the downside. We hold our one-month and three month forecast for gold at \$550/oz and \$580/oz respectively.

▪ **LBMA delegates positive but not euphoric about gold and other metals**

The annual LBMA precious metals conference took place in Montreux, Switzerland on Sunday-Tuesday this week. The conference was well-attended by market participants, although investors were few and far between as usual. As this is the most important event for the bullion market, it does represent an unusual opportunity to gauge the sentiment of the market. Indeed we suspect that very bullish consensus amongst delegates at the November 2005 conference in Johannesburg, South Africa contributed to the sharp move higher in gold over the next six months. Our thoughts on the main highlights of the conference are listed below and we will be commenting in more detail on some elements of this summary in coming days and weeks.

Gold: Both the consensus of the delegates we spoke with and the collective forecast of attendees (\$698/oz for mid-Nov 2007), collected by an electronic voting system, remains bullish but we judge somewhat more tempered than the euphoric mood seen in Johannesburg last year. Traders, however, were less positive than the average delegate with some talking of a \$50-100 fall in gold.

Silver: Still bullish although a wide spread of forecasts to get to the mean forecast of \$16.10/oz for Nov-07, although the median would be much at perhaps \$11-12/oz. Supply and demand news was balanced with some hefty forecast production increases our of China likely to increase silver supply in coming years while new applications for silver, notably in lumber treatment, have the potential for large demand upside surprises.

Platinum: Undoubtedly the most bullish story with positive demand stories from both well-know applications such as autocatalysts but also lesser-known applications such as gas to liquid (GTL) processes were also positive. If there was one slightly negative story it was that jewellery demand is under pressure from higher prices, although this is hardly fresh news.

Palladium: It seems clear that the palladium story has improved in recent years with some interesting snippets on Swiss watchmaker demand and US jewellery demand. But even producers believe that for the next few years palladium remains overshadowed by large visible stocks and unknown invisible stocks.

Precious Metals Data

				Gold			Silver			Platinum			Palladium		
USA	High (bid)	Low (off)	Close (m)	586.10	577	578.75	10.37	10.21	10.255	1189 F	1185	1182.5	311 F	309	308
Asia	High (bid)	Low (off)	Close (m)	582.25	581.30		10.31	10.29		1182	1184		303	308	
Europe Opening				581.30 / 90			10.25 / 10.32			1181 / 1186			304 / 308		
Overnight EFPs: (Aug /)				2.25 / 2.45			-9.5 / -8 (Jul) -1 / -1 (Sep)								
Spec Short / Long (Futures & Options)				5.75m / 18.82			112.5m / 330.5m			167.1k / 332.6k			286.2k / 1194.3k		
COTR June 6 th 2006 (not updated)				Ratio 1: 3.3			Ratio 1: 2.94			Ratio 1: 2.0			Ratio 1: 4.2		
Net Spec & Net Non Rep (all metals)				Net Long 13.07m			Net Long 218m			Net Long 165.5K			Net Long 908.1k		
Change on Previous week (+ = longer)				-1.09m			-29.4m			-58.9k			-81.1k		
Exchange OI / Change in OI (oz) (D-2)				29.28m / +457k			545.12m / -27.44m			404.65k / -2.4k			1314.9k / -22.2k		
Comex / Nymex Stocks / Change				8031 / unch			102.7m / -68.5k			22.5k / unch			1112k / unch		
Support and Resistance				544 / 585			9.5 / 11			1170 / 1200			268 / 325		

Implied Volatility	1m	3m	6m	1y	2yr	3yr
Gold	28.5	28.0	27.0	26.25	25.5	25.0
Silver	47.4	45.3	44	42	40.4	40.05
Platinum	27.35	27.9	27.5	26		
Palladium	43.6	45.75	46.1	46.1		

Forwards	1m	3m	6m	1y
Gold	5.34	5.48	5.60	5.72
Silver	3.75	2.85	2.45	1.40
Platinum	3.30	3.10	2.70	1.75
Palladium	5.31	5.32	5.34	5.36

US Equity Markets	Dow Jones	10973.56 / +0.45%	S&P 500	1246.00 / +0.55%	NASDAQ	2111.84 / +03.55%
Gold Equities / US Treasuries	XAU	131.60 / +0.02%	JGLDX	3004.98 / +0.26%	10 yr	5.25
Commodities	CRB	338.22	MCU3	6925	CLc1	72.47

Base Metals Data

Prices (\$/t)	28-Jun-06					Changes (\$/t)			Changes (%)			2006	
	Close	Open	High	Low	C-3's	1d	3m	1y	1d	3m	1y	High	Low
Copper	6,910	6,750	6,995	6,700	110b	160	1,595	3,555	2.4	30	106	8,800	4,330
Aluminium	2,483	2,480	2,512	2,470	43c	-7	-60	762	-0.3	-2	44	3,310	2,230
Nickel	20,405	19,900	20,550	19,900	875b	555	5,230	5,755	2.8	34	39	23,050	13,500
Zinc	2,950	2,920	3,010	2,870	31b	30	326	1,710	1.0	12	138	3,970	1,880
Lead	970	965	980	965	26c	5	-270	31	0.5	-22	3	1,435	925
Tin	7,940	7,850	7,975	7,900	90c	-10	-310	615	-0.1	-4	8	9,600	6,575

LME Stocks (t)	29-Jun-06						On Warrant				Cancelled Warrant		2006	
	Open	In	Out	Ending	1d chg	1y chg	tonnes	tonnes	1d chg	% of total	High	Low		
Copper	93,000	1,200	275	93,925	925	64,400	86,550	7,375	-275	7.9	134,725	92,225		
Aluminium	763,300	275	3,500	760,075	-3,225	233,925	697,150	62,925	-325	8.3	793,625	643,700		
Nickel	10,350	594	396	10,548	198	3,300	7,524	3,024	1,080	28.7	37,218	10,350		
Zinc	221,000	125	1,900	219,225	-1,775	-392,325	156,200	63,025	-1,000	28.7	393,550	219,225		
Lead	113,300	0	725	112,575	-725	70,525	107,275	5,300	-250	4.7	117,900	42,000		
Tin	11,915	0	25	11,890	-25	7,915	11,435	455	10	3.8	17,100	11,890		
Aluminium Alloy	54,280	840	0	55,120	840	10,160	54,400	720	0	1.3	53,420	32,640		
NASAAC	121,000	0	80	120,920	-80	8,860	120,260	660	-180	0.5	135,400	120,920		

Implied Volatilities	1m	3m	6m	1y	3y	5y
Copper	48.00	45.00	47.75	44.50	36.25	34.25
Aluminium	26.50	26.75	27.00	25.00	24.00	22.75
Nickel	52.00	50.75	49.00	43.75	n/a	n/a
Zinc	53.00	53.50	51.75	45.50	n/a	n/a

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