# Downside looks limited: Copper

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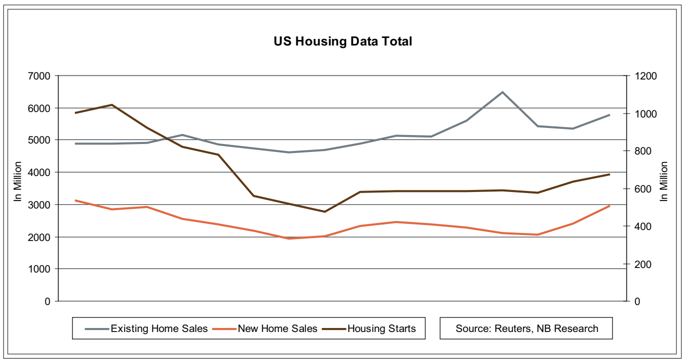
Till date we have witnessed about 25% correction in the prices of copper. The ongoing European debt crisis and the monetary tightening stance by China are two main factors that have led to the recent slump in the prices of metals. The question to be asked is whether the slump is overdone or if still some room is left for the down trend to continue?"

In this short-term report we will try to figure out the outlook for copper based on a few macroeconomic factors which are expected to take guard in determining the prices of copper.

## US Housing Market Scenario

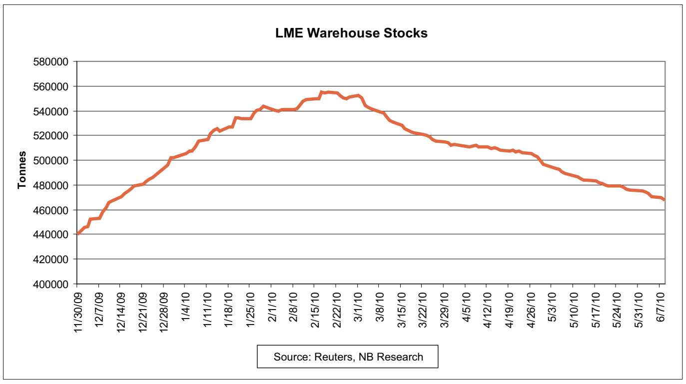
United States of America is one of the major copper-consuming countries with an estimated total annual consumption of around 10-11 percent of the world consumption. Copper is a prominent metal used for construction and housing purposes. About 35% of copper is used in this sector. Hence, any major development in the US housing market is expected to have a direct effect on the prices of copper.



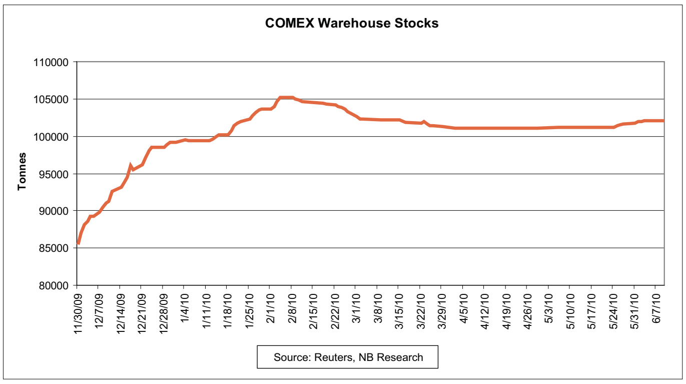

Since the end of 2009, the housing sector in US seems to be in a gradual up trend. The new home sales figures in the US increased by 30%, existing home sales figures surged higher by 5% and Housing Starts data edged higher by around 15% from the December 2009 levels. Construction spending reveals an expansion of 3% in the latest data released by the US officials. The housing market managed to rebound from its worst slump since the Great Depression, not forgetting that this sector was a major factor that triggered recession in the US and throughout the world. Though the recent data released from this sector inched downwards but this sector shows signs of stabilizing.

This phenomenon is sidelined by the recent drop in prices of copper due to the crisis in the euro zone and monetary tightening practice by China. We expect demand to further pick up as the US housing sector is in a boom at this point of time. Hence, for a short-term perspective this factor will lend some support to copper prices.

## Warehouse Stocks (SHFE, LME, COMEX)








Copper warehouse stock levels at all the three exchanges show a similar curve. Copper warehouse stocks are seen in a downtrend since the start of the year on the LME. They have also started declining in Shanghai and COMEX warehouses. Warehouse stocks are a good indicator of the physical offtake of the metal. This means that the spot demand of the metal is picking up day by day. The LME stocks have declined 7% since the start of the year 2010. It is the same with stocks reported by other exchanges. Shanghai warehouse stocks have declined by 17% from its recent high level of stocks. Though a recent correlation between the level of warehouse stocks and copper prices indicates a similar curve, the continuous decline in warehouse stocks across the globe is an indicator that there is still robust demand for copper in the world. Once the market feels free from the economic worries of the Euro zone and Chinese economy begins to stabilize, we could again a historical negative correlation between the two and this phenomenon could be a very supportive factor for the prices of copper in near term.

### Treatment Charges/ Refining Charges Rates

TC/RCs are the fees paid to smelters by mines and traders to refine copper concentrates into metal and are a key part of the global copper smelting industry's income.

According to a senior executive of the US copper mining and smelting group Freeport – McMoRan copper and gold global spot copper concentrate treatment and refining charges (TC/RCs) are likely to stay low in 2010 and beyond. Currently the smelter capacity is larger than concentrate output, forcing smelters to compete heavily for available concentrate supplies. The shortfall in concentrates is expected to continue through 2012 and beyond as planned smelter expansion outpaces new mine developments.

The treatment charges/ refining charges dropped to abound $10 a tonne and 10 cents per pound in February. Now speculation that spot TC/RC rates would be seen in single digits is growing. Expectations are that the spot TC/RC rates would drop to $5 per tonne and 5 cents per pound due to the lack of adequate concentrate supplies from mines. According to latest estimates by ICSG, aggregated production in two leading copper mine producers, Chile and Peru, remained steady as a small increase in Chile offset a minor decline in Peru. Mine production capacity utilization in February 2010 was just over 77%, an increase from the January level but a slight decrease from February 2009 level and much below the levels seen in 2004-2005.

This phenomenon represents a situation where copper concentrate supplies from mines are not proving to be adequate enough to meet smelter requirements, as even supply from scrap remains low. According to a mining official in Chile, the copper concentrate market is expected to remain in a deficit of 5,00,000 to 1 million tonnes for this year. He also emphasized that the supply of concentrate would remain tight for the next three years or even longer. This factor is likely to lend support to prices of copper.

### The Road Ahead

On account of debt crisis in Europe and possible slowdown in China were the main reason for copper prices to crash from Rs.355/kg to 285/kg and since then we have seen marginal bounce back in the price. Going forward we may see copper prices may inch up in short term as negative news from Europe and China are already priced in after the kind of correction we have seen in copper, carpet of liquidity continue to cover negative news flows in global economy, despite of the fact there is debt crisis in Europe the bond auctions of have remain strong, inventories at LME Warehouse has been declining along with rising cancelled warrants indicating good demand for road ahead and though in the month of May we have seen drop in China's copper imports by 9% but its still remains high despite of cooling measure taken by their government. Structural problems in western world are not solved but we believe at least for the short term markets have factored them in and our outlook on red metals remains bullish for the targets of 307-310 on MCX and $ 6750-6800 on LME.