

# LME Outlook

September 2009

New York Industrial Metals Desk (24 hours): 1-212-589-6439  
London Industrial Metals Desk (24 hours): +44 (0) 20 71445885  
www.mfglobalmetals.com

Written by Edward Meir; Direct +1-203-656-1143, emeir@mfglobal.com



## Macro and General Overview:

When we last penned our thoughts on a longer-term metals outlook back in January, we could not imagine prices would recover as strongly as they have. Indeed, the free-fall global economies found themselves in during the end of 2008 and at the beginning of 2009 suggested that any recovery in metals would be anemic at best, and take much of 2009, if not longer, to take root. Instead, only eight months later, base metals have not only regained their footing, but prices have doubled, and in some cases, tripled from their January lows.

What has made this rebound all the more incredible, is that it is occurring amid a recessionary economic landscape, which although now ending, is still fraught with considerable uncertainty. Moreover, despite the recent pick up we have seen in metals demand, we have not seen any corresponding drawdown in LME inventories, even over the last two months when signs of recovery have been most prominent. In fact, of the six base metals covered in this report, only copper has shown a year-over-year inventory decline; the rest have seen their inventories increase over the course of a year. Next year hardly looks any better, in that despite an anticipated pickup in growth, four of the six base metals will end up with modest surpluses in 2010, meaning that stocks will continue to rise.

However, there are several unique undercurrents at work in the world economic picture that make this “boom and bust” cycle very different from what we have seen in the past. For one thing, this year’s price surge in metals amid a challenging economic environment, tells us, if nothing else, how deceptive -- even dangerous-- it can be to rely solely on supply/demand balances to get a sense of what is going on. Instead, markets seem to reacting more to other variables and only by addressing these can we hope to get a sense of where prices are going.

The first question that needs to be explored has to do with just what kind of global economic recovery we can expect. Judging from the way the markets have been reacting over the last several months, investors seem to be discounting a “V”-shaped recovery in the US and around the world. Under this scenario, the world’s “economic juices” will basically start flowing again, as global stimulus money kick-starts demand, credit begins to ease, companies rebuild depleted inventories leading to more production and jobs, consumers start spending, and the whole cycle resurrects itself, with metal prices moving steadily higher in the process - as they have. Proponents of this argument will be point out that China-- having weathered the recession in better shape than most-- will play a key role in ramping up growth.

There are a number of problems we see with this argument, and indeed, on closer examination, the odds are high that the V-shaped recovery markets seem to be expecting will likely flatten out going forward. Here in the US, the consumer is very cautious, traumatized both by imploding equity and housing prices, as well as legitimate fears about losing employment. In fact, the average US worker has a right to worry, as it is hard to see which sectors of the US economy are going to create the jobs of the future. In the mid-1980’s, jobs were partly created when the economy saw interest rates drop from 20% to 6%, as inflation was finally wrung out the system, while US corporations made impressive gains in increasing efficiencies. In the mid-1990’s, the technology and internet revolution spawned a whole new industry, boosted productivity, (thus keeping inflation low), and created millions of jobs in the process. In the 2000’s, low interest rates and easy credit triggered long-lasting booms in real estate, banking, and manufacturing. In each decade, recessions came and went, as one economic growth engine

*This report is issued by MF Global UK Limited (“MFG”) which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658*

replaced another. Many of these growth drivers are not as prominent now, and are either played out, (interest rates are close to 0, and technology has matured), or are flat on their backs, (as is the case for housing, banking, and to a lesser extent, manufacturing). With “green jobs” still many years off--if they are indeed to materialize at all-- it is hard to see which sector in the US economy (apart from health care) will be generating enough growth to make up for the close to 7 million jobs that have vaporized since the recession began in late 2007.

Skeptics will argue that China is the next economic “driver”, and in case of metals, this is somewhat true, as the country consumes a progressively greater share of the world’s metals output. Indeed, Chinese growth rates are expected to be in the 8-9% range this year, fueled by a \$580 billion stimulus package that is currently working its way through the economy. Unlike the stimulus spending here in the US, much of China’s spending is front-loaded, and because of this, the economy has already started to respond. Industrial production was up 11% through to the end of July, second-quarter GDP came in at 7.9%, electricity production reversed months of declines, and was up 5.2% in July, while car sales are booming, up 90% year-over-year. In addition, China’s rebound is pulling many Asian economies up along with it, with good second-quarter growth recently noted in South Korea, Singapore, Taiwan, Japan, and Indonesia. In fact, emerging Asian economies should grow by about 5% this year on average, while the G7 economies will contract by 3 ½%.

And yet, there are problems with the Chinese “locomotive” theory. For one thing, the current boom is heavily government reliant, so much so that the World Bank calculates government spending is driving an astounding four-fifths of the current expansion. Secondly, the Chinese export sector, which account for roughly 36% of the country’s GDP and which generated millions of jobs in the past is struggling, given that China’s main trading partners have yet to fully recover. Most importantly, Chinese consumers are unlikely replace to replace American ones as the predominant world economic engine any time soon; Chinese private consumption is only one-third the size of the US’s, with Asian consumption only two-fifth’s as large.

Partly in response to these factors, the Chinese government is growing the “fixed asset investment” side of the economy, as it embarks on massive infrastructure projects. In the past, growing this sector created immediate demand, but it also resulted in overcapacity in the country’s manufacturing base. Much of this excess was masked when external demand was booming, but was left badly exposed when exports slowed dramatically over the past two years. The government has been moving to make up for the export deficit by stoking local demand instead, and has sanctioned banks to lend a record \$1.1 trillion of new loans in the first half of the year in an effort to support mostly government projects. However, some of this money is moving into speculative sectors, turning into waste, and creating pockets of froth in markets like Chinese stocks and properties. As a result, there has been some backpedaling of late, with the government now requiring the nation’s lenders to raise reserve requirements, while urging them to ensure loans go to projects that “support the real economy”. Recently, the government also announced production “curbs” on certain industries, including steel and cement. In the broader picture, the Chinese government finds itself very much in the same bind the Federal Reserve is in, namely, at what point should it start to rein in the money supply so that inflation and overheating are to be avoided. For the moment, as long as there is excess capacity in manufacturing and labor, (and a crisis in the credit markets), both countries are content to flood their economies with money. And both are also busy spending money on the fiscal side in order to get growth -- and jobs-- back on track.

Our macro assessment outlined above suggests that the global recovery will be uneven, government-reliant, and prone to periodic setbacks, making it unlikely that the V-shaped bounce will last with the initial vigor it has displayed so far. The logical inference to draw from this would be to view the sharp advance in metals prices with a great deal of skepticism, and perhaps sell into the rallies. However, we would be reluctant to draw such

This report is issued by MF Global UK Limited (“MFG”) which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

a conclusion, as there are two other important variables that could override our macro forecast. The first has to do with investors bidding up commodities as an inflation hedge, particularly given the massive deficit spending going on in the US, now estimated to be a whopping \$9 trillion over the next decade. As a percentage of GDP, the US national debt is also approaching alarming proportions, now close to 70%. (If it is any comfort, we are still below the 100% debt-to-GDP ratio reached during World War II). The stage is set for both a significant erosion in the dollar and substantial inflation in the out-years, likely some 2-3 years away (although the fact that gold is on the verge of breaking away from \$1000 resistance suggests many investors are not planning to even wait that long). We believe the market's heightened sensitivity to inflation will act as an important prop over the course of 2010, and will help keep protracted sell-offs in check.

A second variable that should keep metal prices supported has to do with the likelihood that the Chinese will continue to steer their cash, (some \$2 trillion and counting), into commodity investments as a diversification away from the dollar. China could even become a de facto global buffer stock manager for the various LME metals, accumulating large tonnages of metal whether it needs to or not. Earlier this year, the government said it would buy 1,000,000 tons of aluminum, 600,000 tons of lead, and 400,000 tons of copper and zinc each over the next three years, (with the copper purchases separate from the 300,000 tons it had already purchased for the SRB). These moves, in effect, extended a lifeline to local producers by artificially raising prices, and improved the quality of the loans extended to them. A few months later, the government said that it had decided to step back from further purchases, and provided a tally of what it had accumulated so far: 235,000 tons of copper was purchased, as was 590,000 tons of primary aluminum and 159,000 tons of refined zinc. Interestingly, the markets did *not* sell off on this announcement, and instead, metal prices pushed steadily higher. This may be due somewhat to fortuitous timing, as the Chinese buying program ended just as the global economic recovery got underway. However, it also tells us that investors sense China's market presence, and may likely not want to get caught short ahead of another buying program.

To summarize, a few thoughts:

1) The global economic recession seems to be over, as most western economies will likely report positive GDP numbers during the current quarter joining the Asian economies, all of which are currently growing. (See our table below). The recent bounce we are seeing in metals has to do with the markets discounting the end of the recession, (correctly in our view), and also, a V-shaped bounce going forward (incorrectly in our view). We believe that the global recovery will not be V-shaped, but possibly U-shaped or W-shaped, as we do not see the

### Industrial Production History and Forecasts

% Change Y-o-Y	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009f</u>	<u>2010F</u>	<u>2011F</u>
Europe	1.5%	4.2%	0.9%	-2.0%	-11.0%	3.0%	2.0%
Japan	1.5%	4.5%	1.2%	-3.4%	-15.0%	5.0%	3.5%
China	16.0%	16.7%	17.2%	12.3%	8.5%	11.0%	10.0%
USA	3.2%	4.1%	0.1%	-2.2%	-8.5%	2.0%	2.5%
Latin America	4.5%	4.2%	6.8%	3.7%	-3.5%	3.0%	4.0%
<b>Total World</b>	<b>3.6%</b>	<b>4.8%</b>	<b>2.3%</b>	<b>2.4%</b>	<b>-5.8%</b>	<b>3.0%</b>	<b>4.0%</b>

Sources: Official Data/F is MF Global Estimate

This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

beleaguered US consumer coming out swinging anytime soon. Out of China, the government has made a valiant attempt to promote growth, which by most accounts needs to be north of 8% just to accommodate the natural rate of job entrants into the labor pool. However, with the export sector still struggling and the authorities reluctant to let the yuan appreciate significantly, we do not see the Chinese consumer having the financial muscle to replace the traditional role played by the American consumer. Moreover, the government has to be careful that the flood of the liquidity it has unleashed does not backfire, as already there have been reports of waste and highly speculative loans. In addition, rising social tensions are on the rise, caused in part by unemployment and pollution concerns, the latter being a variable we feel has the potential to seriously threaten the Chinese economy.

2) Our guarded macro outlook does not necessarily mean that we are bearish on metals going into 2010, as the current crisis-- just by the sheer magnitude of the fiscal and monetary response-- has the potential to seriously devalue the dollar and lead to a bout of inflation down the road. We think the Chinese are well aware of this, which is why there are positioning themselves into commodity investments, and will likely be an ongoing buyer of metals, particularly on setbacks.

3) With respect to the individual metals, we discuss their outlook in the report that follows, but given what prices have done so far, we do expect a modest pullback over the September-October time period, seasonally a somewhat shaky period for most markets. Looking further out into 2010, we doubt the January 2009 lows will be retested any time over the next 15 months, but having said that, neither do we expect the mid-2008 highs to be reached either. Demand should be steady, if not spectacular over 2010, keeping trading ranges somewhat on the elevated side. In addition, supply constraints should manifest themselves with more regularity as labor unions will be more prone to strike given the sharp rebound in prices. Most importantly, the brief but sharp price correction we saw in most LME metals earlier this year resulted in badly needed expansion plans being postponed or canceled outright, and we are not sure producers will rush to restart them as quickly. A recent study by PricewaterhouseCoopers showed that in the first quarter of 2009 for example, 14 of the top 40 mining companies announced mine closures, production cuts or prolonged maintenance programs at mines. In addition, \$13 billion of capital expenditure has been deferred or canceled.

4) Finally, hedge fund money is down, but certainly not out. A study by Hedge Fund Research estimates that \$142.5bn has been allocated to funds in the second quarter, one of the industry's biggest inflows to date. Better returns have been instrumental in drawing money in, with the average strategy returning around 9% year-to-date and some strategies even delivering gains of 30%. Current fund capital now stands at \$1.430bn, about 10% higher than the March trough, although well below the peak of \$1.930bn reached at the peak. All this means that "hot money", while whittled down from the 2007 highs, could still contribute to considerable volatility in metals.

**MF GLOBAL 2010 PRICE FORECASTS**

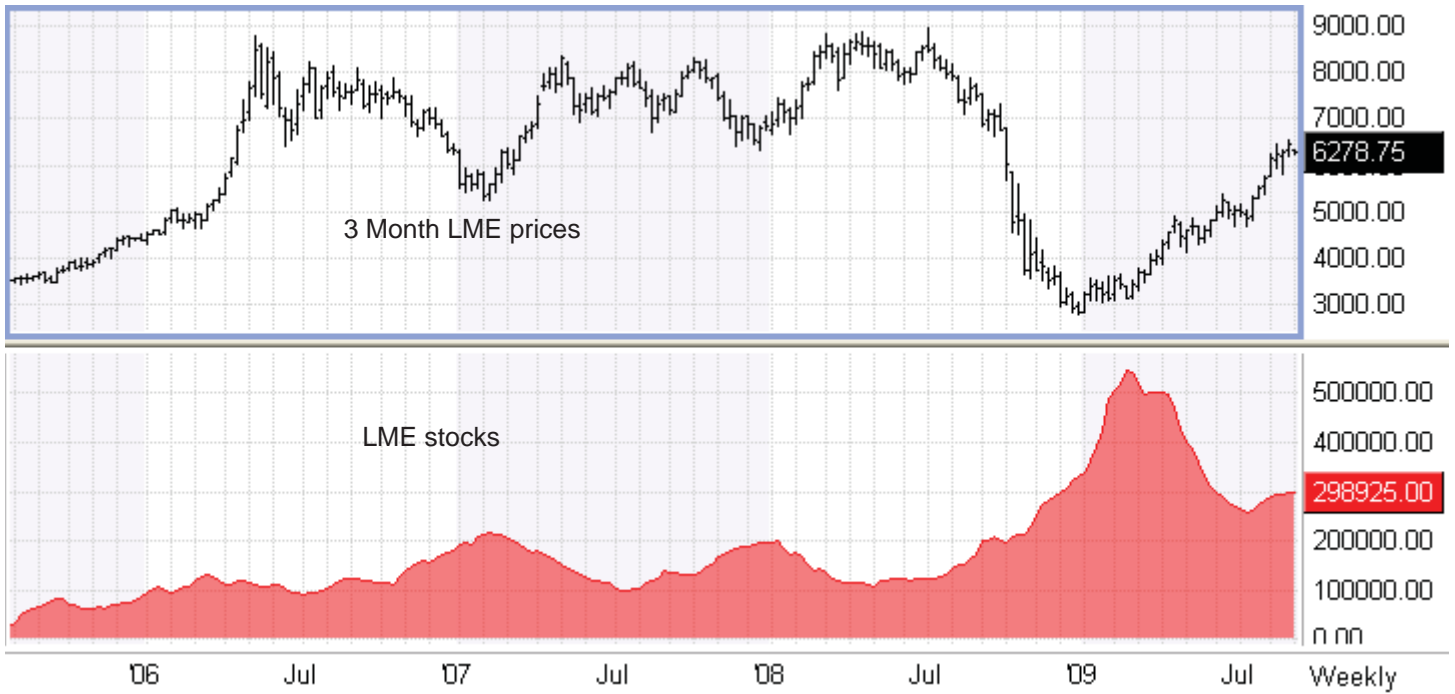
<b>Metal</b>	<b>2010 High Forecast</b>	<b>2010 Low Forecast</b>	<b>Average</b>
Copper	\$7,750	\$4,950	\$5,900
Aluminum	\$2,750	\$1,400	\$1,850
Zinc	\$2,600	\$1,380	\$2,050
Nickel	\$30,000	\$14,000	\$22,500
Lead	\$3,500	\$1,800	\$2,650
Tin	\$22,500	\$15,000	\$18,000

*This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658*

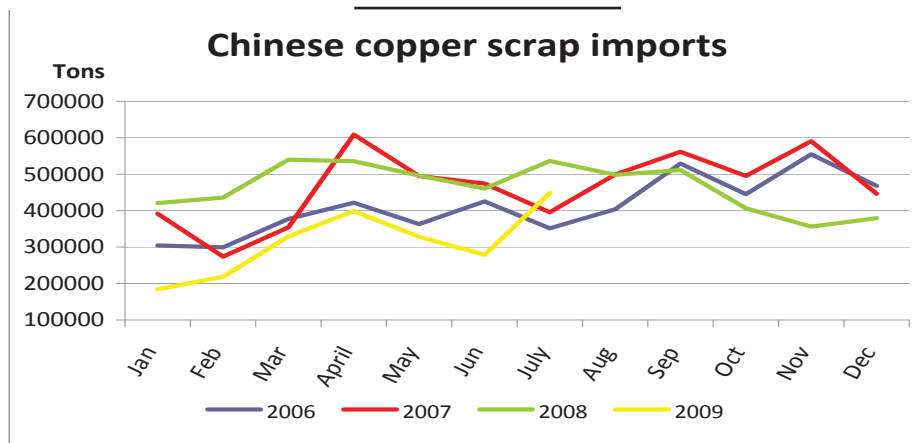
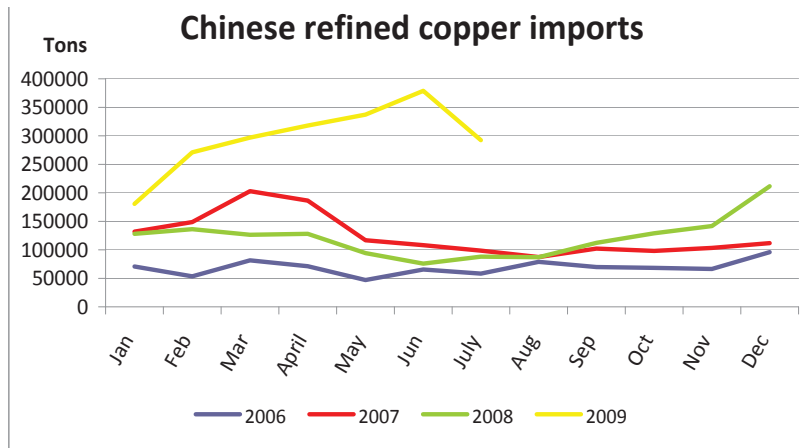
**Copper:** Copper is trading at a fresh 2009 high of \$6500 after plunging to a low of nearly \$3000 earlier this year. Of the six base metals we follow, copper is only one where stock levels have been falling this year, (see chart below), and this is providing some resilience to the latest price advance. The LME stock decline has been brought about by copper's relatively constructive supply/demand balance, where the latest figures furnished by the International Copper Study Group through May of this year, (see page 7) show consumption exceeding production by 150,000 tons versus a deficit of 183,000 tons in the same period a year ago. In addition, the numbers show that both usage and supply, (again through May), are running at almost unchanged levels to what was seen at this time last year, a rather impressive accomplishment in the wake of the financial meltdown. Of course, much of this buoyancy, particularly on the consumption side, has to do with developments in China. In this regard, the ICSG noted that the 1.1% decrease noted in global consumption would have been far worse were it not for the 44% increase in Chinese usage that offset an 18% decrease in the remaining countries.

The surge in Chinese consumption is best reflected in the country's import data, where we see in our chart on the next page that refined copper imports have practically doubled over the course of the year, although July import levels have shown the first decrease this year-- down by 21% drop from June levels. Despite the recent declines on the refined side, copper scrap imports are setting 2009 records practically every month, and show no sign of slowing down. All this begs the related question of whether imports and consumption should be considered as one and the same. We suggest the answer is a partial no, since a good deal of metal imported thus far has been brought in at the behest of the government, either for its stockpiling program or for its ambitious stimulus-related infrastructure projects.

We should add that the drop in July refined imports was not entirely unexpected, as the government simply cannot keep buying metal for its own account without either the domestic manufacturing sector or the export sector stepping in to take up some of these units. In fact, Chinese research group Antaika estimates that as of early July, some 435,000 tons of surplus metal was in the system, with local and government demand taking up only about two-thirds of the 1.4 million tons imported through May. Others point to ever larger surpluses being accu-



This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658



Source for Data; Chinese government data as compiled by Reuters

mulated. Research from Sumitomo, for example, suggests that first-half 2009 imports may have exceeded local manufacturing demand by as much as 1.3 million tons. More of a risk, is if some of this metal is released back onto the markets, as the SRB sometimes is prone to do, but we suspect that having engineered such a rally, the Chinese government has the financial resources to stay the course and in effect, keep this metal in relatively strong hands, (or stored), until it disposes of it when market conditions are stronger.

The fact that China has taken so much copper off the market has also made a dent in LME global stockpiles, even though these inventories may have simply shifted to the “hidden stock” category. We note from our chart on the preceding page that from close to 550,000 tons in February, LME stocks have shrunk to 315,000 tons, equivalent to around 6 days worth of global consumption. This is an extremely low base from which to start the current restocking cycle now taking place in Western economies. According to one European producer, for example, copper stocks, have now apparently fallen to only one week’s supply, with about 66,000 tons of metal spread all over Western Europe.

On the supply side, world mine production grew by 2.2% (135,000 tons) in the first 5 months of 2009 compared with the same period of 2008 when operational problems reduced production. The recovery came mainly from Indonesia, where a sharp rebound offset production declines seen in Chile, China, and the US (off by -4.4%, -12%, and -3%, respectively).

This report is issued by MF Global UK Limited (“MFG”) which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

Looking ahead, things look fairly tight in terms of capacity. In this regard, the ICSG is now forecasting global mine capacity to grow at an average rate of just 3.8% over the next five years. Refining capacity is expected to grow at a faster 5.3%, but for the first four months of 2009, the pace has been lagging, as growth has been well off this mark, with both primary and secondary capacity basically flat versus last year. These production “choke points” are significant, in part because they have been lowered by the ICSG from already depressed levels. In addition, capacity utilization rates are now down to around 78% compared to average utilization of 87% over the past 5 years, suggesting that the copper complex will struggle to respond in providing more supply if demand recovers to more normal levels.

**Price Outlook:** We see a rebound in both refined consumption and production in 2010, but given the sub-par economic recovery we expect, the increases in both these categories over 2009 levels will be relatively modest (up roughly 2% in each case). If anything, production could be under somewhat more pressure given the fact that 2009 thus far has been surprisingly free of major disruptions, so the odds favor a less smoother ride next year. Moreover, with prices attaining the levels they have of late, we suspect that labor unions will be more likely to stage strikes in order to achieve wage goals. This suggests that the likelihood of our projected copper deficit of 100,000 tons for 2010 will likely grow somewhat larger, keeping prices fairly buoyant. Our price forecast through to the end of 2010 is for a trading range of between \$4950-\$7750, with an average forecast of \$5900 for next year. The higher part of the range will most likely be reached by the middle of next year, just before we see major central banks tightening again. In the shorter-term, and specifically over the fourth quarter, we see a modest retrenchment in the cards that could take values down to around \$5900, as we suspect the market has yet to discount a significant, but perhaps temporary, slowing in the rate of Chinese buying. In addition, traditional September/October equity-related jitters could also contribute to the selling.

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>Year-to-date to May 2009</u>	<u>2009F</u>	<u>2010F</u>
<b>World Refined Usage</b>	16,673	17,042	18,175	18,007	7,575	17,850	18,200
Yr-Over-Yr Ch	NA	2.2%	6.6%	-0.9%	-1.1%	-0.9%	2.0%
<b>Mine Production</b>	14,924	14,990	14,464	15,458	6,352	15,767	15,850
Yr-Over-Yr Ch	NA	0.44%	-3.51%	6.87%	2.10%	2.00%	0.53%
<b>Refined Production*</b>	16,573	17,295	17,944	18,245	7,425	17,750	18,050
Yr-Over-Yr Ch	NA	4.36%	3.75%	1.68%	-0.06%	-2.71%	1.7%
<b>Refined Balance</b>	-100	253	-231	238	-150	-100	-150
<b>Total Refined Stocks</b>	867	1131	1027	1164	1054	1064	914
<b>Weeks Use</b>	2.70	3.45	2.94	3.36	7.24	3.10	2.61

\* Primary & Secondary

Source: ICSG / F: MF Global Forecasts

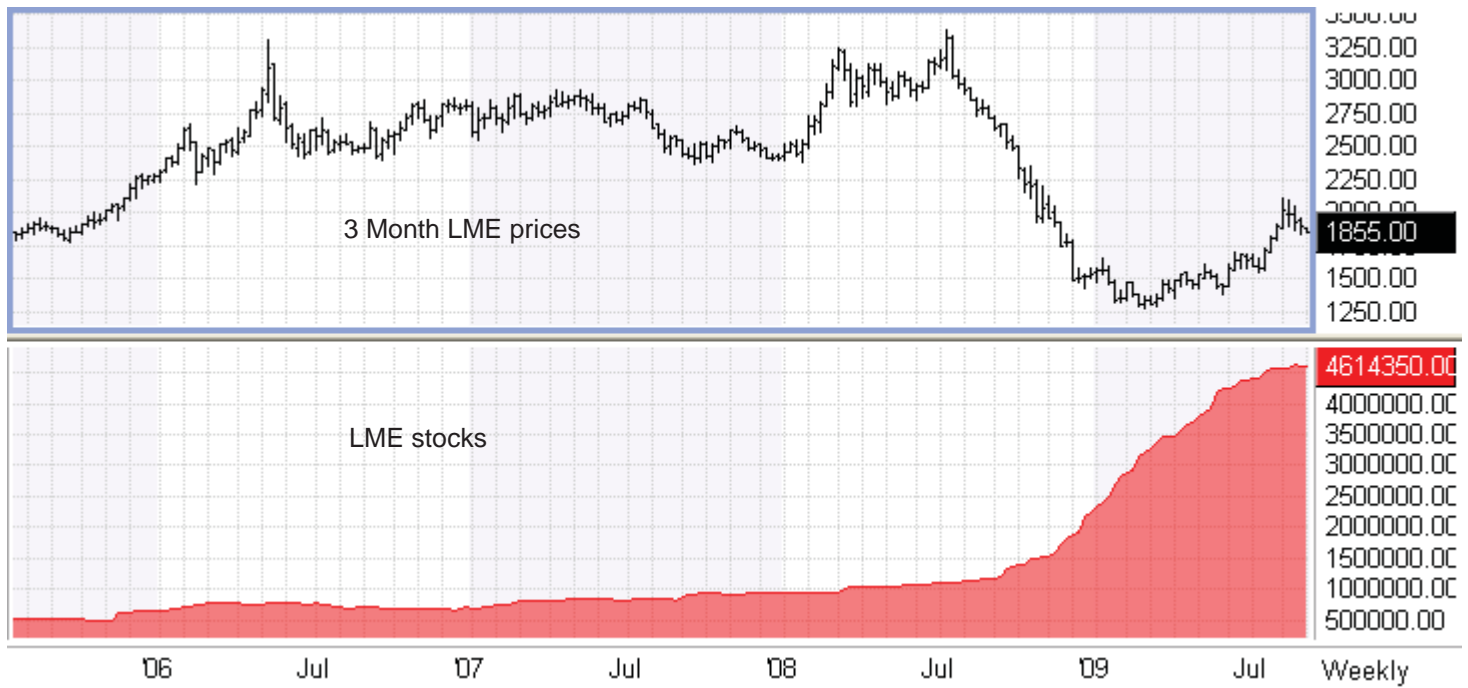
This report is issued by MF Global UK Limited (“MFG”) which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

**Aluminum:** Of all the base metals we follow, we think prospects for aluminum are the most challenging. Ever since collapsing from last year's high of \$3400, prices were in a virtual free-fall until they got to an intraday low of \$1285 in late February. Since then, the market has staged an impressive turn, reaching a high of \$2115 in early August, before fading somewhat shortly after that.

What is more stunning about this dramatic price rise, is the fact that it is occurring against a backdrop of steadily increasing stocks. On the LME for example, stocks have practically doubled this year from around 2.3 million tons to around 4.6 million tons, equivalent to about 12% of world consumption, and yet prices continue to rise. The most frequently cited explanation behind this disconnect lies with the notion that not all this inventory is "visible", locked up as it is in elaborate financing deals. While this may be true, locking up inventory is not the same thing as consuming it, and at some stage, much of this metal will have to come out. Here in the US, this could start to happen as Mid-West premiums (now around 5c, up by about 1c from earlier in the year), continue to rise, or as the forward contangos start to narrow (as they have been doing of late). Moreover, as flat prices rise, producers who were quite content to lock units up will now look to sell this metal outright to bolster badly strained balance sheets.

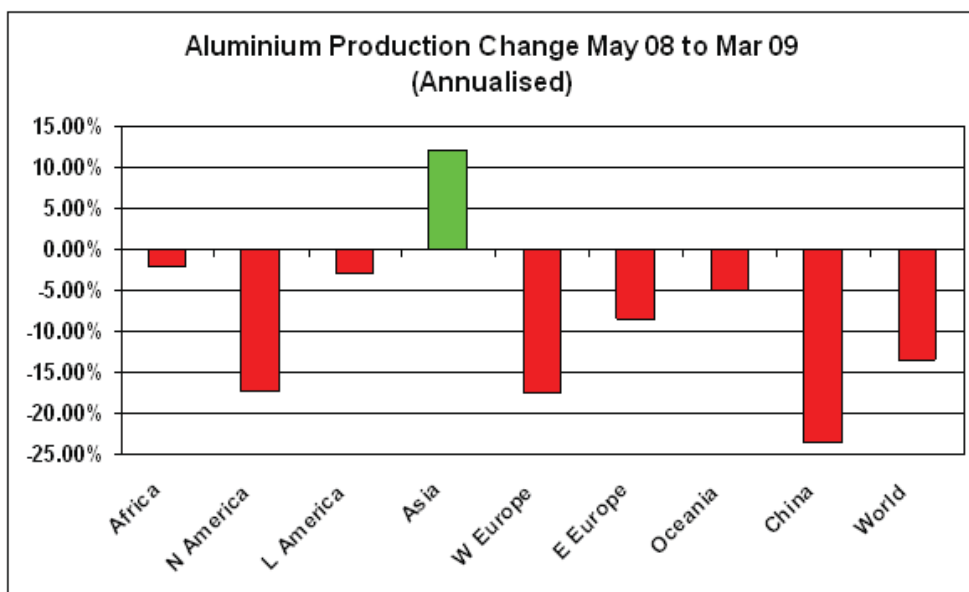
On the supply side, western producers announced some 3.1 million tons of production cuts at the start of 2009, and by and large, seem to have adhered to them. In fact, production numbers put out by the International Aluminum Institute show that total western production in July was 1.956 million tons, rising from 1.899 million in June, but off 11% off from July 2008 levels. However, these cuts were not enough to offset the sharp decline expected in 2009 demand, variously estimated to be off by anywhere between 5%-25%.

Chinese producers did announce some 3.5 million tons of cuts late last year and early this year, and seem to have adhered to them for a time, but recently, they too have restarted production. Roughly 1 million tons of capacity has reportedly been brought back online in recent months to accommodate the government's massive stockpiling and stimulus program, and the rest of China's additional capacity (estimated at some 3 millions tons)

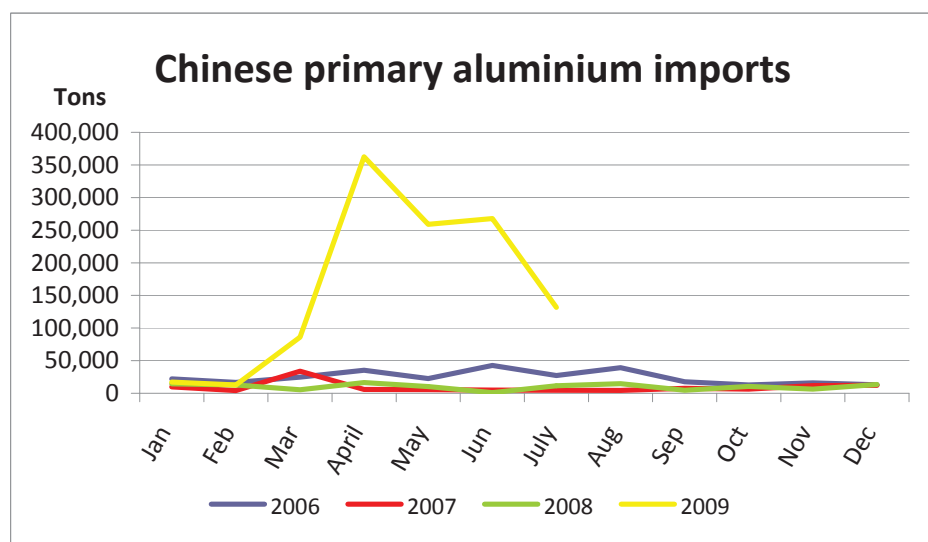


This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

is on standby. So far in 2009 and through to July, Chinese production was at 6.7 mln tons, down 12% from a year earlier, but up substantially from a decline of 22% seen at its peak in March (see our chart alongside). We expect this figure to draw down to the -8 to -10% range by the end of the year, as local industry continues to respond to the government’s stimulus and stockpiling program. Imports have already met a large part of the government’s demands, rising to just over 1.1 mln tons year to date through July, up a stunning 15-fold from the same period a year ago. (See chart below).



Russian production has also been an interesting area to focus on. By most accounts, the Russians are among the cheapest aluminum producers, so they have not been cutting back production as aggressively (likely around 10% year-on-year). Additionally, given how cash-strapped many of the Russian “oligarchs” are, it is conceivable that they would rather keep production going and turn the metal into quick cash by delivering it on to the LME as opposed to selling it into a depressed consumer market. Arguably, there has been some retrenchment recently in Russian production--more because of accident than design. In this regard,



reports surfaced in mid-August that about 500,000 tons of production was lost in the wake of the accident at a Siberian hydroelectric power station. Surprisingly, the markets did not push higher on this news, obviously displaying skepticism about the outage numbers. Moreover, RUSAL has apparently diverted energy supplies from other sources to keep their operations going. At this stage, it is too early to say how much of an impact this incident will have, although judging from the market’s reaction and the relatively modest amount of units involved, investors do not seem to be unduly concerned.

**Price Outlook:** We see demand finishing 2009 off 14.5% year-over-year. (For purposes of comparison, we should note that year to date figures through to May-June period furnished by the World Bureau of Mines and CRU has demand off by -12.7% and -18%, respectively, while Alcoa is on the other extreme, projecting only a 5% year-over year decline). We see supply exceeding the falloff in demand, dropping by only 8.3%, as a revival in Chinese pro-

This report is issued by MF Global UK Limited (“MFG”) which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

duction offsets the more aggressive Western declines. As a consequence, global stockpiles should increase by some 4,2 mln tons by the end of 2009 vs. 2008 levels. We already know that half of this stock increase has already accumulated on the LME, and we suspect the rest is being held by an assortment of Chinese producers on behalf of the government, in Chinese government warehouses, and among Western and Russian producers. With such a tremendous ramp-up seen in stockpiles, it is unlikely we will bend the aluminum supply/demand surplus curve anytime before late 2011, which is why we are forecasting another 2 mln ton surplus in 2010.

On the demand side, we are looking for a bounce of almost 10% in 2010, keeping in mind that this recovery is off an extremely depressed base. Production increases will be a much more modest 3%, as producers will likely be more than happy to work off their existing stockpiles.

Our price forecast for aluminum sees a maximum of \$2750 being reached between now and the end of 2010, while on the downside we would not be surprised to see a retest of the \$1400-\$1500 mark, with an average of \$1850 for the year. As a result, we believe currently elevated aluminum prices offer good opportunities to put on forwards sell hedges, but it is important that any hedging program be implemented on a wide enough scale so as to avoid clustering at any one level.

#### Refined Aluminum Supply/Demand Annual Balance

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>Year to Date to May 2009</u>	<u>2009F</u>	<u>2010F</u>
<b>Consumption</b>	31,720	34,025	37,578	37,769	13,905	32,300	35,500
Yr-Over-Yr Ch	NA	7.3%	10.4%	0.5%	-12.7%	-14.5%	9.9%
<b>Refined Production</b>	32,016	33,971	38,111	39,831	14,617	36,500	37,500
Yr-Over-Yr Ch	NA	6.11%	12.19%	4.51%	-11.90%	-8.36%	2.7%
<b>Apparent Balance</b>	296	-54	533	2,062	712	4,200	2,000
<b>Total Stocks</b>	3009	2764	2961	4672	6105	8872	10,872
<b>Of Which Held By..</b>							
<b>Producer/Consumers</b>	1797	1621	1554	1676	1409	NA	
<b>Exchange</b>	753	744	1043	2553	4462	NA	
<b>Weeks Use</b>	4.93	4.22	4.10	6.43	NA	14.28	15.93

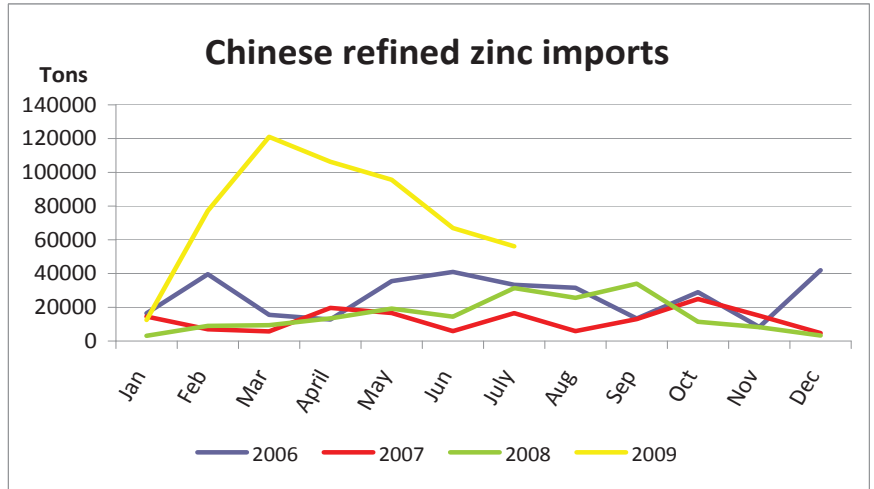
Source: WBM

F: MF Global Forecasts

This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

**Zinc:** After bottoming out close to \$1000 a ton in late 2008, zinc prices have risen substantially this year, hitting a 2009 high of \$2105 as we went to press. The advance has been taking place despite a backdrop of steadily increasing stocks, as Chinese government buying has more than offset growing supply surpluses. Also helpful, was the fact that even before last year's financial meltdown, zinc producers were among the first to cut back on capacity, therefore preventing the complex from being burdened with even more inventories.

No analysis of the base metals complex is complete without examining the role of Chinese buying, and zinc is no exception. China imported 535,000 tons of refined zinc metal in the January-July 2009 period, substantially more than other period in the past five years (See our chart alongside). One would have thought that this level of buying would have made a dent in overall stock levels, but on the contrary, stocks have moved sharply higher on the LME over the last few months, (see chart below), and have also almost doubled since April on the Shanghai exchange.



This suggests that despite the Chinese government's best efforts to jump-start demand, zinc metal units have not been entirely taken up by end-users, and much of the metal is sitting either in warehouses or is in speculative hands. China is not helping the market move towards balance either, as the government has been getting local producers to *step up* production. In this respect, latest Chinese data shows that July zinc production was up 12% year-on-year, running at 2.27 million tons year-to-date. In fact, Chinese research group Antaika projects that zinc production will reach an all-time record in the third quarter of this year, and for the year as a whole, the group expects zinc production to rise to a whopping 4.2



This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

million tons vs. estimated demand, which we think will come in around 3.9 millions tons. On a global basis, the International Lead and Zinc Study Group sees the market in surplus by 273,000 tons in the first half of 2009. Global refined zinc use is projected at 5.079 million tons, down from 5.737 million a year earlier. Zinc output was 5.352 million tons, down from 5.858 million a year earlier, while June producer stocks are expected to rise to 404,000 tons from 398,000 tons in May, and above the 366,000 tons seen last year. (See our table on the next page).

As we watch developments in China, other producers are restarting production in the meantime. In this respect, Kazakhmys has reopened its 100,000-ton Balkhas smelter and Boliden has said it will likely boost production at its 315,000 ton smelter in Finland and at a 162,000 ton smelter in Norway, adding that the increase in production “can be done profitably despite the continued weakness in the market”. Teck Resources also said in August that it would resume full production at its Trail zinc smelter, raising output by a modest 25,000 tons a month effective Sept. 1st from the current 20,000 tons a month. Lastly, Votorantim said it would bring on 150,000 tons of additional smelting capacity, while producers in India and Peru are also looking to increase output.

Things are somewhat tighter on the mining side; in its spring 2009 forecasts, the ILZSG noted that mine production is expected to fall at a faster pace (6%) than refined production (4%) reflecting the closure of marginal facilities and deferral of new projects. This could leave the concentrate market in a small deficit in the order of some 100,000 tons. However, we suspect that this too could change, particularly if producers restart operations.

On the demand side, it remains to be seen how things shape up going into next year. If our scenario on the macro picture is correct, demand increases will be modest at best, and likely not enough to absorb the extra production coming on stream, particularly on the Chinese side. In fact, the Chinese local market is now struggling to absorb extra units, and physical premiums are said to be under pressure, perhaps explaining why we have seen a dip in the latest refined zinc import tally, which was off some 30% from June levels. In the US, zinc premiums are between 3-5c, with a 1-1.5c increase noted in recent weeks, but demand has been spotty depending on which sectors of the economy one is talking about. Zinc demand from the steel mills has been the strongest, as many mills were destocking substantially earlier this year, and have now stepped up their buying. In addition, an uptick in car sales due to the recently concluded “cash for clunkers” program is also feeding through into the demand chain, but we suspect that much of these “new” sales will likely replace future ones. The US die-casting business remains poor, no doubt dragged down by the sorry state of affairs in the housing market, which despite a recent uptick in home sales, has a long way to go before it recovers.

**Price Outlook:** Our general take on a zinc market is one that seems comfortably supplied, but where demand will not be that strong. We likely will end 2009 with a substantial surplus in the order of some 400,000 tons, and a surplus will still be with us next year, although the number could fall to about 150,000 tons. These back-to-back increases should bring overall global stocks to 1,270,000 tons by the end of 2010, equivalent to about six weeks of consumption. This is not exactly a backdrop for runaway prices going, and we suspect zinc will have trouble breaking above the \$2600 mark over the next 15 months. On the downside, we see prices dipping to \$1380 during this period, likely by early next year, as the apparent Chinese retrenchment from the import market sinks in. However, it should be noted that this trading range is still historically high, and will remain elevated given market perceptions that Chinese buying will likely not completely recede from the background. We are forecasting an average price of \$2050 for zinc for 2010.

---

This report is issued by MF Global UK Limited (“MFG”) which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

---

**Refined Zinc Supply/Demand Annual Balance**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>Year-to-date to June 2009</u>	<u>2009F</u>	<u>2010F</u>
<b>Consumption</b>	10,648	10,448	10,896	11,294	11,361	5,079	10,650	11,100
Yr-Over-Yr Ch	NA	-1.9%	4.3%	3.7%	0.6%	-11.4%	-6.3%	4.2%
<b>Mine Production</b>	9,709	10,055	10,421	11,096	12,098	5,312	11,200	11,500
Yr-Over-Yr Ch		3.56%	3.64%	6.48%	9.03%	-7.00%	-7.42%	2.20%
<b>Refined Production</b>	10,392	10,184	10,659	11,360	11,530	5,352	11,050	11,250
Yr-Over-Yr Ch	NA	-2.00%	4.66%	6.58%	1.50%	-8.60%	-4.16%	1.81%
<b>Apparent Balance</b>	-256	-264	-237	66	169	NA	400	150
<b>Total Stocks</b>	999	783	489	549	724	968	1,124	1,274
<b>Of Which Held By..</b>								
<b>Producers</b>	219	239	255	271	280	404	NA	NA
<b>Merchants</b>	17	19.3	15.6	16.5	16.6	17	NA	NA
<b>Consumers</b>	134	131	128	119	111.3	111	NA	NA
<b>Exchange</b>	628	393	90	143	316	360	NA	NA
<b>Weeks Use</b>	4.88	3.90	2.33	2.53	3.31	NA	5.49	5.97

Source: WBM/ILZSG

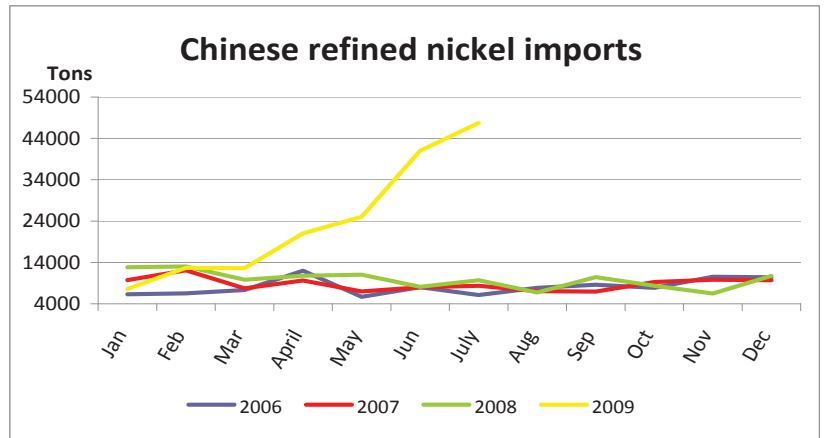
F: MF Global Forecasts

---

*This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658*

**Nickel:** Nickel is also very much a China story, as the country produces about a third of the world's stainless steel, while Asia as a whole soaks up almost half the world's nickel. In China's case, local mine production of both refined metal and concentrates, coupled with pig iron production, only supplies about 40% of the country's total nickel needs. The rest of the metal has to be imported, but as the spike in the chart below shows, the country's normal import requirements have been augmented by additional metal earmarked for the government's stockpiling program. Surprisingly, unlike copper and zinc, there has been no leveling off in the rate of Chinese nickel imports to date. In fact, our chart shows July imports rising to 47,000 tons, the highest reading for the year, and up sharply from the 25,000 tons seen in May. Year-to-date through July, nickel imports totaled 167,000 tons, up from 75,000 tons during the same period last year. Some Chinese traders expect imports to fall going forward, and there are reports that spot physical premiums are off by some 50% from mid-June levels, but none of this seems to be reflected in the import data just yet.

The Chinese government's decision to prime the nickel "import pump" has been fortuitous in that it has coincided with a natural rebound in stainless consumption after global output plunged to a nine-year low of 4.83 million tons in the first quarter of this year, virtually depleting producer inventories. In addition, the drop in stainless production earlier this year resulted in stainless scrap getting quite tight over the spring and summer month, thus prompting mills to pick up refined nickel units when they did come back into the market.



This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

Right now, stainless production is on an upswing practically around the world. Chinese stainless mills have raised production every month for the past six, with some even producing at full capacity. Stainless mills are also busy in Japan and South Korea, while here in the US, production has pushed up to around 60,000 tons per month, up from about 35,000 tons seen earlier this year. US operating capacity is around 50-60% versus 40% seen earlier. European producers are also restarting operations, with Outokumpu announcing the restart of its Torneo smelter in September, and Acerinox raising capacity to 60,000 tons per month (to 75% of capacity).

Of course, the across the across-the-board restarts we are seeing in stainless begs the question of whether producers are ramping up capacity to levels that could eventually exceed demand. One measure that is not painting a particularly positive scenario for nickel prices in this regard, is the fact that LME stocks have been rising steadily for most of the year, and now stand at about 110,000 tons, almost triple year-ago levels. One would have expected that with stainless production ramping up, nickel stocks would not be rising as dramatically, but they are. As a result, some producers are already retrenching, with Chinese June nickel production down 0.8% during June to 17,419 tons after a rise of 24.5% in May. However, the big production push put through earlier in China means that the local market is currently overstocked, with about 100,000 tons of nickel estimated to be stored in public and private warehouses, this according to state research firm Antaike. And more could feed the market going into 2010 as Vale expects to start commercial production from its Goro nickel project in New Caledonia by the end of this year.

Another variable that could sink the nickel run and which has done so before, is pig iron production. If nickel prices get too expensive, mills could turn to both low-grade and lower grade pig iron to for certain high-grade nickel. Already, we are seeing production ramping up, with nickel ores flooding into the country, up to 2.2 mln tons in July, three times last year's levels, although still about 20% off the 2007 highs.

**Price Outlook:** Overall, we are not that enthralled about nickel's prospects going forward, although in the short term, prices will very likely find support due to the work stoppage at Vale's Sudbury operation, which potentially could bring the company's entire Canadian nickel operations to a halt. However, assuming that the strike will eventually be settled, participants will be left looking at a market which is quite comfortably supplied. In this regard, and as our table on the next page shows, we expect to see total global stockpiles surpass 200,000 tons by the end of 2009, thanks mainly to the implosion in nickel demand seen this year. The World Bureau of Mines estimates that through May, refined nickel demand was off by a stunning 18% year-over-year, but we are assuming that a second-half pickup should pare this year-over-year decrease to -8%. Even with this bounce, the market will not avoid slipping into yet another surplus of about 65,000 tons by year-end 2009. The surplus will narrow somewhat next year to about 40,000 tons, as increased demand makes a dent in stockpiles, even accounting for Goro units. Nevertheless, with stocks forecast to be at the equivalent of about 10 weeks of world consumption during both this year and next, we see a potential high on nickel over the next 15 months of around \$30,000, likely on the back of a short-lived technical rally, with retrenchments taking prices down to \$14,000, and even perhaps slightly lower. Nickel prices should average \$22,500 for next year.

---

This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

---

**Nickel Supply/Demand Annual Balance**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>Year to Date to May 2009</u>	<u>2009F</u>	<u>2010F</u>
<b>Consumption</b>	NA	1,296	1,365	1,353	1,294	472	1,190	1,270
Yr-Over-Yr Ch	NA		5.3%	-0.9%	-4.4%	-18.5%	-8.0%	6.7%
<b>Mine Production</b>	NA	1,371	1,445	1,571	1,493	584	1,400	1,425
Yr-Over-Yr Ch	NA	NA	5.40%	8.72%	-4.96%	-4.80%	-6.23%	1.79%
<b>Refined Production</b>	NA	1,288	1,341	1,455	1,365	557	1,255	1,310
Yr-Over-Yr Ch	NA	NA	4.11%	8.50%	-6.19%	-2.60%	-8.1%	4.4%
<b>Apparent Balance</b>	NA	-8	-24	102	71	86	65	40
<b>Total Stocks</b>	98	112	87	125	154	143	219	259
<b>Of Which Held By..</b>								
<b>Merchants/Consumers</b>	77	76	80	77	76	33*	NA	NA
<b>Exchange</b>	21	36	6.6	48	79	109	NA	NA
<b>Weeks Use</b>	NA	4.49	3.31	4.80	6.19	NA	9.57	10.60

\* Through June

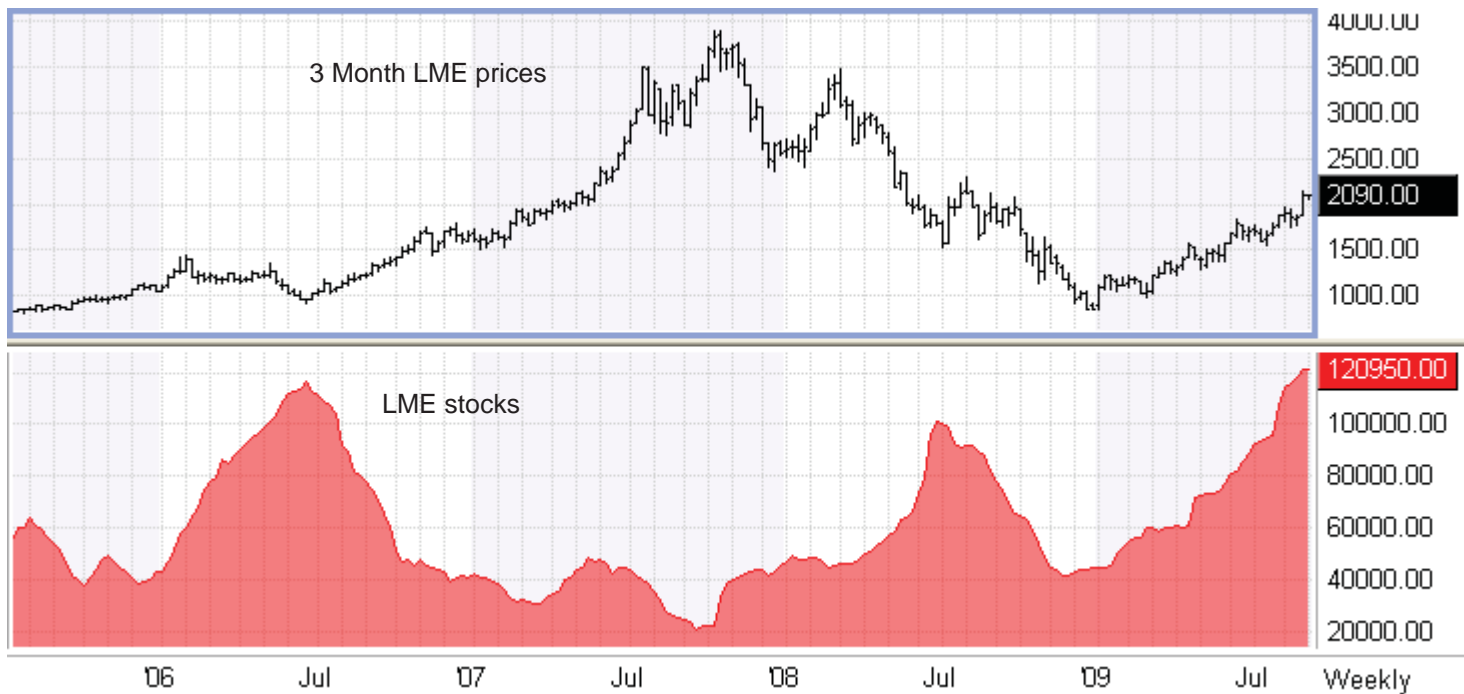
Source: WBM / F: MF Global Forecasts

*This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658*

**Lead:** Lead prices sank to \$850 a ton in December of 2008, but the market has not looked back since, and prices began a steady climb higher. In early September, prices hit a 2009 high of \$2505, with the advance sparked by news of a substantial outage in China, where as much as 240,000 tons of annual lead smelting capacity in Hunan province was shut down on reports of wide-spread poisoning. The closed capacity, which Chinese officials said could be phased out permanently, is nearly 6% of refined lead capacity, and there is talk that up to a third of the province's facilities could eventually be shut down. In fact, research group Antaika said that as much as 60% of China's lead plants do not meet national pollution standards, a big risk to supply for a country that produces more than a third of the world's lead.

Another spark behind the recent rally has been the fact that the US car industry has been saved from the brink of liquidation by massive government subsidies and reorganization efforts. The latest shot in the arm came from the recently terminated "cash for clunkers" program, which to everyone's surprise, helped catapult August sales to around 14 million units annualized after they crashed to just below 9 million earlier this year. Of course, it is now very likely future sales could fade in light of the program's termination, just as it usually does when incentive programs are over.

Of course, the most important variable behind the lead price rally has been the aggressive Chinese purchases of metal. During all of 2008, total Chinese intake of refined lead metal was just under 31,000 tons, with lead concentrates coming in at 1.4 million tons. This year, (through July) refined lead imports have soared more than four-fold to 139,000 tons, while concentrate imports in the same period are running 24% higher than in 2008. Local production has responded accordingly, with the Chinese producing 1.71 mln tons of refined lead in the first half of 2009, up 20% from the same period last year. Output of mined lead rose by 4.6% over the same period to hit 625,500 tons.



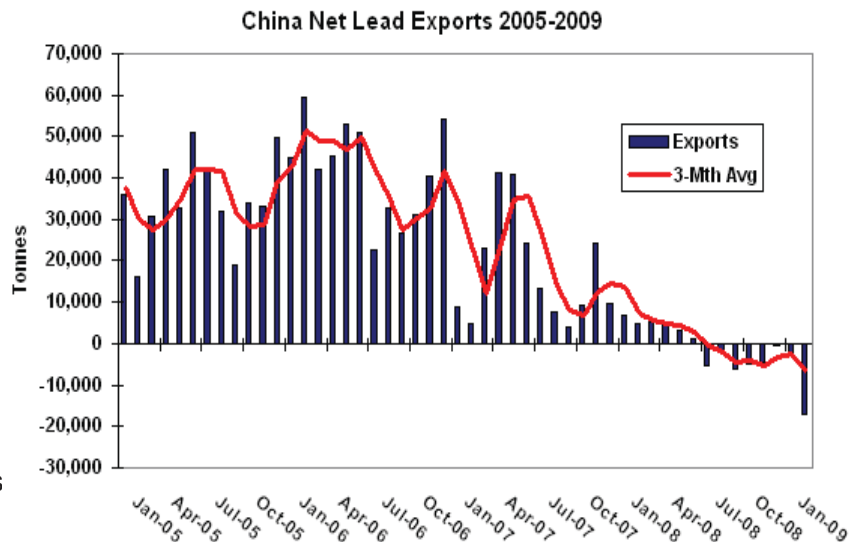
This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

Granted, some of this increase is attributable to the booming Chinese automobile market, but this growth cannot fully explain the tremendous supply increases seen. In fact, Chinese car sales have not always been moving along a straight line higher, and even stalled earlier this year until the government rolled out a series of incentive programs. Rather, the substantial increase we are seeing in imports, once again, has to do with the Chinese government's aggressive stockpiling program. Chinese research firm Antaie estimates that about 100,000 tons of refined lead is held by Chinese merchants who have been incentivized to purchase metal because of low interest loans offered by the government. This speculative tonnage is something of a double-edged sword, as the units could conceivably be put back onto the market on order to pay the loans back. There is less chance of that happening with units held by the government.

Despite the steady Chinese production gains, the International Lead and Zinc Study Group's latest monthly bulletin shows the market to be in surplus by a relatively modest 37,000 tons in the first six months of 2009. Global refined lead use was 4.204 million tons compared with 4.233 million a year earlier, as sharper consumption declines in Western Europe and the US were offset by higher Chinese and Asian demand. On the production side, refined lead output was 4.241 million tons, little changed from 4.232 million seen in the same period last year.

On the inventory side, the ILZSG sees western world commercial stocks at 335,000 tons at the end of May (or roughly 2 weeks of demand) compared with 306,000 tons at the end of last year. These numbers tell us that the lead market is not saddled with large inventories, and in fact, we do not see the 2009 surplus growing substantially from May levels given the production shortfalls at various facilities. In this regard, Doe Run Peru's setback is the most prominent, where output is off by 70%, with some 80,000 metric tons of metal taken off as a result. In addition, the recent stoppages in China's Hunan province could also pinch refined supplies, as it will take refining capacity off the market. On the plus side, Ivernia's Magellan subsidiary is back in the picture, and now able to commence exporting lead concentrate through the Port of Freemantle. Nevertheless, despite this renewed source of supply, China should continue to provide an underlying bid to the market given that they are now no longer an export powerhouse. (See chart alongside).

**Price Outlook:** Among the six base metals, lead looks to us to be the most tight in terms of its supply/demand balance. We note from our table on the next page that the market will likely finish 2009 with only a slight surplus, while for next year, we forecast a 30,000 ton deficit. Developments in both China and at Doe Run Peru will be key variables in influencing prices going forward, as these potential supply bottlenecks could push against improving demand prospects going into next year. In China's case, pollution related production shutdowns could also result in the Chinese picking up more refined ingots (presumably after working off their local stockpile). In the case of Doe Run, should the facility fail to get financing and close down, we could see lead prices gradually push towards \$3500 as we roll into 2010. On the downside, lead prices could conceivably fall below \$1800 in a major correction, but we would be looking at such levels as attractive buying opportunities. Prices should average around \$2650 during 2010.



This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

---

**Refined Lead Supply/Demand Balances**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>Year-to-date to June 2009</u>	<u>2009F</u>	<u>2010F</u>
<b>Consumption</b>	NA	7,766	8,050	8,363	8,703	4,204	8,530	8,650
Yr-Over-Yr Ch	NA	NA	3.7%	3.9%	4.1%	-0.7%	-2.0%	1.4%
<b>Refined Production</b>	NA	7,706	8,012	8,177	8,679	4,241	8,560	8,620
Yr-Over-Yr Ch	NA	NA	3.97%	2.06%	6.14%	0.00%	-1.37%	0.70%
<b>Apparent Balance</b>	NA	-60	-38	-186	-24	NA	30	-30
<b>Total Stocks</b>	269	269	280	281	307	335	337	305
<b>Of Which Held By..</b>								
<b>Producers</b>	96	107	108	97	114.4	112.2	NA	NA
<b>Merchants</b>	0.4	0.3	0.9	0.8	1.3	0.8	NA	NA
<b>Consumers</b>	132	118	130	138.5	146.2	152.1	NA	NA
<b>Exchange</b>	41	43.6	41.1	45.4	45.2	92	NA	NA
<b>Weeks Use</b>	NA	1.80	1.81	1.75	1.83	NA	2.05	1.83

Source: WBM/ILZSG /F: MF Global Forecasts

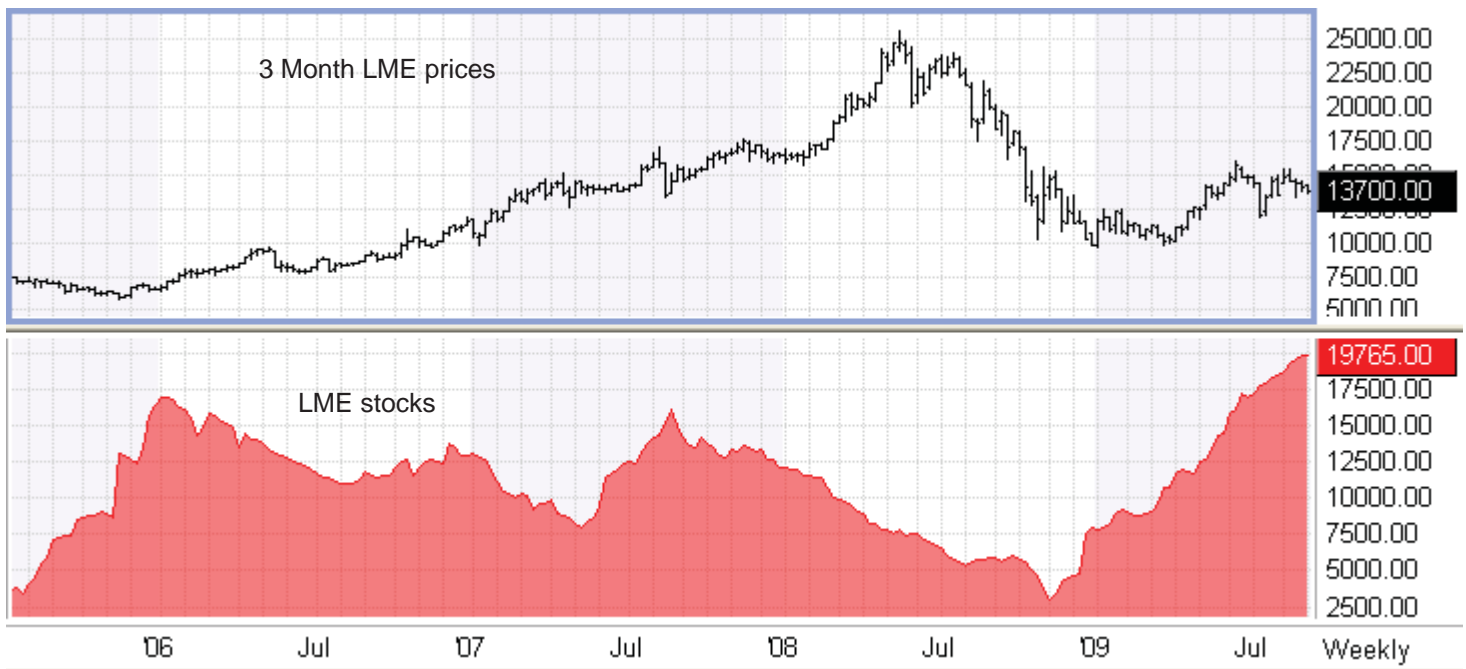
---

*This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658*

**Tin:** To a large extent, tin is marching to the beat of its own drummer. The complex has not shown the dramatic price rise that has characterized movements in many of the other metals this year, and in fact, is the only metal that has yet to hit fresh 2009 highs. We suspect the inability of the complex to “break out” has less to do with tin’s own fundamentals, (which, incidentally, are not overwhelmingly bearish), and more with the fact that tin has been noticeably left out of the Chinese buying program.

With regard to the complex’s fundamentals, LME tin stocks now stand at about 12,000 tons, quadrupling since hitting a November low of 3,000 tons. We attribute this increase mainly to the fact that the Indonesians have not cut production as drastically as they said they would, mindful of the hardships local miners are already enduring. Although latest estimates shows Indonesian production running at about 8,800 tons in July, down about 11% from July 2008 levels, the decrease is coming mainly from smaller operators who come under more scrutiny than their larger and more established counterparts. PT Timah, for example, (the world’s largest exporter), sees no decline in production and, in fact, raised its export target in mid-June to 50,000 tons from an original forecast of 46,000 tons.

**Price Outlook:** The International Tin Research Institute is anticipating a 2009 surplus of some 15,500 MT, and we forecast a slightly smaller surplus for next year in the order of 6,500 MT, as a rebound in consumption narrows the gap. We expect prices to range between \$12,000 to \$16,000 over the course of 2009, but with a smaller deficit expected next year, we see the trading band shift noticeably higher. In this regard, we could prices range between \$15,000-\$22,500, to average \$18,000 for the year. We think tin’s upward price bias has much to do with the fact that it lacks diversity in its production base. As production out of China, (now no longer a substantial exporter), continues to fall due to declining ore grades, tin is becoming overly dependent on Indonesian, and to a slightly lesser extent, Peruvian supply, with all the production and/or political problems that this dependency entails. Moreover, on the demand side, tin should continue to benefit from the gradual migration away from lead use in solder.



This report is issued by MF Global UK Limited (“MFG”) which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office: MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658

### Global Tin Supply/Demand Balance

('000 tonnes)	2005	2006	2007	2008	2009F	2010F
Production	346	354.7	345.8	325.5	325	321.5
DLA Sales	7.7	9.3	7.7	3.9	0	0
Consumption	331.8	364.6	355.5	337.5	310	315
Market Balance	21.9	-0.6	-2	-8.2	15	6.5
Reported stocks	36.5	33.5	32.4	30.6	44	40.5
Stock Ratio (weeks consumption)	5.5	4.8	4.7	4.7	7.4	6.6

Historical Data ITRI; F: MF Global Forecasts

*This report is issued by MF Global UK Limited ("MFG") which is authorised and regulated by the Financial Services Authority. The report was prepared and distributed by MFG for information purposes only. The report contains information and opinions, which may be used as the basis for trading undertaken by MFG and its officers, employees and associated companies. The report should not be construed as solicitation nor as offering advice for the purposes of the purchase or sale of any security, investment, or derivative. The information and opinions contained in the report were considered by MFG to be valid when issued. The report also contains information provided to MFG by third parties. The source of such information will usually be disclosed in the report. Whilst MFG has taken all reasonable steps to ensure this information is correct, MFG does not offer any warranty as to the accuracy or completeness of such information. Any person placing reliance on the report to undertake trading does so entirely at their own risk and MFG does not accept any liability as a result. Securities and derivatives markets may be subject to rapid and unexpected price movements and past performance is not necessarily a guide to future performance. Registered Office : MF Global UK Limited, Sugar Quay, Lower Thames Street, London, EC3R 6DU. Registered in England No. 1600658*