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European shares down sharply on disappointing Chinese data

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* FTSEurofirst 300 and Euro STOXX 50 drop more than 2 pct

* DAX down more than 4 pct as weak China data hits markets

* Ferrari outperforms car sector on Milan debut

* Euro STOXX 50 Volatility Index rises

LONDON/MILAN, Jan 4 (Reuters) - European shares fell sharply on Monday, the first trading day of 2016, as weak Chinese data weighed on world stock markets and a rebound in oil prices added to market volatility.

The pan-European FTSEurofirst 300 index lost 2.6 percent by 1535 GMT, its biggest one-day drop since a 3.3 percent decline on Dec. 3.

The euro zone's blue-chip Euro STOXX 50 index fell 3.3 percent and Germany's DAX slumped 4.2 percent.

China's factory activity contracted for the 10th straight month in December and the decline accelerated compared with November, a private survey showed.

China's benchmark CSI300 share index tumbling 7 percent on Monday, prompting the stock exchange to halt trading for the rest of the day.

"This year got off on the wrong foot because of China," said **ActivTrades chief market analyst Carlo Alberto De Casa.**

All sectors were in negative territory with auto stocks , for whom China is a key overseas market, leading the way with a fall of more than 4 percent.

But shares in Ferrari were little changed in their debut in Milan on Monday as the luxury sports car maker completed its spin-off from parent Fiat Chrysler. De Casa said the listing of such an important brand could be a good sign for Italy after many delistings.

Oil prices rebounded from previous lows, helping oil stocks outperform, as tensions escalated in the Middle East following Saudi Arabia's execution of a prominent Shi'ite cleric. Market volatility increased, with the Euro STOXX 50 Volatility Index gaining ground.

JP Morgan's equity strategist Mislav Matejka said he would stay "overweight" on euro zone equities, given signs of an economic recovery in the region. But he was more cautious on equities overall, citing tensions in the credit market and a weakening in the U.S. stock market.

"We would look to use any strength as an opportunity to reduce equity allocation," Matejka said. He advocated selling out on any move up.

Telecoms were also in focus, with French conglomerate Bouygues rising 1 percent after a media report that Orange was closer to buying Bouygues' telecoms arm for 10 billion euros.

Air France KLM shares rose 2.3 percent after Bank of America Merrill Lynch upgraded its rating on the stock to "buy".

Today's European research round-up