

3 Stocks Exposed to China; Should Investors Be Worried?

Description

The news out of China yesterday was ugly. The government released trade statistics that showed an 18.1% decline in exports year-over-year. This came after a March 2 report that showed a decline in manufacturing activity.

As a result, commodity prices plummeted. Copper prices fell 5% while iron ore fell 8.3%, and both metals finished at multi-year lows. The day reignited talk of the end of the “commodity supercycle”, an era in which demand from China fueled abnormal commodity prices for more than a decade.

Many Canadian stocks felt the pain from yesterday’s news, but some more than others. Below are three companies that have especially large exposure to the Chinese economy.

Teck Resources

Teck Resources (TSX:TCK.B)(NYSE:TCK) makes money from three commodities: coking coal (47% of gross profit), copper (38%) and zinc (15%). Coking coal is used exclusively in steelmaking, and China accounts for 45% of steel demand worldwide.

It is important to remember that if China suffers a slowdown, steel will almost certainly suffer more than copper. This is because steel use is heavily weighted towards construction. And if China suffers a correction, construction (and thus the steel market) will be hit especially hard. So Teck investors are certainly hoping that yesterday’s news was an aberration.

Unsurprisingly, Teck shares fell 2.46% on Monday.

Labrador Iron Ore Royalty Corporation

Even more dependent on the steel market, **Labrador Iron Ore Royalty Corporation** ([TSX:LIF](#)) makes all of its revenue from iron ore – this means that the company makes all its revenue from the steel market as well. Thus LIORC is especially dependent on China.

Many investors are drawn to LIORC’s dividend – last year, cash distributions totaled \$1.875 per share, not bad for a \$31 stock. But these are not stable dividends at all. For example, when the steel market softened in 2012, cash distributions dropped by a third.

LIORC shares dropped even more sharply than Teck’s, down nearly 4% on Monday.

Capstone Mining

Capstone Mining ([TSX:CS](#)) makes all of its money off of copper, which should make the company less exposed to China than the two companies above.

But Capstone is much more ambitious about growth. The company hopes to develop a large copper

mine in Chile, called Santo Domingo. Capstone estimates that Santo Domingo's cost will fall between \$1.5 billion and \$1.8 billion, a steep price tag for a company with a \$1 billion market capitalization (Capstone owns 70% of Santo Domingo).

Capstone also has a more levered balance sheet than Teck and LIORC. So even if copper isn't as risky as steel-based commodities, Capstone shares are still a more daring China bet.

Unsurprisingly, Capstone shares fell by 5% on Monday.

Foolish bottom line

The companies listed above are all very dependent on the Chinese economy, and are thus very risky bets. Investors who have confidence in China, and are looking for a way to profit from a rebound, may want to consider these names. But investors who prefer not to make such gambles should instead stay on the sidelines.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:TECK (Teck Resources Limited)
2. TSX:LIF (Labrador Iron Ore Royalty Corporation)
3. TSX:TECK.B (Teck Resources Limited)

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