Could Teck Resources Ltd. Hit $35?

Description

Teck Resources Ltd. (TSX: TCK.B)(NYSE: TCK) is really taking it on the chin these days. The company is Canada's largest diversified miner and just about everything Teck produces is being crushed by the weakness in the overall commodity markets.

The stock has been on a slide since topping $60 in early 2011 and is now trading at a five-year low of $17.50. The shares are down 25% in just the past month!

The old adage, "don't try to catch a falling knife" certainly comes to mind here but it looks like the knife might be close to hitting the floor.

Here are the reasons why I think value investors should consider adding Teck Resources to their portfolios right now.

1. Metallurgical coal

Steelmaking coal or "met coal" is the largest part of Teck's business. In fact, the company is the world's second-largest shipper of coking coal in the seaborne market. Met coal prices have been floating around multi-year lows due to lower Chinese demand and higher output from Australian suppliers. Recent news that China will implement a new coal tariff is largely responsible for the accelerated selloff in Teck's shares but the market has overreacted.

Teck announced in September that it is reducing shipments of coal to China. China will be the destination for roughly 25% of 2014 coal production. The net effect of the new Chinese tariffs on Teck's earnings will be minimal.

In its second-quarter earnings report, Teck said it has new agreements in place with quarterly contract customers for 5.5 million tonnes of met coal at a price of $120 per tonne. Teck's Q2 average realized met coal price was $111 per tonne and the division reported a gross profit margin of 3%.

Analysts say the current market price is not sustainable in the long run because a significant number of producers are simply unprofitable at prices in the $100-$120 per tonne range.

The good news is that global demand is slowly increasing. At the same time, North American producers are shutting down more production and delaying mine expansions. By the second half of 2015, the met coal market should see a turnaround.

2. Low-cost copper production

Copper is Teck's second largest source of revenue. With prices stuck near the $3.00 per pound mark, you would expect profits to be scarce. In fact, Teck still does quite well on its copper sales, even at rock-bottom prices. In the second quarter Teck reported gross profit margins of 25% on copper with an average realized price of $3.08 per pound.

3. Effective management of capital

Teck embarked on an aggressive cost-cutting program in 2012, and has been very successful at maintaining profitability through the difficult market conditions. The company is now a lean, mean, mining machine and well positioned for the rebound in met coal and copper. In its latest report, Teck said it had already reduced 2014 operating expenses by $150 million and reduced capital expenditures by another $150 million.

4. Fort Hills project

Investors are avoiding anything that smells of oil sands these days, but it is important to point out Teck's 20% ownership of the Fort Hills project that will start producing 160,000 barrels per day in 2018.

5. Get paid to wait

Teck pays a dividend of $0.90 per share that currently yields about 5%. The dividend is probably safe. Teck is still profitable and the company announced a share buyback plan to repurchase up to 20 million shares in the next 12 months.

Should you buy?

Teck's capital commitments for Fort Hills will wind down in the next few years as the project switches from development to production. This will free up cash, and add a new revenue stream. With the bottom in sight for met coal and copper, it might be worth a contrarian shot to collect 5% and wait for the rebound. Teck's shares could run significantly higher in a very short time span.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

1. NYSE:TECK (Teck Resources Limited)
2. TSX:TECK.B (Teck Resources Limited)

Category

1. Investing
2. Metals and Mining Stocks

Date
2025/08/03
Date Created
2014/10/17
Author
aswalker