Teck Resources Ltd: Should You Buy or Bail Out?

Description

Teck Resources Ltd. (TSX:TCK.B)(NYSE:TCK) has been hit by a three-year perfect storm and investors are wondering if the sky is finally starting to clear.

Let's take a look at the current situation to see if you should consider adding the stock to your portfolio right now.

Stock price

Teck has lost almost 80% of its value in the past three years. As far as charts go, it's about as ugly as they come. Every sign of a possible rebound has been followed with a lower low and the recent rollover after a short pop off the December crash is indicating another possible swoon.

Commodity prices

Teck produces zinc, copper, and metallurgical (steelmaking) coal. Al three products have been under pressure in recent months, but the met coal and copper industries have really taken it on the chin.

Met coal is Teck's largest operation. Back in 2011, producers were getting as much as US$330 per tonne. In the fourth quarter of 2014, Teck had contracts in place to supply met coal at just $119 per tonne and market prices for the first quarter of 2015 are expected to be similar or slightly lower.

A slowdown in Chinese demand coupled with increased production from Australian suppliers has offset nearly 25 million tonnes of supply cuts by other global producers.

On October 29, Teck CEO Don Lindsay said another 10 to 15 million tonnes of cutbacks are needed to bring supplies in line with demand. The reductions are expected to materialize, given that roughly a third of all producers are unprofitable at current prices.

Teck isn't one of them. The company still made money on its coal operations in Q3 2014, with production costs coming in at $84 per tonne. Lindsay said he sees the met coal market coming back into balance as early as the middle of 2015.

Copper has also been in a nosedive. Prices have fallen from US$3.20 per pound in July to less than $2.60. Reports of a boost to infrastructure spending in China have some pundits thinking the bottom of the cycle is within sight.

China's Q4 2014 gross domestic product rose 7.3% compared to the same period for 2013. The number was better than expected, but still quite low.

Teck's copper operations are extremely efficient. In the third quarter of 2014, the company reported gross margins of 46% on an average realized price of about $3.00 per pound. The numbers won't be as good in the current quarter, but the company is still profitable.

Oil prices

Much of the weakness in the shares during the past few months is attributed to Teck's connection to the Fort Hills oil sands development. Teck has a 20% interest in the project and is committed to kicking in $3 billion to get it completed. At current oil prices, some analysts say Fort Hills is at risk of being mothballed.

The project is scheduled to go into production in 2018.

Dividend

Despite difficult markets and a falling stock price, Teck has actually increased its dividend by 50% in the past three years. The current distribution of $0.90 per share is still safe according to a statement Teck made in December. The company would likely scale back its share repurchase plan before cutting the dividend payout.

Even at current commodity prices, Teck is still making money, and the company finished the third quarter with $2 billion in cash and a US$3 billion line of credit.

Should you buy?

It takes some guts to step into the stock at this point, but the long-term upside could be significant from these levels. The company is a low-cost producer, and both copper and met coal should see better prices by the end of the year. Contrarian investors who believe the stock has finally bottomed can collect a 6.3% dividend while they wait for a rebound.

CATEGORY

1. Investing
2. Metals and Mining Stocks

TICKERS GLOBAL

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