# Don’t Try to Catch This Falling Knife: First Quantum Minerals Ltd.

## Description

Softer commodities, in particular copper prices, have brought the spotlight firmly back on base metal miners with fears among investors that the outlook for commodities, including copper, can only worsen. This is bad news for Canada’s largest copper miner **First Quantum Minerals Ltd.** (TSX:FM), which has seen its share price crash to earth over the last six months, down a massive 54%.



The increasingly pessimistic outlook for copper and other commodities coupled with concerns over First Quantum’s financial condition saw its outlook recently downgraded.

**So what?**

Copper, which generates 65% of First Quantum’s revenue, recently touched a five-year low, triggering alarm bells among investors and analysts as to the state of the global economy. Such low prices have a significant impact on First Quantum and are a key driver of its decision to defer 2015 capital expenditures in order to preserve its balance sheet.

But the long-term outlook for First Quantum remains pessimistic.

The outlook for copper depends heavily on China, with the metal being a key component in manufacturing and housing construction. In fact, China is one of the world’s single largest consumers of copper. Yet investment in China’s housing sector continues to fall, with 2014 investment down by 10.5% in comparison to 2013.

Even more troubling is that the decline in China’s housing sector is expected to continue and this certainly doesn’t bode well for copper prices. Another concern is that China’s economy continues to slow, with 2014 GDP growth of 7.4%, the lowest level in two decades. Of greater concern, China’s GDP is expected to fall even further to 6.8% in 2015 and then 6.2% in 2016.

This certainly doesn’t bode well for growing copper demand. Declining consumer demand and industrial activity in the Eurozone is also a factor, with the economic region finding itself stuck in a deep economic slump.

The declining outlook for copper will have a deep impact on First Quantum's financial performance and it appears unlikely the company will deliver any tangible improvements in the foreseeable future.

The uncertainty surrounding First Quantum's financial position is also of considerable concern. The company has a mountain of debt totalling US$5.5 billion, with net debt a whopping 3.6 times cash flow. This indicates First Quantum is overleveraged and this is particularly worrying in an operating environment where earnings and cash flow will at best remain flat, or more than likely fall.

**Now what?**

While the consensus analyst outlook for First Quantum is a "buy" I believe it is a company investors should avoid. It is unlikely that First Quantum will be able to sustain any meaningful growth over the long term and the weakness of its balance sheet and flat cash flow growth is of considerable concern in such a difficult operating environment.

There are better investment opportunities offering far greater potential upside coupled with more consistent returns that are not as heavily exposed to the whims of commodity markets and the profound disruption in base metals demand we are now seeing.



**CATEGORY**

1. Investing
2. Metals and Mining Stocks

**TICKERS GLOBAL**

1. TSX:FM (First Quantum Minerals Ltd.)

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**Date**
2025/07/04
**Date Created**
2015/01/29
**Author**
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