Is Now the Time to Buy Teck Resources Ltd.?

Description

It's sure been a rough ride for shareholders of **Teck Resources Ltd.** (TSX:TCK.B)(NYSE:TCK). After the company's stock skyrocketed from less than $5 in 2009 to over $60 in 2011, the share price has fallen back below $20.

The main culprit has been China, whose slowing growth has weakened demand for copper and steelmaking coal, which together accounted for 70% of Teck's revenue last year. Each of those commodities has been steadily dropping in price, and Teck's profitability has been eroded as a result.

And this showed through once again when Teck reported Q4 2014 results on Thursday. Revenue was down 5% year-over-year. Gross profit was down 24%, as was EBITDA. And pre-tax profit declined by more than half.

Oddly enough, Teck's shares have increased in response, as of this writing. Clearly the company's expectations are so low that even these numbers can be interpreted as good news. So why are the shares up? And is now the time to buy Teck Resources?

A couple of nice tailwinds

Amid all the doom and gloom, Teck benefits from a couple of economic trends. One of them is the decline in the price of oil. Remember, diesel fuel is a major input cost for any mining company, so any decrease in the oil price should help improve margins. In Teck's case, at current exchange rates, every US$1 drop in the price of oil saves the company $5 million in operating costs.

But there's another benefit that should help even more: the decline of the Canadian dollar. This helps because Teck's sales are denominated in USD, while "a significant portion" of expenses are incurred in CAD. To put this in perspective, each 1 cent change in the exchange rate alters EBITDA by over $50 million. And unlike the oil price tailwind, Teck does not have to share this exchange rate benefit with its international competitors.

A couple of other nice positives

For years, Teck has had to deal with a strong CAD and high oil prices. But that may have been a blessing in disguise, because it's forced Teck to reduce costs in other areas. Those efforts now seem to be paying off.

More specifically, Teck's cost reduction program has achieved approximately $640 million in annual savings so far. And in today's commodity environment, which seems to be a war of attrition, these cost savings could pay off big time.

Secondly, there is some modestly good news from the coal business. Teck has agreed to sell 6.2 million tons of steelmaking coal at US$117 per ton "for the highest quality products". By comparison, Teck's coal sold at US$110 per tonne last quarter. While these two numbers are not entirely comparable, it signals that coal's decline may not be so severe anymore.

This is still a stock to avoid

As can be seen, Teck is likely more exposed to China's fortunes than any other company on the **S&P/TSX 60**. So if you're really looking to make a bet on China, this is the stock for you. But I wouldn't make that bet.

China's rise has been fuelled mainly by debt, and there are plenty of signs that the country has overbuilt. Numerous analysts have predicted a very hard landing for the country's economy. And if they are even half right, Teck's shares could tumble a lot more. And that's not a risk worth taking.

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
2025/07/22
Date Created
2015/02/12
Author
bensinclair