



## Why Are Copper Producers' Share Prices Plummeting?

### Description

While the prices for some natural resources have fallen off a cliff, copper prices have held up relatively well. The metal peaked at just over US\$4 per pound back in 2011, and still trades for close to US\$3 today. By comparison, commodities such as coal, iron ore, and oil have fallen by far more.

This has been a nice relief for companies like **First Quantum Minerals Ltd.** ([TSX:FM](#)) and **Hudbay Minerals Inc.** ([TSX:HBM](#))([NYSE:HBM](#)), both of which make the vast majority of their cash flow from copper. Copper also accounted for 41% of gross profit at **Teck Resources Inc.** ([TSX:TCK.B](#))([NYSE:TCK](#)) last year.

That said, there are some dark clouds on the horizon for copper producers. Below we take a closer look.

### The bull case for copper

There are some strong arguments for why investors should like copper.

First of all, the market remains in surplus, but that surplus is declining, and represents a tiny fraction of the overall market. Secondly, copper mining costs continue to rise as grades decrease, and the best mines are increasingly found in high-risk jurisdictions.

Meanwhile, mines continue to deplete, and exploration companies are having trouble getting financing. So, we could see a copper shortage in just a few years' time. And the last time we were in this position (in the late 1990s), the copper market wasn't ready for China's boom years. That led to many years of supply shortages and price increases.

### The Mongolian giant

The Oyu Tolgoi (OT) mine, located in the southern Gobi desert of Mongolia, is a mammoth project by any standard. It is estimated to produce 450,000 tonnes of copper per year, more than First Quantum's 2014 production. By 2021 the mine will generate up to a third of Mongolia's GDP, according to the IMF.

Until this week OT's underground phase (which contains roughly 80% of the total deposit) was held up over disagreements with the Mongolian government. But on Tuesday those issues were finally hashed out.

Granted, there are still some additional steps that must be taken, including a feasibility study. And no copper will be produced from OT's underground operations until 2020. But this does not bode well for copper's long-term fundamentals.

### **What should investors do?**

Hudbay Minerals shares are down by 3%, and First Quantum's shares are down by 6%, as of this writing. Even Teck Resources, which is supposedly less affected by this news than the pure-play copper producers, is down by nearly 5%.

Still, I would avoid these stocks. At nearly US\$3 per pound, copper still trades well above marginal costs for the vast majority of the industry. So, there's still plenty of incentive for new projects, and plenty of room for prices to fall. I'm not sure that's being fully accounted for by these companies' stock prices.

### **CATEGORY**

1. Investing
2. Metals and Mining Stocks

### **TICKERS GLOBAL**

1. NYSE:HBM (Hudbay Minerals Inc.)
2. NYSE:TECK (Teck Resources Limited)
3. TSX:FM (First Quantum Minerals Ltd.)
4. TSX:HBM (Hudbay Minerals Inc.)
5. TSX:TECK.B (Teck Resources Limited)

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