



## Teck Resources Ltd.: Turnaround Candidate or Value Trap?

### Description

Surprisingly, despite sharply weak commodity prices, a number of analysts continue to talk up the prospects of embattled miner **Teck Resources Ltd.** (TSX:TCK.B)(NYSE:TCK). This positive outlook relies upon the view that commodity prices are cyclical and likely to recover, with their current weakness leaving Teck attractively valued and a prime turnaround candidate.

However, this couldn't be further from the truth, even though commodities are typically cyclical.

### Now what?

These analysts are failing to recognize is that there has been a fundamental shift in the commodities landscape. This is because China, whose emergence as an economic giant, triggered an epic commodities super-cycle that is now in the process of winding down as its economic growth falters.

You see, China's GDP in 2014 was at its lowest point in almost three decades and is expected to continue slowing, with 2015 GDP forecast to be 6.8% and 2016 to be 6.3%. This, along with diminishing construction and manufacturing activity, two sectors among the biggest consumers of steel and copper, does not bode well for any increase in demand.

As a result, coking coal is hovering at about US\$100 per tonne, while copper is trading at US\$2.80 per pound. It is also expected that neither of these commodities will experience any meaningful recovery in the foreseeable future because of ongoing economic weakness in the Eurozone and lower growth in China. This doesn't paint a pretty picture for Teck, with coking coal generating about 40% of its total revenues and copper another 26%.

Even more worrying is that global supplies continue to grow despite decreasing demand and weaker prices. Two of the world's largest producers of coking coal, **BHP Billiton Ltd.** and **Rio Tinto Plc.**, continue to ramp up output despite weak prices as a means of creating economies of scale and depressing prices in order to push high-cost producers out of the market.

This doesn't bode well for Teck's cash flow, which continues to decline. For the first quarter 2015 cash flow plunged by a massive 32% year over year and will continue to decline as coking coal and copper

prices remain depressed.

Of even greater concern is Teck's growing mountain of debt. For the first quarter, long-term debt shot up by 19% year over year, leaving it heavily leveraged, with net debt of \$7.6 billion being almost four times its operating cash flow. When this is considered in conjunction with its declining cash flows and commitment to invest a further \$1.6 billion in the Fort Hills oil sands project, and \$4 billion in debt repayments falling due in the next five years, Teck is facing a potential liquidity crunch.

### **So what?**

For all of these reasons, it is extremely difficult to see any upside in Teck, with the poor outlook for coking coal and copper weighing heavily on its ability to generate sufficient cash flow to meet its financial obligations. In fact, the risk of a liquidity crunch in the foreseeable future makes it challenging to see how Teck can ever deliver value for investors. For these reasons, I don't see any upside in Teck and believe it is a stock that investors should avoid.

### **CATEGORY**

1. Investing
2. Metals and Mining Stocks

### **TICKERS GLOBAL**

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

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