



Teck Resources Ltd.: This Turnaround Stock Has Huge Potential

Description

It hasn't been good to be a shareholder in **Teck Resources Ltd.** (TSX:TCK.B)(NYSE:TCK) over the last few years.

Since shares peaked at more than \$60 each back in early 2011, it's been a long, painful ride for shareholders. Shares are currently trading at \$8.63 each, which represents a haircut of nearly 90% from the highs. The company hasn't been this cheap since 2009, when its very future was in doubt.

The recovery from the lows back in 2009 was amazing, with shares soaring from less than \$5 each to \$45 a year later, eventually peaking at more than \$60.

Does the company have the potential to do that again? Perhaps not, but there are still plenty of reasons to believe that patient investors will be rewarded if they get in now.

It's insanely cheap

Many value investors start their search for undervalued companies by screening for stocks that are trading at a discount to their book value. It's not a perfect system, since often book value is overstated by things like goodwill and intangible assets. Still, it provides a good place to start looking.

On a price-to-book basis, Teck is perhaps the cheapest company in Canada that isn't on its deathbed. The company has a book value of more than \$32 per share, which puts the share price at approximately one quarter of book value. In comparison, most Canadian stocks trade at about twice book value.

Remember, Teck is still solidly profitable as well, even though the metallurgical coal market is about as bad as it has ever been. It has earned \$0.60 per share over the last 12 months, and analysts predict the company will be able to earn \$0.56 per share in 2015, growing that to \$0.71 in 2016.

How often can you find a company that trades at a quarter of book value and is actually making money? There aren't many.

Growth potential

One of the reasons why the market is writing off Teck is because of the company's commitment to the Fort Hills oil sands project, a partnership with **Suncor** and Total that's slated to begin production in the last quarter of 2017. Teck is still committed to providing some \$3 billion in financing for the project.

The issue is Teck doesn't have that much cash. The company is sitting on \$1.3 billion in cash as of June 30th, and has generated about \$340 million in free cash flow thus far in 2015. After spending \$259 million on dividends in the first half of the year, that only puts it on pace to generate about \$160 million in cash this year, although 2016 should be slightly better because the company cut its dividend earlier in the year.

Still, Teck is looking at having to raise between \$1 billion and \$1.5 billion come 2017. Investors aren't sure the market will continue to fund this expansion if commodities stay weak.

But instead of looking at the negatives, let's look at the positives of Fort Hills. If the price of crude averages \$70 per barrel and the Canadian dollar is worth US\$0.80, Fort Hills will deliver \$350 million in annual pre-tax cash flow. That's a free cash flow yield of approximately 12%, not even assuming a full recovery in crude. At \$90 per barrel, the numbers are even more attractive.

Commodity recovery

Teck's management has done a nice job of cutting costs as the price of its commodities have fallen. Now investors just have to wait until the market for metallurgical coal recovers, and to a lesser extent, zinc and copper.

Yes, I realize the outlook for commodities looks pretty bleak. The price of just about every major commodity isn't anywhere close to a 52-week high. But I'm willing to bet they'll recover at some point. Sentiment is just too low the whole sector to not recover.

Just a small recovery in the price of commodities is very beneficial to Teck. If copper goes up a penny per pound, Teck's annual profits go up \$5 million. If metallurgical coal goes up \$1 per tonne, \$21 million flows to the bottom line.

Teck is one of the cheapest companies in Canada. If all goes right and commodities recover, shares of this mining giant could end up much higher. Yes, it's a risky company at this point, but there's plenty of potential reward if it can figure things out.

CATEGORY

1. Investing
2. Metals and Mining Stocks

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

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