



## Will Teck Resources Ltd. Be Forced to Sell its Assets at Fire-Sale Prices?

### Description

Investors are starting to get concerned about **Teck Resources Ltd.** (TSX:TCK.B)(NYSE:TCK).

There are two big concerns. The first is the future of the metallurgical coal market. Back in 2010-11, China's real estate bubble was fueling a huge bull market for the type of coal used in the production of steel. As we approach 2016, it's obvious that China's construction market isn't going to return to 2011 levels anytime soon.

China still has plenty of steel-producing capacity. It also has domestic coal available for use in steel production and labour that's cheaper than North American steel producers. China is flooding the market with cheap steel, content to get something for the metal. Teck can't even count on growth in domestic production to help boost the price of coal, since cheap Chinese steel is forcing world prices down.

Teck has responded to these macro issues by doing a number of things. It has laid off thousands of workers. It has cut its semi-annual dividend twice from \$0.45 per share all the way down to \$0.05. It has idled production, cut back on capital expenditures, and delayed certain projects. The company has also been helped by the price of oil going down. Oil is one of its largest input costs.

### Balance sheet issues

The health of Teck's balance sheet is the other big issue facing the company.

If it were just business as usual, investors wouldn't be so concerned. The big issue is Teck's commitment to Fort Hills, a huge new oil sands development which is slated to begin production sometime in late 2017. As a 20% owner, Teck's share of the project's cost is north of \$3 billion with some \$1.5 billion still owing.

**Total**, the French energy giant, previously owned a 39% stake in Fort Hills. In September, it and **Suncor Energy**—the majority owner of the project—announced a deal in which Total sold part of its stake to Suncor at a discounted price. Total now owns 29% of the project, while Suncor now owns more than 50%. Teck's ownership stake remains at 20%.

Total is a massive energy company. Its ADR shares on the New York Stock Exchange have a market cap of \$121 billion and, as of June 30, the company was sitting on US\$29.7 billion in cash. And remember, Total pulled out of the Joslyn oil sands project in 2014. There must be a reason why a company with the resources of Total is skittish about oil sands in general.

The worst-case scenario for Teck is to have to sell part or all of its stake in Fort Hills at a fire-sale price. Suncor seems like the only oil company in the world that's interested in oil sands assets right now. One bidder isn't conducive to getting the best price.

Fortunately for Teck, it doesn't look to be that bad.

### **Can it afford \$2 billion?**

Teck is on the hook for \$1.5 billion for Fort Hills as well as approximately \$500 million in capital expenditures for its core business over the next couple of years.

Where's the \$2 billion going to come from? Teck is currently sitting on about \$1.5 billion in cash. The existing mining business is also marginally cash flow positive, on pace to generate approximately \$250 million in 2015. If it could maintain that cash flow over the next two years, Teck looks to be in good shape.

It has US\$600 million worth of debt due in 2017, but the company also recently announced a deal where it generated \$1 billion in cash from two streaming agreements. It also has nearly \$6 billion in available credit.

In short, Teck looks like it can afford its obligations over the next two years without adding much to the company's already bloated debt load of nearly \$10 billion. It doesn't look like Teck will need to sell its stake in Fort Hills.

Teck is a levered play of commodities recovering, particularly coal. If you believe the price of coal will rise from the current multi-year lows, Teck could be a huge winner. If it doesn't recover within a few years, Teck will ultimately be forced into bankruptcy. There's only so much cutting that can be done.

### **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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