Could Teck Resources Ltd. Hit $30 in 2016?

Description

Teck Resources Ltd. (TSX:TCK.B)(NYSE:TCK) is up more than 70% since the start of the year, and investors are wondering if this is the start of another epic rally.

Let's take a look at the current situation to see if Teck deserves to be in your portfolio.

A perfect storm

Five years ago Teck traded for more than $50 per share. Today the stock is available for $9, but savvy investors had a chance to scoop it up for fewer than $4 last month.

What's going on?

Teck produces metallurgical coal, copper, and zinc. All three of these products have been in a nasty bear market for the better part of five years, and investors have pretty much left the stock for dead.

A quick glance at the state of the global economy would suggest more pain could be on the way in the near term, but markets tend to look beyond the immediate horizon, and contrarian investors are seeing some light at the end of the tunnel.

Metallurgical coal is now in its longest slump since 1950. North American producers have reduced production in an effort to bring the market back into balance, but weak Chinese demand and increased output from Australian producers are keeping coal prices under pressure. The situation is expected to persist through 2016, but better times could be in the cards sometime next year.

Copper also remains in a slump, down 50% from its cycle highs. Reduced investments in the sector are expected to reverse the slide in the medium term, and Teck is positive on the long-term fundamentals of the copper market.

Zinc might already be in the early innings of a recovery. The metal has rallied more than 15% over the past month, and some industry observers believe the bottom has been reached.

The role of oil

Teck is not an oil producer, but the crash in crude prices has played a significant role in the stock’s slide.

Why?

Teck is a 20% partner in the Fort Hills oils sands development. The project is on target for completion in late 2017, but investors are concerned Teck has ploughed billions into a facility that will never make money.

The worries are certainly valid if WTI oil prices remain at US$30 per barrel, but most analysts expect oil to rebound.

Teck finished 2015 with nearly $2 billion in cash and cash equivalents, so there is enough liquidity to cover the roughly $1.5 billion needed to get Fort Hills finished.

Debt issues?

Teck finished 2015 with $9.6 billion in debt, which is another reason for the huge sell-off in the stock. None of the long-term notes are due before 2017, so there is no immediate concern of a cash crunch.

Despite the weak market conditions, Teck is still turning a profit, and the company has significant access to capital through its credit lines. If commodity prices are going to recover in the next two years, the debt load should be manageable.

Should you buy?

Based on historical trends, copper, coal, and zinc should be near the bottom of the current cycle.

Teck has done a great job of reducing costs through the downturn, and Fort Hills will be online in less than two years. If coal, copper, and oil begin to turn the corner in the back half of 2016, investors could see Teck continue to move much higher through the end of the year.

A run to $30 would require some serious good news, but contrarian investors with a long-term outlook might want to start nibbling at the current level.

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1. Investing
2. Metals and Mining Stocks

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1. Editor's Choice

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