Teck Resources Ltd.: How High Could it Go?

Description

Teck Resources Ltd. (TSX:TCK.B)(NYSE:TCK) was pretty much left for dead in January, but the stock has since doubled off the lows and contrarian types are starting to bet that history might once again repeat itself.

What happened the last time?

During the financial crisis Teck's stock plummeted from $50 per share to less than $4. Most analysts expected massive debt and low commodity prices to crush the firm, but a restructuring followed by a rally in commodity markets sent the stock skyrocketing.

In fact, it topped out above $60 per share less than two years after hitting the March 2009 lows.

Long-term investors are certainly wishing they had cashed out in early 2011 as the stock has been on a nasty five-year slide ever since. It recently hit the $4 mark again before rising to the current price of $8 per share.

Another commodity downtrend

Teck's current woes are due to a meltdown in the metallurgical coal, copper, and zinc markets as well as the rout in oil.

Coal prices are not expected to recover in 2016 as weak Chinese demand and strong Australian output offset production cuts from North American suppliers. The coal rout is the worst since 1950 and, while the near-term outlook remains bleak, the cycle is likely close to a bottom.

Copper is also struggling, but market observers believe the situation should improve before the coal market recovers. Teck says the long-term fundamentals for copper remain positive, and the company is a low-cost producer in the industry.

Zinc is probably the closest to a meaningful recovery. Prices are approaching six-month highs, and some analysts believe the zinc market has bottomed.

What’s the oil connection?

Teck is not an oil producer, but it does have a 20% stake in the large Fort Hills oil sands project, which is scheduled to begin production in late 2017.

Fort Hills has been a huge cash drain, and market observers are concerned that oil might not recover enough to make the facility profitable. Things could play out that way, and the risk is a large reason why the stock has been hit so hard in the past five years.

However, oil sands facilities are built with a production horizon of decades, so there is plenty of time for the Fort Hills investment to pan out. For every analyst calling for WTI oil to remain below US$40 per barrel, there is another saying prices are headed back to US$80.

We will see how it all works out, but Teck and its partners are taking advantage of the tumultuous times to demand lower prices from suppliers and contractors.

Teck has about $1.8 billion in cash and cash equivalents, which is more than enough to cover its $1.2 billion in remaining obligations over the next two years to get Fort Hills finished.

Debt concerns

Teck finished 2015 with $9.6 billion in debt, which is another reason the stock has been under so much pressure. None of the debt is due before 2017 and only US$600 million has to be repaid that year, so Teck has flexibility before Fort Hills goes into production.

Should you buy Teck?

A repeat of the spectacular two-year stock surge is unlikely, but a longer-term rebound to a significantly higher price is certainly possible. If oil manages to recover in time for the Fort Hills start up, Teck will get a big boost. That event could also coincide with a bottoming of coal and copper markets.

Volatility should be expected in the near term, but contrarian types might want to add a bit of Teck to their portfolios. As we have seen in recent weeks, the name can move a lot higher in a short period of time on good news.

CATEGORY

1. Investing
2. Metals and Mining Stocks

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