An Improving Global Economy Bodes Well for Base Metals and Miners

Description

The International Monetary Fund, or IMF, recently lifted its outlook for the world economy**,** forecasting GDP growth of 3.6% in 2017 and 3.7% in 2018 — about 20 basis points higher than its earlier projections. This bodes well for the outlook for commodities — notably, metals such as steel, copper, zinc and nickel — particularly when it is expected that capital expenditures on infrastructure will also grow across the globe.

Now what?

As a result, in recent months, many investment banks have revised their forecasts upwards for base metals miners. That includes **Morgan Stanley**, which raised its target prices for a range of miners, including Canada's **Teck Resources Ltd.** (TSX:TECK.B)(NYSE:TECK). The bank's analysts are exceptionally bullish on steel-making or coking coal, which is responsible for generating almost half of Teck's revenues. They lifted their 2018 price target for coking coal by 28% compared to an earlier forecast.

Much of the optimism surrounding the outlook for the global economy and base metals can be attributed to improved economic growth in China, along with India's sustained rapid development. IMF analysts hiked their average annual GDP growth forecast for the world's largest consumer of coal and metals, China, from an average of 6% to 6.4% for 2017 through to 2021. That higher growth in China will lead to increased consumption of metals for manufacturing and construction. This is because, despite Beijing's attempts to transition to a service-based economy, export-focused manufacturing is still the primary driver of economic growth.

Over the last 10 years, China has emerged as the world's workshop and has become a global manufacturing hub. While industrial activity contracted sharply as economic growth dipped in 2015, it has continued to expand strongly over the last year.

Meanwhile, activity in China's real estate sector has also improved significantly with renewed property construction activity further bolstering demand for steel and copper. This is being supported by increased investment in infrastructure driven by Beijing's credit-led economic stimulus packages.

Considering that the manufacturing and construction sectors in China are among the single largest consumers of steel, copper, and zinc globally it is easy to understand the optimism surrounding the outlook for base metals.

According to the World Bank, supply constraints for base metals in conjunction with firmer demand will support higher base metal prices over the remainder of 2017 and into 2018. Industry insiders are also predicting that the global copper market will be in deficit in 2018 because of constrained supply caused by a lack of fresh projects. That will cause prices to rise, particularly if demand from China and India remains firm.

So what?

For these reasons, Teck appears attractively valued, especially since it is down by almost 2% over the last year, providing investors with a handy entry point. This is also good news for miner **First Quantum Minerals Limited** (TSX:FM), which earns the majority of its revenues from copper and nickel mining. Unlike Teck, however, First Quantum has enjoyed a solid rally to be up by almost 27% over the last year, meaning that there is potentially less upside available for investors, because markets have already priced in the optimistic outlook for copper and nickel.

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1. Investing
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Date

2025/10/01

Date Created

2017/11/08

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