Contrarian Investors: A Cheap Commodity Stock to Play the Global Economic Rebound

Description

The stock market rally off the March lows wiped out many of the great deals, but some unloved stocks still trade at fire-sale prices.

Let's take a look at one industry leader that might be interesting contrarian pick right now to position your portfolio for a rebound in global commodity prices.

Teck Resources

Teck Resources (TSX:TECK.B)(NYSE:TECK) has a history of going on wild rides. Investors who time the moves correctly can reap massive gains. Those who get in at the end of the rally tend to lose their shirts. As such, this isn't a typical buy-and-hold pick for the long haul, but rather a strategic investment to take advantage of the cyclical nature of commodity markets.

Teck is primarily a producer of steelmaking coal, copper, and zinc. It also has investments in oil sands crude production. All of these business segments are under pressure amid the downturn in the global economy due to the pandemic, but the bottom might be in the rearview mirror.

Copper prices are trending higher. The base metal hit a low of US$2.10 per pound at the bottom of the crash in March. The current price is US$2.37. Fiscal stimulus measures expected in China and the United States should help drive a rebound in copper demand in the next few years.

As economies open up again and manufacturing gets back on its feet, demand for steel-making coal should also recover. In the Q1 2020 earnings results, Teck said steel-making coal actually had a strong finish to the quarter, although prices dropped through April.

Teck said it anticipates a decrease in sales through the end of June as clients consider delaying purchases, so the Q2 results might be ugly.

Zinc prices appear to be in recovery mode. The metal traded below US$0.84 per pound in March and is now back to US$0.90, although this is still well off the 12-month high near US$1.25. Again, a rebound in Chinese demand could boost the market through the end of the year and into 2021.

On the oil front, Teck is a 21.3% partner in the $17 billion Fort Hills oil sands mine. The project was built through the downturn that occurred in the wake of the 2014-2015 oil crash. Fort Hills went into operation in early 2018 just as it appeared the oil market might be picking up steam for an extended recovery.

The meltdown that occurred in recent months, however, puts the facility's future in question. Teck took a $474 million impairment charge on the site in Q1 2020. That's after a $910 million write-down in Q4 2019.

As calls for the company to exit oil become more common, it wouldn't be a surprise to see Teck take a hit and sell its stake to the other partners, including **Suncor**.

Teck's management team did a good job in the past few years of reducing debt. Teck had US$7.2 billion in notes outstanding in 2015 — down to US$3.2 billion as of Q1 2020. Approximately US$500 million in debt is due over the next four years. No significant debt maturities are due before 2035.

Teck finished Q1 2020 with $5.8 billion in liquidity, including $525 million in cash. The firm continues to receive investment grade credit ratings from the major credit rating agencies.

Should you buy Teck today?

The stock trades at $12.50 per share compared to the 12-month high above $30. Teck bottomed out below $9 in March.

A quick look at past crashes suggests that this might be a good time to start a contrarian position. Teck went from $4 in March 2009 to $60 in Jan 2011. It then slid for the next five years and hit $5 in early 2016 before rallying to $38 in June 2018.

The balance sheet is in better shape than it was the last time the commodity markets crashed. Teck has the means to ride out the downturn and should benefit as global economic growth recovers.

The upside potential at this point likely offsets the near-term downside risks.

While I wouldn't back up the truck, contrarian investors might want to take a small speculative position in Teck at this level.

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