



Metals Snap Back Rally

*From the August 2009 HRA Journal
David Coffin & Eric Coffin, HRA Advisories*

The continued enthusiasm for metals can be tied to a combination of devaluation of the Greenback and hopes that western recessions are bottoming. The deteriorating US Dollar is an element that will have to be weighed against the demand picture for the next decade. However, western demand hasn't been fundamental to pricing metal, or oil, for over a decade. Current enthusiasm, especially in light summer trading, should be treated gingerly.

It is that hope of a broader bottoming that is causing the US\$ to break below its established range. As fear leaves the market, the capital that had gone to the Dollar because of its liquidity seeks higher returns. These include commodities that are, for the moment, being treated as "early cycle participants of the global (read: western) recovery".

In 1997 the Asian Tigers crashed as their Dollar pegs broke against a flood of cheap Chinese goods. The resource sector smacked down as metals hit new floor prices well below actual costs despite continued boom times for the western economies. We have now moved to the inverse of that 1997 market as capital moves away from the greenback and its flood of cheap (so far) debt. That has just taken over from internal fundamentals as the push on higher mineral commodity pricing.

We have been taking advantage of commodities that were oversold during the Crunch against sustainable demand in Asia, and in China most specifically. That will hold into the medium term since there is insufficient capacity in metals to create a supply bubble. However, the anti-Dollar move we are in can create overbought price spikes, and the nascent bottoming of the western downturn wouldn't support them. We now want to be clear that spikes are two edged, and this summer rally could in end in the fall.

The **copper** price did consolidate back to its near-term base at US \$2.14 (\$4720/t) on July 8th. It then turned around and has recently been making new 2009 highs with this latest burst of enthusiasm. This is despite a steady, though not yet large, rise in LME copper stockpiles. Shanghai stockpiles have held steady, but the exchange indicates orders have fallen off with the recent price gains. We doubt much of the excess stocking in China will get sold back into the market, but it does still need to be used up.

Some idled mine capacity may come back on-line, but caution will still reign during a price spike. It is time to sort out where you want to realize some gains from our earlier quick move into the oversold copper producers after the Crunch. However, the point has been made that Asia, and China in particular, is the price maker for this market.

The post Crunch price recovery for copper will generate a selective reentry of capital into the junior space. Good copper stories with expanding deposits can begin to bear fruit as they have for us in the gold space. But, they too will consolidate on the downside of a spike, so do treat them as the speculations they are.

Gold continued to be range bound, with a push from the weakening \$ countered by the pull of private stocks being sold down. The Indian market has continued to be the important source of "scrap" sales. However, with a break down of the greenback below 2008-09 support levels we expect those sellers to back off and wait for gains. For how long probably will have as much to do with other Mumbai markets as anything else.

Strong gains by several of our junior gold picks in July have validated our view that there is capital willing to take risk for higher gains in the yellow metal's space. Lifting a couple of junior valuations by \$100 million isn't large in the broader scheme; it was in fact tougher for them to find volume when they were trading at \$20 million market caps. The new found liquidity will of itself help to sustain the new price levels, but on-going results will also have add to that support.

This is not yet a broad move into the junior gold space, but more issues are at least seeing their share prices going green. Until a few more large wins are confirmed by take-over this will continue to be a stock pickers market. Some interesting new deals are beginning to show up again, and we expect to outline a few of these going forward.

There has also been a significant lift in the **nickel** price. Impressive gains for auto sales in China, and in Germany have offset declines elsewhere. Government subsidy accounts for a part of the gain in China, and essentially all of it in the form of a "€ for clunkers" program in Germany. The rapid run through and expansion of the 1 billion \$ for clunker program in the US should help as well. However, it is work stoppages in almost all of Canada's nickel mining regions the market is truly counting on now.

Over capacity continues to plague the nickel sector. While some further gains are possible near term it will take a less fragile growth picture to sustain nickel pricing as the Canadian output comes back up to speed.

The Trail **zinc** smelter is getting enough business to be brought back to full capacity, despite continued *gains* for zinc stockpiles on the LME. Import of zinc concentrates into China had increased this year due to an unwillingness by China's smelters to buy some "dirty" domestic concentrates. We are not yet ready to focus on zinc, but do continue to watch for closure of near depleted deposits as a future buy signal.

Iron ore has without question become the most interesting of the bulk minerals this year. The system of annualized price setting based on negotiation between sellers and primarily Japanese users continues to look broken. It took three months after the usual March 31st price setting date for some large Chinese buyers accept a contract rate 33% below last year's highest ever pricing for Australian ore. The national steel producers group is still arguing. This is the same cut Japanese and South Koreans had accepted, but less than the 40% cut Chinese firms had been looking for.

Recent news indicates that, the 2009 markdown notwithstanding, this largest of metal markets still belongs to the sellers. According to Platts the price of Chinese spot importers of iron ore rose by over 21% in July over June, which is still a y/y 50% decline in average prices that had spiked a year ago.

Bloomberg has reported that spot pricing to China is now above \$100/tonne, a 7% increase over the July average, which means the spot price is sitting about 20% above the annual price negotiated with the Japanese and Korean mills. The near term gains are attributed to poor spot availability in Australia, and shipping bottlenecks out of India. Cheaper prices earlier in the year also led to shutdowns in China itself which has a large number of small inefficient miners producing substandard product.

Teck Corp (TCK) has also indicated that its **metallurgical coal** operations have moved back to full capacity due to higher Chinese demand than had been expected at the start of the year. In the rest of the world steel makers are seeing a gradual up-tick in orders and still limited profitability. There is however an up-tick in both Japanese and German industrial output that may signal the worst is in fact over for at least these two cashed up members of the industrialized world.

In gauging future supply of iron ore it is important to note that infrastructure is at least as important as holding a deposit. Rail and port facilities must be in place to sell iron ore. That is why our review this month is a company moving to production in an iron ore region that was left behind by the shift of steel production to Asia 30 years ago. They have the pieces in place to get started. We expect to have more to say on this region over the next while and perhaps on other iron ore developers when they look ready. Ω

David Coffin and Eric Coffin produce the Hard Rock Analyst publications, newsletters that focus on metals explorers, developers and producers as well as metals and equity markets in general. If you would like to be learn more about HRA publications, please visit us [HERE](#) to view our track record, see sample publications and other articles of interest. You can also add yourself to the HRA FREE MAILING LIST to get notifications about articles like this and other free analyses and reports.

The HRA – *Journal*, *HRA-Dispatch* and *HRA- Special Delivery* are independent publications produced and distributed by Stockwork Consulting Ltd, which is committed to providing timely and factual analysis of junior mining, resource, and other venture capital companies. Companies are chosen on the basis of a speculative potential for significant upside gains resulting from asset-base expansion. These are generally high-risk securities, and opinions contained herein are time and market sensitive. No statement or expression of opinion, or any other matter herein, directly or indirectly, is an offer, solicitation or recommendation to buy or sell any securities mentioned. While we believe all sources of information to be factual and reliable we in no way represent or guarantee the accuracy thereof, nor of the statements made herein. We do not receive or request compensation in any form in order to feature companies in these publications. We may, or may not, own securities and/or options to acquire securities of the companies mentioned herein. This document is protected by the copyright laws of Canada and the U.S. and may not be reproduced in any form for other than for personal use without the prior written consent of the publisher. This document may be quoted, in context, provided proper credit is given.

©2009 Stockwork Consulting Ltd. All Rights Reserved.

**Published by Stockwork Consulting Ltd.
Box 85909, Phoenix AZ , 85071
hra@publishers-mgmt.com <http://www.hraadvisory.com>**