

Resources- Boom or Bust?

By Neil Mc Kenna

For the past few years we have continually been reminded that it is boom time for resources. Few would question this and the only debate centred around just how long it would last.....another 5 years, another 10, perhaps 20 years? The insatiable demand for commodities, specifically industrial metals, from the east provided the fundamentals for an unprecedented resources boom. Early last year I wrote briefly on my thoughts of such a boom and cautioned companies valuating projects on the basis of inflated resources prices.

The events in the past few months, and in particular the past 2 weeks, have been unprecedented in resource volatility. The losses experienced on all global financial markets have been staggering and resources have not escaped. Daily losses of 5% and more have occurred with frightening frequency. Even blue chip mining stocks such as Anglo and BHP Billiton have taken large knocks.

Business Day on 1st October 2008, discussed the affect on resources stocks at length. The article (the front page article, "Resources Shares Take a Beating"), discussed, as examples, how at the close of the JSE on 30th September 2008:-

- BHP Billiton was trading at a level (ZAR187.95) last seen in March 2007, having peaked at ZAR320 four months ago;
- Anglo American was trading at a level (ZAR278.00) last seen in late 2006, having peaked at ZAR548 four months ago.
- Impala Platinum has lost 40% of its value; and
- Wesizwe Platinum has lost 70% of its value.

The article goes on to demonstrate how some juniors have been hit even harder, and discussed, as examples, how at the close of the JSE on 30th September 2008:-

- Petmin was trading ZAR3.20 from ZAR4.50 only two weeks prior and off a high of ZAR5.35 in May 2008; and
- Wits Gold was trading at ZAR35.05, off its 12 month high of ZAR180.00.

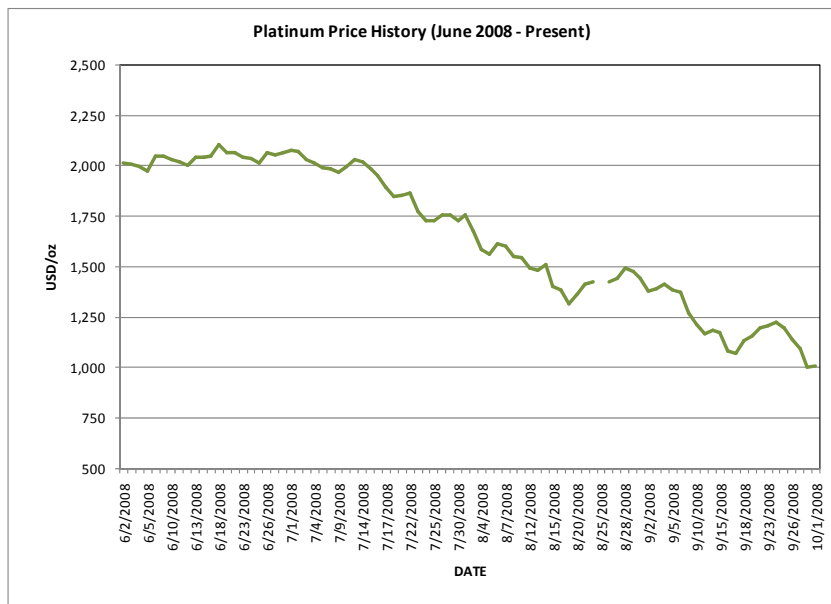
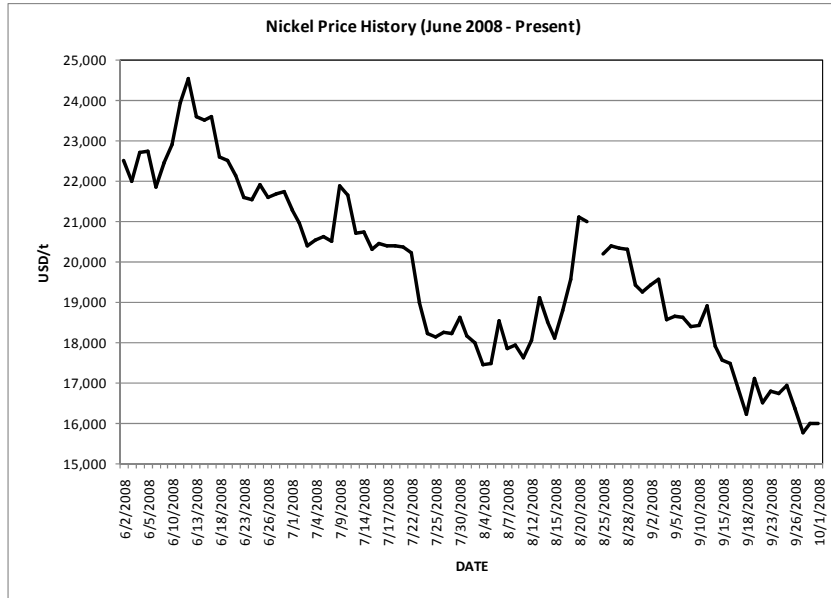
To me the shock has come from the realisation that the sharp drop in commodity prices has been the result of factors largely unrelated to this sector and principally as a result of the global financial crises, not least of all related to the political and financial instability within the United States. Of course local political and financial uncertainty has done little to help this. It is an important reminder of just how vulnerable our sector of the market can be to external factors. It is quite apparent that in times of great uncertainty, investors very quickly shy away from commodities (perhaps with Gold as the exception).

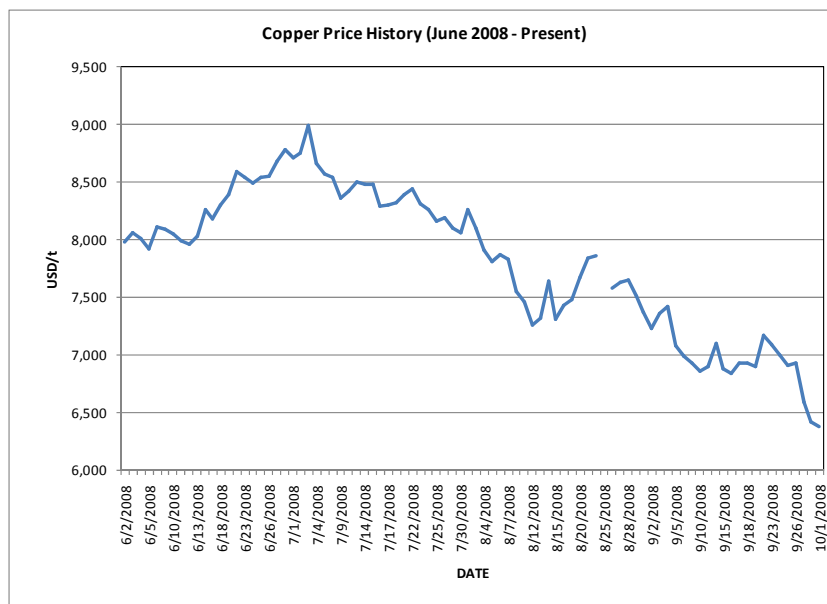
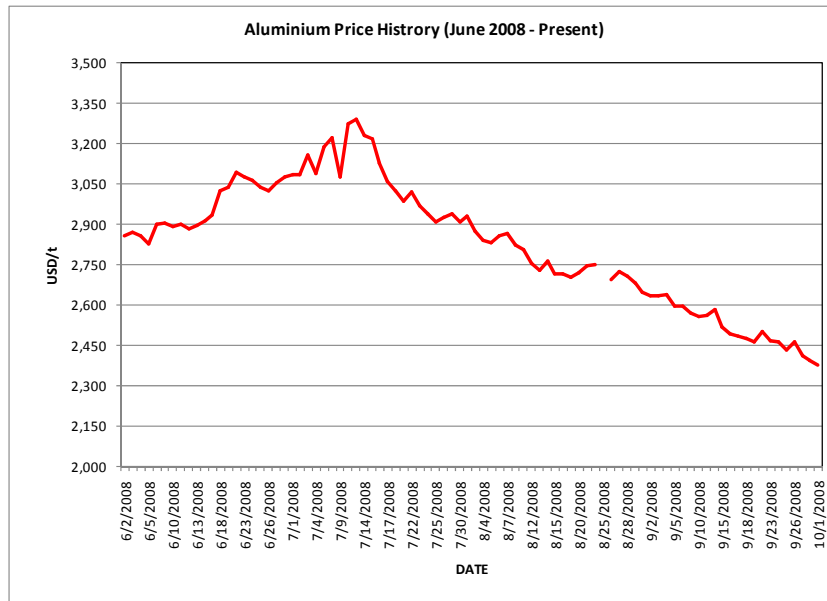
The fundamentals of demand must still be strong, and as we see more and more minerals projects being put on hold due to financing constraints, I question from where the demand for commodities will be satisfied in the long term. This should really be the time for rapid expansion of minerals projects, and I certainly hope this current market crisis is only temporary.

Cash is now certainly king, and companies that can progress projects without the need for financing will surely have a clear advantage. In the South African context I can only see this having a significant adverse effect on Junior Companies, and their ability to compete without having to dilute to the majors.

Is this the end of the Boom cycle? I have to believe it is not. If it is anything more than a temporary correction, I fear that all the gains the industry has made over the past few years will be completely eroded. If the cycle fails, projects will fail. And if key projects fail, despite the fundamentals of demand, then how can global development sustain itself?

I present below a series of graphs of various commodities, over the past 4 months. These graphs certainly paint a pretty gloomy picture. I must believe that we are nearing the end of this very bearish cycle.





While the long term fundamentals of our industry remain strong, we should not lose sight of the external factors that can play havoc with our industry, most of which we have no control over. Again I refer to the devastating effects the financial crisis in the US has had on global markets in recent weeks.

I have posted a new blog on our website (www.venmyn.com), relating to these issues and the current debate over where our industry is headed. I would be very interested in hearing what your thoughts are.

Blog:
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