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Analysts' Ideas of the Week – Las Bambas Sale to Instill More Life Into Mining Sector

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Las Bambas Sale to Instill More Life Into Mining Sector

Yesterday, MMG Limited (HK: 1208), an Australian based Chinese owned company, announced their plans to acquire the massive Peruvian copper project, Las Bambas, from Glencore Xstrata (LSE: GLEN) through a joint venture for $5.85 billion. The JV will be formed by MMG, and two other Chinese entities - Guoxin International Investment Corporation Limited (GXIIC) and CITIC Metal Co., Ltd. MMG will hold 62.5% of the JV, while GXIIC and CITIC will hold 22.5%, and 15%, respectively. MMG and its partners have also agreed to reimburse Glencore for all the capital spent on Las Bambas since the beginning of the year, which is estimated to amount to $400 million. This will bring the total purchase price to $6.25 billion.

Las Bambas is one of the world's largest copper projects. Production is expected to commence next year. The project is expected to produce 400,00 tonnes of copper a year. Approximately 55% of the construction is complete. Another $2.5 billion is required to advance the project to production.

Source: Copper Development Centre

This sale is likely to bring renewed interest into the sector. A 10% drop in copper prices over the past few months had started to concern investors. I had written earlier this year (in February) to advise investors to watch for copper-gold stories due to the favorable outlook for both commodities in the first half of 2014. Shares of Western Copper and Gold Corp. (TSX: WRN), a name I suggested back in February, are up 19%. I continue to expect high quality gold-copper stories to perform well over the coming months.

This deal is also likely to increase interest in companies with projects in south Peru. We expect to initiate coverage on one such company, Vena Resources Inc. (TSX: VEM), shortly.

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Outlook on Input Capital Strengthens from March Update

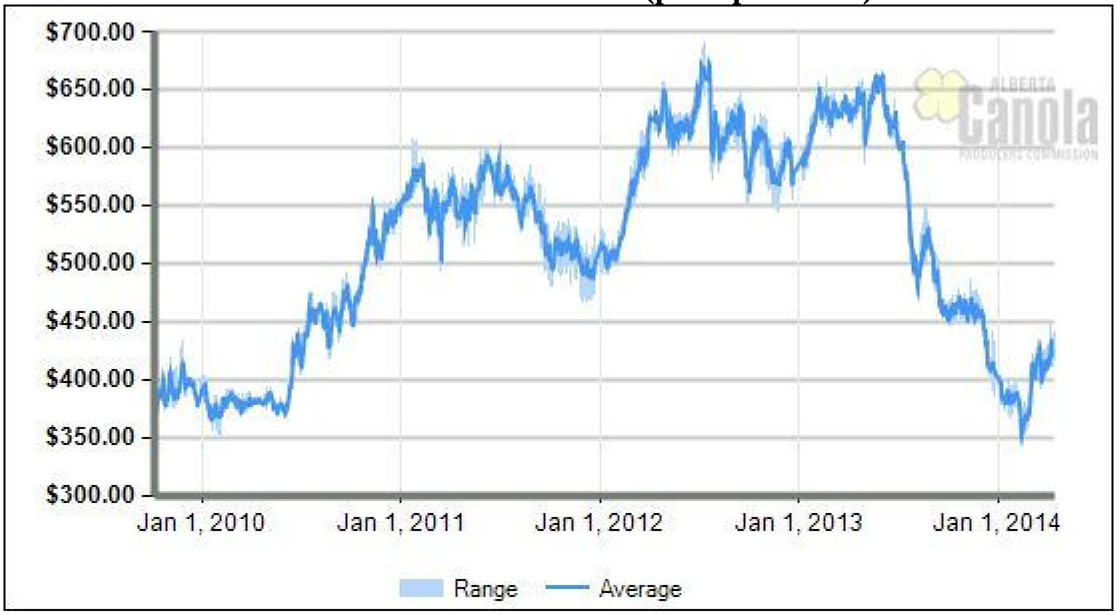
Input Capital (TSXV:INP) recently released their March update. This was a crucial update as March 31 is the end of the company's fiscal year. The monthly updates combined with quarterly financials give investors a good idea of what to expect for the year-end financial statements. It also provides indications for performance in the coming year. We feel that the update provides a positive outlook for the coming year due to deployment of capital, and the cost of canola in new contracts. Deliveries for the year are still delayed, and we expect Input to report lower revenues for FY2013 than we anticipated.

For March, Input reported that they received 1,345 tonnes of canola. This is a big increase over previous months, however, it only brings the canola received for the year to 6,067 tonnes or 33% of contracted tonnes. We anticipate revenues from canola will be much less than our estimate from our last update. However, this is not a fault of operations, but rather, the backlog in transportation. We feel that investors understand the situation and 2013 revenues will not have a significant impact on the company's share price. We feel that in 2013, the company has proven their business model and viability of it.

In February, Input reported that they had not entered into any new streaming contracts, which we felt was slightly concerning. In March, Input reported strong deployment entering 7 contracts with upfront payments of $7.1 million. This brings the amount of capital deployed in new canola contracts to $13.2 million for the most recent quarter. We feel this is strong, as last year, Input had entered into $6.1 million in contracts over the same period, and was still able to deploy another $13.1 million throughout the seeding and growing season. In the update, management expressed that deployment is ahead of schedule, and were more positive on their outlook for deployment. In previous updates, and quarterly MD&As, management was more cautious of capital deployment. We feel this is a strong sign for the upcoming year.

Another positive sign we saw from the update was that the average cash cost paid by Input was decreasing. Due to the current price of canola, the lower cash cost per tonne will allow them to maintain their targeted returns. The average cash costs per tonne of canola in 2013 were $78.95, but this has declined to $68.62, indicating that new contract cash costs are being priced well below previous contracts. We feel this is beneficial for management as Canola prices are much lower than previous years (canola price chart shown below). If canola prices return to the 4 year average price, returns to Input will be very strong.

Canola for Alberta Crushers (price per tonne)



Source: Alberta Canola Producers Commission

We feel that the increased deployment and declining cash costs of canola have set Input up for a strong start to their Fiscal 2014. We expect that if the Canola industry normalizes (delivery timing and pricing), the returns generated from the canola contracts will be strong.

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