COMMODITIES MARKET

Mining – a bull sector within a bear market

While the overwhelming majority of global industries and economic sectors have found themselves under severe pressure over the past year, the mining sector has largely bucked this trend. In fact, Nedbank's Nivaash Singh tells Munesu Shoko, the global commodities sector is positioned as a 'bull sector within a bear market', seemingly immune to the widespread havoc being wreaked in most other sectors by the COVID-19 pandemic, offering unique opportunity for African mining.

Traditionally, the performance of the mining industry, like any other sector of the global economy, tracks the movement of the global GDP. This has become the norm over the years, which is why, traditionally, when global GDP figures trend upwards, the mining sector counters often follow suit. The opposite, says Nivaash Singh, co-head of Mining and Resources Finances, Nedbank Corporate and Investment Banking, has also generally been the case and the sector has historically been at the mercy of periods of negative GDP growth.

However, this historic correlation between the fortunes of global economies and the mining industry has not repeated itself against the backdrop COVID-19, a truly global health and economic crisis of proportions. The commodities market has been resilient in the face of the widespread carnage being wreaked in most other sectors by the pandemic.

According to Singh, there are two major reasons why the commodities sector is enjoying a bull run in a bear market. Firstly, the COVID-19 and the resultant intermittent lockdowns have driven demand for high-tech products, which in turn, has propelled the demand for some critical and strategic metals. The supply/demand fundaments of these minerals have improved during the COVID-19 pandemic as critical raw metals play an increasingly important role in global economic and technological development.

Secondly, reasons Singh, is the whole 'green' impetus. The rising demand for critical raw materials needed for renewable energy technologies and e-mobility is also apparent.

The COVID-19 scenario

The COVID-19 pandemic and the intermittent lockdowns have given rise to a surging demand for high tech products, such as laptops, tablets, mobile phones, as people's reliance on technology has increased enormously. "The market capitalisation of tech companies during the COVID-19 pandemic, for example, Google, Microsoft and Apple, is proof that these companies are doing well and clearly there is a demand driven reaction," says Singh.

The commodities that are largely being impacted by this insatiable appetite for high tech products, he says, are copper, nickel, graphite, manganese, vanadium and lithium. Essentially, copper is a conductor of electricity, while the other commodities are battery ingredients. These are critical minerals in the manufacture of lithium-ion batteries, which are used to power these high tech products.

While this bull within a bear scenario has most people, including those involved in the mining sector, somewhat perplexed, another primary reason for it has a lot to do with timing, says Singh. When COVID-19 first struck in China, the country went into immediate lockdown, well ahead of the rest of the world. As a result, when most other countries, and entire continents, eventually "caught up" with the need for strict lockdown responses, China found itself at the tail end of the first wave of the pandemic, and was already working intensively to restart its economy – with a particular focus on manufacturing.

"This is clearly evidenced by air quality readings taken in China in the midst of the COVID-19 crisis. While lockdowns in the rest of the world were resulting in clear blue skies, emissions in China in May 2020 were actually higher than those of the same period in 2019 – which points to a very busy manufacturing industry in that country during that time," says Singh, adding that this means that China was ramping up production to levels we have never seen before. This, he says, was a ‘fight-or-flight’ response by downstream Chinese producers, who were afraid that there could potentially be another lockdown, which could result in lost production days.

While the impact on this unique scenario of second and third COVID-19 waves across the world was still to be seen, the demand for commodities was still very evident at the end of 2020. This, says Singh, points to the likelihood that the Chinese industry is still working tirelessly to make up for lost production earlier in the last year, and is in all likelihood building significant stockpiles of finished goods to act as a cushion against the economic impact on any possible future COVID-19 lockdowns.

The green impetus

While most sectors and industries across the world found themselves suffering from a significant decline in demand, commodities were, and continue to be, highly sought after. That continued high demand has served to drive up the prices of most resources in 2020, thereby creating this apparent commodities bull market anomaly. The green revolution has been central to the growth in demand of some of the critical metals.

“The growth in demand for electric vehicles, for example, particularly in developed countries, as well as the demand for hydrogen fuel cell technology in hybrid engines, has given critical minerals like Platinum Group Metals a significant boost in terms of price,” says Singh.

The renewable energy sector is also driving demand for these minerals. Demand from renewable power generation, battery storage, electric vehicles, charging stations and related grid infrastructure is driving commodities such as copper, iron ore, manganese and PGMs (platinum, palladium, rhodium, nickel and zinc). With governments aiming for aggressive net zero emission targets in the coming decades, that means more clean electricity, a shift that’s likely to be critical metals-intensive.

To provide context, according to forecasts from BloombergNEF, the global power grid will grow by 48-million km by 2050. That’s enough to wrap around the circumference of the Earth nearly 1 200 times and equates to a doubling in copper demand to 3,6-million tonnes.

“Demand for more renewable energy is creating a massive boom in the upstream mining sector. Being a supplier to the industries that need battery ingredients has helped the mining sector, even under the toughest of economic conditions,” says Singh.

The gold sector

Apart from critical metals, the gold sector also enjoyed a good run during the pandemic, given that gold is more of a sentiment or investment commodity than a demand-driven commodity.

“For gold it’s always a bittersweet experience – when the rest of the world is in turmoil, the only positive reaction we normally see is in the price of gold. That’s because, in simple terms, investors don’t like uncertainty,” he says.

Investors move in between investment categories depending on the risk curve in the rest of the world, says Singh. For example, he says, at the start of the pandemic there were talks about the vaccine, but during the early stages of COVID-19 there was no clear indication that a vaccine could be achievable and when the vaccine uncertainty set in, the first thing that was triggered in the commodity sector was the gold price.

“We saw gold trending upwards to as high as US$2 060 per ounce – the highest it has ever been in the history of the world. It has since come down significantly since the announcement of the vaccine. As soon as the vaccine success was announced, we saw gold trending downwards, and it’s currently sitting around US$1 820 per ounce, which is still not a bad price,” he says.

For South Africa, it was a double benefit; the US dollar price of gold went up against a depreciating rand. A weak rand works to the advantage of the mining industry in South Africa, says Singh. Thus, gold companies, not only in South Africa, but on the African continent at large, were literally thriving during the pandemic.

While the shutting and suspensions of mining operations due to COVID-19 restrictions, primarily during the second quarter, resulted in the decline in global gold production in 2020, Singh believes that lost production days were offset by a sharp increase in the price.

The outlook

Despite this bull market, Singh believes mines will remain cautious, and there are three critical areas that they are likely going to focus on. Firstly, he says, it will be to take advantage of the bull market that they are currently experiencing. “Nobody knows, by any degree of accuracy, how long the bull market will last, but I think mining companies will have to be disciplined in managing their cost base,” he says.

Secondly, says Singh, mining companies will need to manage their liquidity strategically, and that’s purely a function of not knowing how long this bull market is going to last.

Thirdly, Singh believes that there will be more prudent capital allocation. Where companies would traditionally look at ‘throwing’ capital or reinvesting to expand production, they are likely to be more careful on how they spend their capital.

“There are sufficient views out there by market analysts that we are on the cusp of a commodity super cycle. The signs are there and I firmly believe that we will experience it,” says Singh.

Opportunity for Africa

The benefits of this commodity super cycle are flowing through to mining sectors across the world. And given that it is a leading supplier of many of the currently in-demand commodities, Africa is one of the main beneficiaries. This has a number of positive knock-on effects that Africa’s mining sector would do very well to capitalise on.

The first, says Singh, is that there has clearly never been a better time than now to invest in mining stocks. And African mining stocks, in particular, offer a compelling investment proposition.

Secondly, the outperformance of the mining sector on the continent creates a real opportunity for it to realign itself with the role it can, and should, be playing in terms of driving the sustainable wellbeing of Africa and her people. COVID-19 is obviously a massive crisis for what is undeniably a ‘poor’ continent. While governments across Africa are doing their utmost to fight the pandemic and protect the health of their people, funding is in short supply.

Singh believes that mines currently have that funding but they need to be willing to apply it beyond merely making the required tax and royalty contributions. If they are also willing to leverage their good financial positions to make strong corporate social investments into COVID-19 relief and support initiatives, these African mines may well emerge from the pandemic with much more than just strong balance sheets; they will also enjoy the immense benefit of positive local and international perceptions that will help to attract the investment needed to grow their operations and profitability into the future.

“There is no African mine that can afford to squander this unique opportunity to position themselves for such future growth by leveraging their healthy balance sheets to restore their reputation, enhance their appeal as a good corporate citizen, and return their licence to operate to good standing. And, hopefully, the resulting transformation of mining in Africa will allow the sector finally to realise its vast potential fully to be the engine of sustainable social development and economic growth that it can, and must, be for the continent,” concludes Singh.

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