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Zinc, Potash or diamonds - choosing the right commodity sweetener

While the diversifieds are unlikely to move their primary focus from iron ore anytime soon, there does seem to be some disagreement over where the cream is likely to come from

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GRONINGEN(Mineweb) -

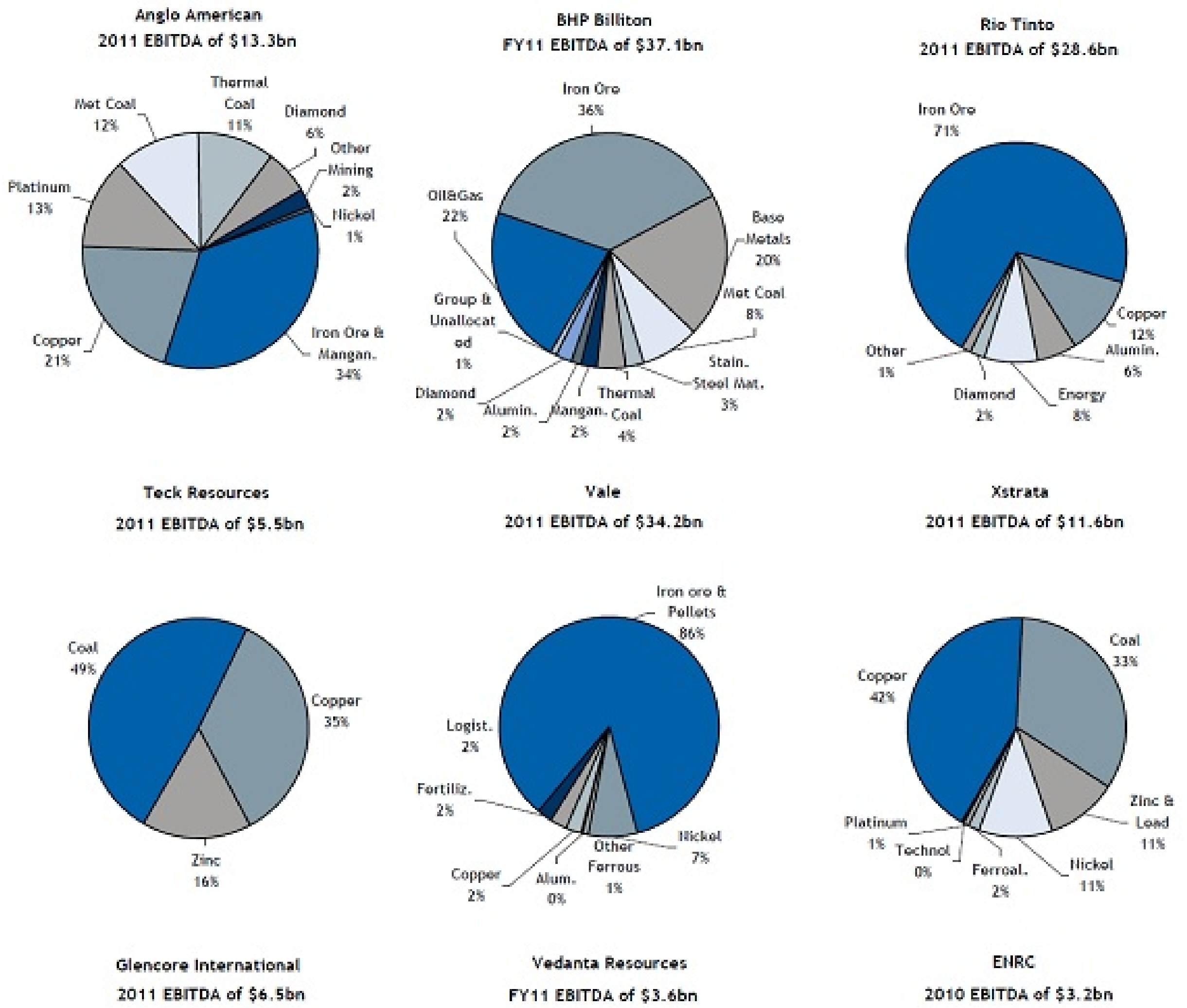
Ten years ago Alcoa was the world's most heavily capitalised mining stock.

Today, it is orders of magnitude smaller than BHP Billiton, the new holder of that crown and its peers Vale and Rio Tinto. The main reason for this is that the aluminium producer suffered the indignity of being on the wrong side of China's massive growth spurt.

Alcoa's fall is well explained in the piece [The heaviness of being Alcoa - no longer No. 1] but, the gist of the story centres around China's ability over the last decade or more to produce remarkably cheap power, primarily through steam coal, which then enabled it to produce aluminium at a much lower cost than the rest of the market.

But, while Alcoa struggled in the face of a growing China, the diversifieds with strong interests in coal and iron ore benefitted strongly from the Asian superpower's growth spurt.

As can be seen from the charts below, iron ore and, to a lesser extent coal, are the common threads that run through these companies and, while none have played a mistake free game over the last 10 years, being on the right side of the steel-making process has served them well.



Source: RBCCM

They also, unlike Alcoa, had the benefit of a much more diversified portfolio, which helped to even out earnings over time.

While it is unlikely that there will be a significant move away from their core holdings, mainly in iron ore, over the short or medium term, especially as China still needs a massive amount of steel, recent announcements by the various players suggest differing views on which commodities are likely to be best at sweetening the commodity pot going forward.

Potash

For BHP, Vale and Rio Tinto, the focus seems to be primarily on potash. BHP last year made a big play for Canada's Potash Corp and was roundly rebuffed by the Canadian government, but, CEO Marius Kloppers still has the massive Jensen project in his back pocket, into which the group has already sunk more than $1bn and it also bought Athabasca potash in 2010. Rio Tinto too has re-entered the potash business after selling its existing business to Vale in 2009.

And, as [Rick Mills pointed out recently on Mineweb] it is easy to see why, "China produces just 10% of the potash it utilizes, India's economy is 60% agricultural based and the country produces very little potash. Brazil is one of the world's breadbaskets and imports most of its potash. Both the Chinese and Indians have groups given government mandates to secure potash assets. Brazil's government is also very active in regards to its agricultural sector. There's a global macro theme - "Feeding the World" - and certainly longevity to the potash story."

Diamonds

For Anglo American perhaps by default, perhaps by design, diamonds seem to be where it's placing some of its long term bets. While both BHP Billiton and Rio are looking to get out of the game, Anglo, with its purchase of the Oppenheimer's stake in De Beers, is diving in head first.

Of course, while the precious stones only accounted for 2% of Rio and BHP's EBITDA earnings, when the Oppenheimer deal goes through Anglo will produce 25% of the world's caret output, worth roughly 37% of the global market by value.

Despite the size of the stake, it is perhaps less easy to see why one would bet big on diamonds as the sector is a very different prospect to the market that was under the firm grip of De Beers 10 years ago.
As David Hargreaves points out in his latest The Week In Mining note, "Diamonds are recognised as the ultimate luxury. Because industrial synthetics can be produced so cheaply there is no commercial fall back. As cosmetics, they are the first to fall in a recession and the last to rise in a recovery. Production cost pressures are acute, none more so than in cutting. The majority of stones are polished to less than one quarter carat weight (0.05 gram) where India has a grip on the market. It is all about cost."

That's not to say that Anglo is putting all its eggs in to, what would be a very sparkly basket. As CEO Cynthia Carroll told Mineweb in February, looking out to 2020, "In terms of our project pipeline or unapproved project pipeline, where we are different from our competitors is that we're sitting on, first of all, the best assets in the world but then the best project pipeline in terms of its diversification. So as we look forward from the standpoint of an unapproved project pipeline, which is represented by about $98bn, about a third of that actually is in copper and about 20% would be in iron ore, about 15% or so in metallurgical coal and about 15% in platinum."

Zinc

The **third horse in this race is zinc** and it is one that could well see some of the smaller diversifieds surprising at the finish line.

As **RBC Capital Markets** points out in a recent note, "**Over the coming 3 years there is only one base metal for which we see structural change in the price profile and that is zinc.** The degree to which we see pricing strength as both Century and Brunswick come off line is anyone's guess. However, **the largest zinc producers globally have already started to reposition themselves**. Vedanta has announced its restructuring to align its P&L and balance sheet. The proposed Glencore/Xstrata merger should also relevel the asset side of Glencore's balance sheet. Meanwhile Teck is directing its excess cash towards copper reinvestment while keeping an eye on its investment grade rating. **The most interesting bit of**

all this is that none of the majors are investing significantly in zinc. Reinvestment in zinc is being left to some of the smaller zinc miners like Nyrstar."

Scotiabank'sPatricia Mohr is also a fan of zinc **writing recently, "Zinc may represent the next big base metal play. Zinc will shift into 'deficit' (at latest by 2014) due to ongoing demand growth in the face of significant global mine depletion in mid-decade."**

"In 2013, the closure of the Brunswick mine in Canada, Century in Australia and Vedanta's Lisheen mine in Ireland will **shift sentiment towards zinc**, **with prices rallying in anticipation of tightening supplies**," she forecast. "In the second half of this decade, **zinc demand will be boosted** by a recovery in G7 construction activity, particularly in the USA, China could start to use more galvanized steel in the underbody of a car."
Of course there is no way to know which of these horses is likely to 'win' but with emerging markets like India and China continuing to change the course, it should be an interesting race.

About **Canada Zinc Metals Corp.** (**TSX.V : CZX ; Frankfurt: A0RAQJ**)

Canada Zinc Metals is a mineral exploration company focused on unlocking the potential of a future long life mining district in British Columbia, Canada. The Company is the dominant land holder in a world class mineral belt called the Kechika Trough which hosts in excess of 80 million tonnes of base metal resources.

Canada Zinc Metals owns a total of 77,855 hectares in 235 mineral claims which extend northwestward from the Akie property for a distance of 140 km.

The Company has outlined a NI 43-101 compliant mineral resource at its flagship Akie property, including an indicated resource of 12.7 million tonnes grading 8.4% zinc, 1.7% lead and 13.7 g/t silver (at a 5% zinc cut-off grade) and an inferred resource of 16.3 million tonnes grading 7.4% zinc, 1.3% lead and 11.6 g/t silver (at a 5% zinc cut-off grade). Using this estimate, the **deposit contains** 2.35 billion pounds of zinc, 471.8 million pounds of lead and 5.6 million ounces of silver in the indicated category, **and** 2.65 billion pounds of zinc, 482.2 million pounds of lead and 6.1 million ounces of silver in the inferred category (at 5% zinc cut-off).

The deposit remains open in all directions. Tongling Nonferrous Metals Group and Lundin Mining are significant shareholders of the Company.

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