

The Zinc Putsch is On

There was a curious juxtaposition this week that we noted on the kitcometals.com price page. While a story thundered that the World Bank was trimming global growth projections the reality of prices was very different with all base metals up for the day and Zinc up a stunning 2.5% to 93 cents, the highest level in years. It was only a couple of weeks ago crossing the 80 cts threshold and it is now a long way from the 67 cts at which it bottomed in the second half of last year.

It seems but a distant memory, but last October the obituaries were being written for Glencore, the world's largest Zinc trader with over 60% of global traded volumes. Now those fears are well in the past and Glencore, like Zinc, has arisen from its grave.

At this point in time we are looking at a nearly 50% uplift in the price in a period of a mere nine months. There is no other major metal, precious or base, that has managed such a rise in such a short amount of time in recent memory. If anything the pace has picked up in recent times. The rises are starting to look almost symmetrical with the diabolical fall from the middle of last year.



As the chart above shows, zinc has found resistance in previous years around the \$1.10 per lb level and has then retreated. However the supply situation has never been as bad in the last ten years as it is now. Heavy underinvestment has taken its toll on the pipeline of new projects, to the effect that there aren't any to speak of. Therefore the International Lead and Zinc Study Group (the leading "thinkers" on this topic) have projected a shrinkage in supply for 2016, just as prices have started to surge. Here is their projection.



It may not be a large decline but it's the second negative year in a row and reflects declining production from existing mines rather than mothballing or production cuts as a response to weak prices. We are gearing up for the long awaited perfect storm in zinc, where a modicum of demand growth encounters a chasm in the production pipeline. Though maybe we should rephrase that as there is NO production pipeline to speak of. This is the major metal where least money has been spent since 2006 in new discoveries or development than any other metal. Zinc is of course linked inextricably with the fortunes of Lead, where prices have lagged and production has also been impacted by closures of mines (and repurposing of refineries). This trend is shown in the chart below:



The year to contrast with is 2008, a bad year for every metal where the opening/closing was not even vaguely as unbalanced as now with an even greater accentuation of the closures in 2015.



Then if things couldn't get worse in 2016 we are seeing:

- Glencore has reduced zinc mine output by 500kt/yr in Australia, Kazakhstan and Peru
- Reduced output at HZL's Rampura Agucha operation in India due to technical difficulties
- CBH Resources and Perilya to reduce production at Endeavour and Broken Hill mines in Australia
- Suspension of output at Al Masane in Saudi Arabia

This trend is feeding through to LME warehouse levels as the chart below shows.



Statistics (always rubbery out of China) suggest that Shanghai stocks are not what they were either with a considerable shrinkage.

Conclusion

Added to this is the estimate for the trade study group of a 3.5% rise in demand in 2016, we can see a supply crunch that is motoring the price along nicely. With such a tailwind, and end users scrambling to write contracts to guarantee supply, I would expect the price to breach \$1 per lb in the very near future and then head steadily towards the previously impenetrable \$1.10 barrier. As they said on old maps "Beyond here there be monsters". What will happen is that no one in the mining industry shall stir from their behinds until prices breach \$1.20 and even then they would rightly (on previous bad experience) want to see them hold there before getting over-excited about launching projects. This means an ever-worsening supply situation. For existing producers this will be a deeply profitable and long overdue development. The mood will fire up the hunt for juniors that have respectable projects. Many have been on the backburner so long they have melted onto the pot... With an investor universe largely clueless on zinc's dynamics this will very likely degenerate into a blind rush in the direction of the best promoted offerings. Ever was it thus, but still zinc above \$1.20 will be exciting territory and well worth positioning oneself for now.