Is there Life After Glencore?

"Everyone loves a winner"… or is it that "Everyone loves an underdog". Ivan Glasenberg has managed to be unloved either as a winner or as a loser. Frankly, the long-time chief of Glencore has won no friends over the years. Straddling two industries, commodities and mining where big egos are a common denominator, Glasenberg has managed to rub almost everyone up the wrong way. Now with his unsinkable Glencore having ploughed into an iceberg of its own devising, the question is "would you throw this man a life ring if he was drowning?".

It sounds rather harsh but the takeover of Xstrata was the last straw. Previously he had been just a hard-nosed trader out to get the best deal and build his company into the undisputable 800-lb gorilla in the space. His symbiotic relationship with Xstrata has been somewhat arm's length so the marketplace had cognitive dissonance in that it "liked" Xstrata while it feared and respected Glencore. Putting the two together in a most unhappy merger made the corporate suite of Xstrata resemble the aftermath of the *Shower Scene* from *Pyscho*. Veteran managers, known and famed across the mining industry, were bundled out the door with unseemly haste.

Then the started rattling its cage about going after Rio Tinto as if such a merger was its birthright. Fortunately higher powers stomped on that deal. If the RTZ takeover had occurred, with the massive amount of debt that would have been needed to consummate it, then the bankruptcy of Glencore would already have happened. It was a very dumb deal in an industry in which there is much competition for that title. Beyond financial fecklessness, everybody in the industry knew that such a deal would also have involved massive bloodletting. The whole industry dodged a bullet there.

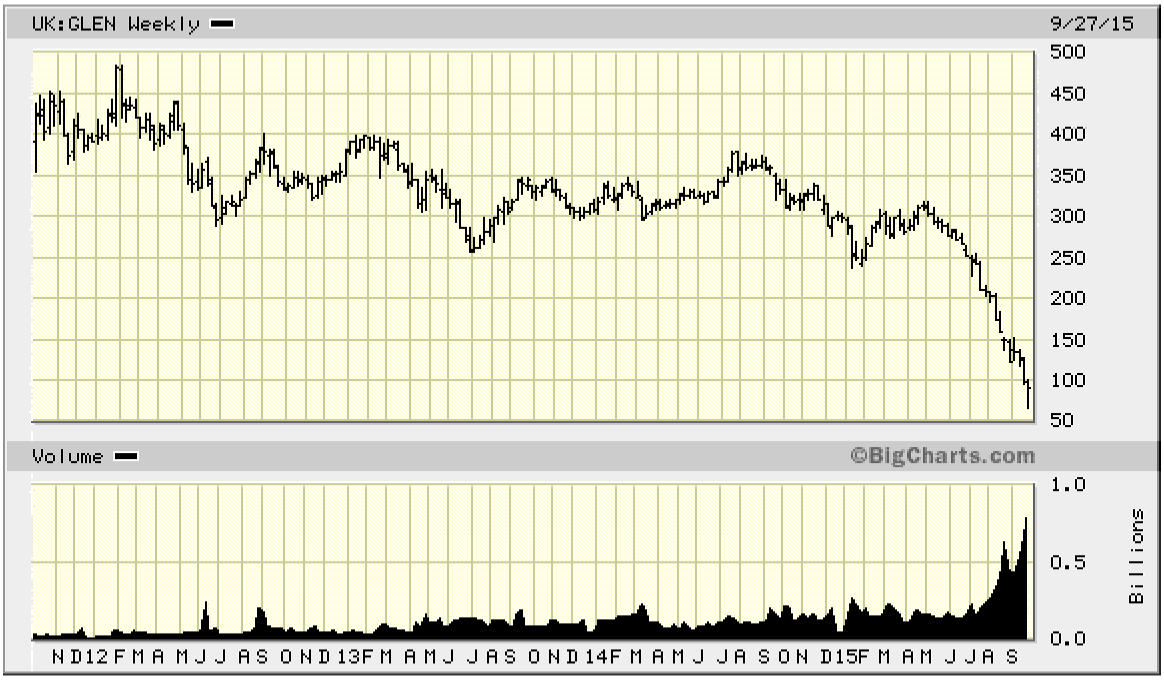
Then there was the sad but almost unnoticed case of Donner Metals, the junior partner to Xstrata in the Bracemac McLeod Zinc mine. Donner was treated by Glencore like a horde of Cossacks would treat a blushing virgin. The downfall of Glencore may be little consolation for shareholders there but they are certainly entitled to a liberal dose of *Schadenfreude*.

Fins in the Water

With Glencore being daily battered by the rough waves of global financial markets its market share in many metals is up for grabs. Certainly it has contracts with many miners that require them to keep selling to it, but there is also the discretionary business that is done by many miners, the type of business that gave the trader its 68% share in the global zinc market for instance. After the bad experience of REFCO and father back Metallgesellschaft, one can bet that miners that are not tied down by contracts to sell specified amounts will already be ringing the phones off the hook at the other traders looking for bids so they can diversify (let’s face it – lower) their exposure to Glencore.

Lead & Zinc traders, for instance, at Trafigura and Traxys must have had a bumper week. They would be the most obvious winners from a Glencore stumble. Noble and Wogen would benefit in other metals and then there is the massive Vitol, which jungle drums tell us has long harboured ambitions to match its heft in oil & gas with similar weightiness in metals trading. It should not be forgotten that Glencore itself was the Phoenix that arose from the ashes of the Marc Rich empire. As we have noted before the principal assets of trading houses pick themselves up at 5pm every afternoon and head out of the building. If they did not come back one day (due to the firm hitting the rocks) and instead set up operations across the road they would not have all their former business to play with, but certainly they would have a lot of it. What's more they would have whatever proceeds they had cashed out at the IPO, and in the after-market as seed capital for Son of Glencore. This means that the demise of Glencore, or any other trader for that matter, would make only limited rippling of the metals markets and mining sphere millponds.

There are enough other traders out there for the business of the stricken giant to be divided up and redirected with days let alone weeks.



White Knights in Short Supply

If fate does claim Glencore, it will not be end of the world. The Swiss government certainly won't be stepping in to save it. Tax havens have their advantages up to a point. We cannot see any other potential takers. Traders can be poached easily from a stricken trader and major miners would not want it because the overlap with their existing mines would precipitate hefty bargain basement disposals to satisfy competition authorities meanwhile the trading part of the business would be walking out the door.

Revenge is a Dish Best Eaten Cold

As for the mining assets, Mick Davis must be salivating at the thought. Maybe this outcome was the method in his madness in not splurging the cash pile he has at X2. If he stands a chance at recuperating big chunks of his old empire then funders would probably be lining up to put more cash in his warchest.

The question is whether he would want all of his former vehicle’s assets. At the time of the takeover of Xstrata it was a major producer of coal (and the world’s largest exporter of thermal coal), copper, nickel, primary vanadium and zinc and the world’s largest producer of ferrochrome. It had operations in 19 countries across Africa, Asia, Australasia, Europe, North America and South America. A few assets were sold off (most notably the Las Bambas project in Peru that went to MMG). Frankly if offered the entity we would pass on the coal which is not passing a happy moment and does not have the turnaround prospects of the other metals. As mining assets are a buyer’s market, X2 could afford to play the choosy buyer and pick and choose which of these it can afford with its current (or prospective) warchest.

Quite a number of the assets are worth substantially less now that prices have declined from the levels they were when Glencore grabbed Xstrata and beyond that several of the prime Zinc assets are reaching the end of their mine-lives. There is scope to push a hard bargain as it is far from being a seller’s market at the moment. Competing offers would be few and far between.

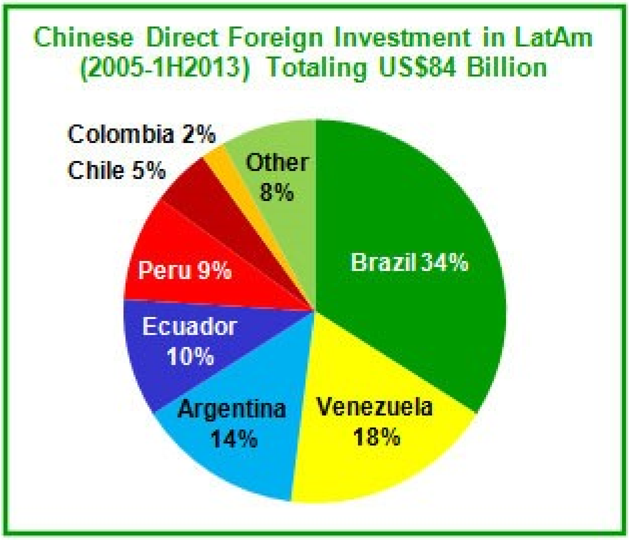
Conclusion

What goes around comes around. In many ways, pure trading houses are a *will-of-the-wisp* with little in the way of profit generating assets. Some have backfilled with upstream assets (i.e. mines) in recent years but done so at the cost of enormous debt burdens which are now mismatched with the beaten down value of mineral properties. The trading business is largely goodwill so the creditors are looking at a whole lot of nothing as security for their loans. Some have said that the demise of Glencore is “bad news” for miners but we are not sure that that is true. Its bad news for those that extended credit and equity holders of the stock, but that does not necessarily have any overlap with the mining community.

Great names come and great names go. Some generate tears when they depart. Some merely a shrug. Remember Donner Metals…. Karma is a bitch..

South America is the 2nd largest destination for Chinese direct foreign investment

Trade and foreign direct investment (FDI) relations between China and Latin America and the Caribbean are growing in the past 15 years by a factor of 25 according to the Economic Commission for Latin America and the Caribbean (ECLAC). The majority of Chinese FDI is directed towards the banking sectors of the Cayman Islands and the British Virgin Islands, but Chinese companies have increasingly been targeting the Latin American natural resource and industrial sector. China has targeted several countries but Brazil and Argentina, which are rich in land, as well as mineral resources, are among the countries to experience the largest trade increase. U3O8 Corp (TSXV: UWE | OTCQX: UWEFF), a Canadian company developing uranium, phosphate and vanadium deposits in Colombia and Argentina could benefit from this rising phenomenon.



In the past nine years, China has invested about US$ 10 billion in Argentina. Estimates suggest that China could become the main importer of South American goods (Brazil, Chile, and Peru) by 2030, surpassing the United States. The region is preparing for the shift through infrastructure projects that will facilitate trade with China: largely, this means more ports and links to ports. The Chubut province in Argentina will likely build a railway linking it to Chilean ports, reducing distances to ports in China. It so happens, that U3O8 Corp (TSXV: UWE) is developing a uranium/vanadium project in the Laguna Salada district, in the Chubut province of Argentina.

Uranium is another resource that China needs and in this respect the combination of China’s rapidly increasing investment and trade flow with South America, particularly in energy and agriculture, could benefit U3O8 Corp, which is nearing the production stage at its low-cost uranium deposit. U3O8 Corp. is active in the uranium space in Argentina because the country has adopted policies that favor the development of nuclear energy and resources. Argentina's has an advanced nuclear industry that started in the 1950's. Argentina has even developed unique modular reactors – the first of which is being built now. U3O8 Corp also owns the Berlin deposit in Colombia which is close to production stage with resources in uranium, vanadium, phosphate and rare earths. Therefore, U3O8 Corp is in a position to both supply Argentina's growing nuclear appetite (which includes a nuclear powered shipping fleet) and take advantage of growing Latin American trade opportunities with China with which Argentina has a nuclear co-operation agreement.

Chinese investors are drawn to Latin America as they search for new markets; they want to establish production facilities in the region to help Chinese enterprises reduce trade conflicts (Many Latin American countries have adopted anti-dumping measures against products made in China) because they find it more difficult to do the same in the so-called fully developed countries. Moreover, Latin America is eager to give China access to energy and natural resources. Naturally, given the size of its economy and population, China sees Brazil as the big 'prize' location and the vast majority of Chinese investment has targeted its natural resources, particularly oil and gas. China has also taken advantage of the vacuum left by the absence of North American players in Venezuela to engage that country's electricity, construction, food, technology and even satellites sectors. China maintains important economic relations with other countries such as Mexico, Chile, Peru, Ecuador and Cuba. In fact, while Brazil may be the main target now, historically, Peru has been the largest Latin American recipient of Chinese investment in the mining sector.

In March of this year, Chinese investment has intensified further as large conglomerates have been targeting the Latin American agricultural sector. Chinese state-owned COFCO, a huge conglomerate responsible for essentially feeding millions of Chinese citizens, has taken over Noble, the largest private trading company (energy, metals and agricultural products) in Asia. One of the most important factors motivating this transaction is the fact that Noble has many investments in Brazil and Argentina, which has now given COFCO, control of Noble's South American warehouses of sugar, cereals and oil seeds (as well as cotton, coffee and cocoa from Africa or Asia).

This is merely the beginning. Beijing has given up subsidizing Chinese agriculture by using fixed procurement mechanisms for such staples as rice, soy or cotton as in the past. Moreover, Chinese soil has been degrading rapidly and this will make China ever more addicted to other countries for food. The Chinese are already the largest importer of soybeans in the world and becoming the largest importers of corn to feed their livestock, and for the past three years they have been net importers of rice. China consumes 20% of global food supply, but has only 9% of the world's acreage under cultivation.

China, therefore, needs to find alternative lands to secure food supplies. In this regard, Brazil, offers 500 million acres of arable land and it is the world's third largest market for fertilizer for which demand is increasing. Currently, Brazil has to import about half of its phosphate needs and South American phosphate and potash producers will be in a position to benefit from China's agricultural 'invasion'. Fertilizer use in Brazil has risen by 70% over the past 15 years and the government is very keen on stimulating phosphates and potash mining, which could presumably include an increase of royalties for mining companies. Brazil produces many fertilizer intensive crops – soya, maize and sugar cane (some 80% of total agricultural output) – that are necessary for food production and for biofuel, which is an important alternative fuel in South America. These crops respond very well to phosphate based fertilizer. Brazilian soil needs external nutrients in the form of mineral fertilizers.

Here is a quicklink to our latest interview with Richard Spencer of U3O8 Corp.: