Investors beware!

Production costs should not be your only investment guide

Investors who are keen on investing in a particular commodity should not assume that, if a company's cost of production is lower than the commodity price, it is a profitable venture.

Such was the case with many investors in the platinum and gold sector historically, and investors who continue to make the same assumption about other commodities do so at their peril.

Venmyn Deloitte MD Andy Clay warns that investors into the copper sector, for instance, must identify the $824 cash cost curves of producers as favourable when evaluated against the copper price.

Total cash costs for copper as a primary product are usually quoted (as measured in $/lb) by: 74.5c/lb for Freeport McMoRan Inc's Chino SX-EW project, in the US, through to 330.4c/lb for Aditya Birla Minerals Ltd's Nifty Project, in Australia. This is a good example of a host of producers' cash costs between these two values, as can be seen in the diagram below.

However, while the potential total cash costs for copper include labour, energy, reagents and other on-site and off-site costs, they do not include exploration charges, depreciation, capital, and the cost of debt. This was the same in gold until Clive Davis exploited that myth and gold companies started to report 'management charges', which included everything, rather than the 'all-in-sustaining-costs' that he had previously.

"While many investors, into the platinum and gold sectors found out this principle too late, it is hoped that investors in other commodities, including copper, let this principle direct their investments," Clay adds.

"The world cannot do anything without copper but, until low-grade deposits are taken out of the market, and a rational approach to supply and demand is established, the market cannot recover," he says.

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Kind regards,
Andy Clay

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The current copper price is $2.86/lb, after showing a marked downward price trend since February 2011 (as illustrated in the Net Bridge copper price graph below), and this has suggested the lost place, that at least some copper producers are profitable (as shown in the diagram below).

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Also read:

Cape Town and Johannesburg Mining Events in 2016

Venmyn Deloitte's Andy Clay, Tarryn Orford and Chris de Vries will be arranging meetings at the Waterfront in Cape Town, South Africa, during the Mining Indaba that runs from the 8th to the 11th February 2016. Please see www.vdm.deloitte.co.za to arrange to meet with them.

Venmyn Deloitte is hosting an after-work drinks party in March 2016 to publicise its metal accounting and environmental sustainability service line. If you are keen on exploring these topics, please email venmyninfo@deloitte.com and receive an invitation to attend this event in Johannesburg, South Africa.

Deloitte is pleased to announce the launch of Venmyn Deloitte (Pty) Ltd. In its eighth year, this edition explores not only familiar themes, but also new areas which miners must take into account, in order to navigate an increasingly uncertain future. Once again, Deloitte draws on the experience of Deloitte's global mining professionals to help identify the questions miners must ask—and suggests answers.

Kind regards,
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