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Markets will always outwit miners

Markets are smart, possibly too smart for a mining community constantly driven by long evident errors of judgement.

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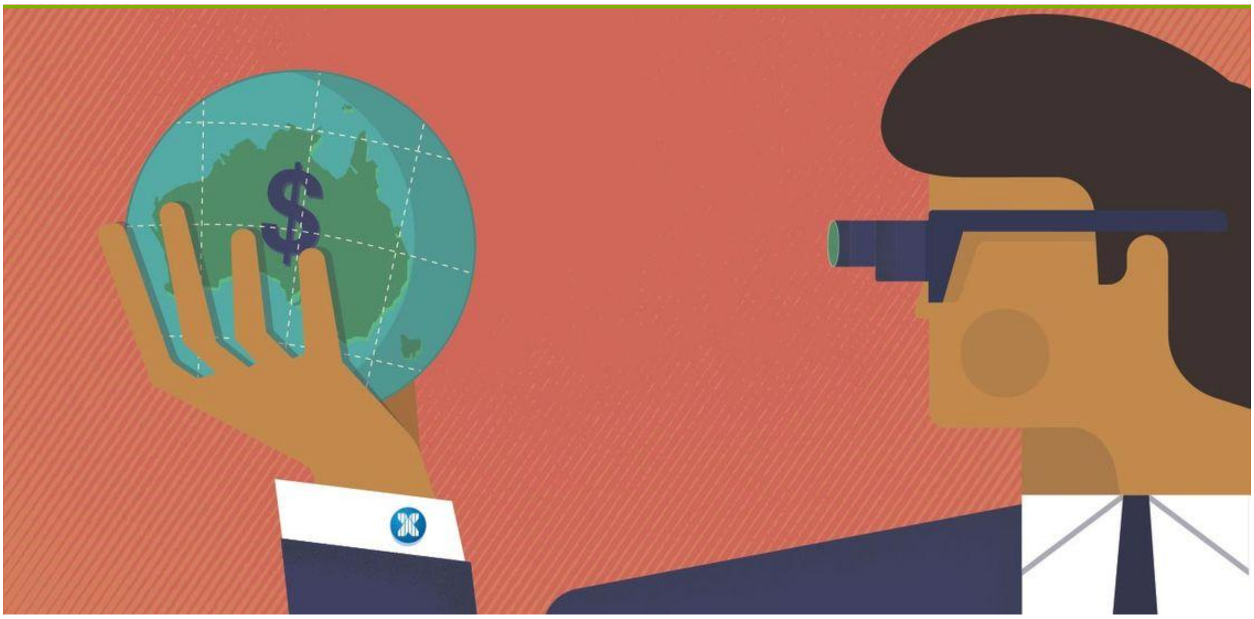

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The idealised goal of a budding miner is to create a project that is profitable throughout a largely unknowable future. The bigger and better a project, the less likely will its promoters comprehend the full array of conditions through which it must survive. They will simply hope that good times, impossible to predict, outweigh times of inevitably mediocre or poor results.

Despite their ultimate reliance on the future, mineral explorers are almost wholly engrossed in the present. Today's assay will dictate how they proceed tomorrow. Tomorrow's efforts will depend on having solicited sufficient funds yesterday.

Narratives about the future used to support funding efforts will depend overwhelmingly on today's understanding of what the future will resemble. If explorers have a different view of the future than the prevailing consensus, they are better off keeping it to themselves.

New World Cobalt illustrates the challenges and temptations facing a company trying to bridge the pressures of present circumstances and an unknown future.

The company acquired exploration tenements in Idaho and Nevada in late 2017 "to meet surging demand for cobalt from the US and European auto industries". Previously known as Longford Resources, it had been primarily interested in finding zinc in Ireland until then.

New World Cobalt was not alone in having the battery metals theme dictate a decision to dump one strategic direction in favour of another for which funding, at least on face value at the time, seemed easier to obtain.

The flirtation with battery metals did not last long. By April 2019, the company had jettisoned the energy storage narrative in favour of copper-gold prospects in New Mexico. In May, company chief executive Michael Haynes told investors the fall in the cobalt price during 2018 had dictated his revised view of how to position the company for the 2020s and beyond.

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New World Cobalt is hardly an extreme example. A strategically promiscuous mining-industry culture puts far greater emphasis on keeping the doors to the executive suite open than meeting emphatically stated goals based on unambiguously proclaimed narratives about the future.

Miners will frequently profess irritation at having their plans thwarted by unsympathetic markets populated by unthinking investors. Analysts abet their misunderstanding of how markets work with research purportedly showing how much higher prices must climb to validate development. It is only a matter of time.

In reality, prices may only fleetingly cover costs over the duration of a project life and rarely provide an adequate return on invested capital. Developments still proceed. Creating the necessary expectation about the future through a seemingly compelling narrative is often enough.

Sometimes, the optimistic narrative loses momentum, leaving projects marooned in a development no man's land until industrial needs intensify. Tin in Morocco, uranium in Namibia and zinc in Greenland are all examples of a devilishly cunning market luring gullible miners on promises of never-realised rewards to help kick start development efforts.

No metal-demand narrative has appeared more compelling than the needs arising from transport electrification and growth in mobile energy storage capacity. Any vestige of dissent is almost impossible to discern. And, yet, the fortunes of miners like Haynes are as bleak as ever.

New World Cobalt, along with dozens of others, have been manipulated by a clever market. The invisible hand has worked. New targets, resources, reserves and feasible projects that would have otherwise gone unrecognised have been defined in a short space of time. That job done, prices can fall back to where they had been before Haynes and like-minded investors were excited into action.

Prices may yet need another spurt down the track but, if the market works, prices will move just enough to excite emotions but never by enough to sustain a profitable future.

This predicament is not peculiar to modern markets or a product of heightened cyclicality. Famed British economist John Maynard Keynes provided an insight into the workings of today's mining industry 80 years ago.

In the course of rebutting criticism about his revolutionary views on the conduct of macroeconomic policy (The General Theory of Employment, The Quarterly Journal of Economics, Vol 51, February 1937), Keynes characterised attempts to forecast the price of copper, among other future events, as having "no scientific basis on which to form any calculable probability whatever".

The near impossibility of the task, Keynes observed, does not deter "practical men to do our best to overlook this awkward fact and to behave exactly as we should if we had behind us ... a series of prospective advantages and disadvantages, each multiplied by the appropriate probability, waiting to be summed".

Keynes described the three most-used techniques, all of which should resonate with the modern mining executive, "which saves our faces as rational, economic men".

The first technique used to convey rationality is to assume that the present is a better guide to the future than it has ever been before.

The second is to assume that the existing state of opinion about prices or output is based on a correct summing up of future prospects.

The third technique used to add cogency to a narrative about the future is to have it conform to the views of the majority or the average.

Modern corporate presentations commonly embrace all three techniques to strengthen their pitches to investors. The most excited executives will cite recently high prices, projected market deficits without regard to the track record of the analysts behind the summation of future prospects and the universality of views about what will happen.

Theorising about the future using "so flimsy a foundation", Keynes asserted, risks sudden and violent changes.

Haynes, among many others, might have been caught by surprise by unsupportive market moves but Keynes had warned him eight decades earlier that "all these pretty, polite techniques, made for a well-panelled board room and a nicely regulated market, are liable to collapse".

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