Lithium brain fade

Lithium is causing confused thinking, delusions, memory loss and hallucinations among miners in an ironic reversal of its role as a psychiatric medication.

John Robertson* | 27 Jul 2016 | 20:11 | Opinion

Lithium is causing some questionable behaviour and decision-making among industry leaders

Speaking recently to a meeting of investors, Kidman Resources chief executive Martin Donohue found difficulty committing to a coherent business strategy despite early successes in its gold mining initiatives. Kidman Resources displays the symptoms of a confused corporate personality arising from an exposure to lithium.

Kidman had adopted an increasingly prevalent gold mining strategy involving the purchase of historical workings in Western Australia. The low capital model had allowed a rapid start at its Burbanks gold mine acquired in June 2015.

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The recent purchase of its Mount Holland property near Southern Cross from administrators will enable another speedy move toward production on already granted mining leases.

The move on gold comes after the company had decided to discard the base metal properties in New South Wales and the Northern Territory, which had underpinned its ASX listing in 2011.

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The switch from base metals to gold was understandable enough. A good bullion price, low capital needs and easy marketing gave it the edge over most other forms of mining.

Making clear to investors that one course would be abandoned in favour of another suggested a clear strategic pathway.

Barely 12 months into the gold-focused strategy, the company has re-assayed five RC holes at the Mount Holland prospect with an eye on lithium-bearing pegmatite occurrences near its historical mine workings.

"The psychological biases within investment banks, and the business pressures requiring the cultivation of company relationships, have consistently overwhelmed the quality of their thinking"

Assay results have highlighted a lithium-endowed pegmatite possibly up to 50m thick.

The broader prospect hosts at least five mineralised pegmatite bodies with the company now planning follow-up holes to confirm the thickness and the lithium grade.

Unsurprisingly, in the current wave of lithium-caused mania, the Kidman Resources share price leapt 120% on the news of its lithium connections.

Many companies floundering in obscurity will have jealously coveted Kidman's market good fortune but the company's investment challenge becomes obvious when Donohue has to explain a new and still ill-defined strategy to investors.

In short, there is confusion and indecision about whether the company is a gold miner or a lithium prospector.

Silver City Resources is another company confronting this form of corporate split personality.

Silver City, as the name implies, has exploration properties around Broken Hill.

Chief executive Chris Torrey had outlined a credible plan to tap zinc-silver mineralisation close to existing processing facilities enabling a low-capital route to quick production.

In its March quarter activities report, Silver City never mentioned lithium. There seemed no doubt from the way it presented itself about the strategic direction of the company.

In mid-May, after the company's surprise announcement that it would begin assessing the lithium potential of its tenements, its market value spiked 150%.

Now, when the company presents, "the metal of the future" is given priority treatment with the first meaningful mention of zinc occurring on page 19 of the company's 25 page presentation document.

Silver City directors might be right. Outcropping pegmatites are widely found on the company's tenements. Broken Hill may yet prove a prolific source of lithium.

Unfortunately, Silver City no longer has a clear-cut investment proposition. Lithium has created in Silver City the mining industry equivalent of a multiple-personality disorder.

Executives trying to push multiple investment propositions risk appearing wishy-washy as they dart from one idea to another. Investors are left wondering where their true priorities lie.

Multiple projects are particularly problematic for management groups without a track record to demonstrate their multi-tasking abilities.

Multiple projects, where choices must be made about the allocation of capital, often invite the noisiest shareholders to become overly influential about the direction of the company.

Giving up on a near-term production option in favour of longer-term more capital-intensive developments is another source of risk in a highly capital-constrained market.

Even among well-established companies in the industry, lithium is playing havoc with clear thinking.

Orocobre's investment prospects, according to chief executive Richard Seville, rest on sustaining a high-margin business centred on its recently constructed Olaroz lithium carbonate plant in Argentina.

Seville has succumbed to what Nobel Prize winning psychologist Daniel Kahneman described in a 1974 paper written with Amos Tversky (Judgment under Uncertainty: Heuristics and Biases; Science, Vol 185 pp.1,124-1,131) as the use of heuristic principles that sometimes lead to severe and systematic errors.

Among a range of mistaken approaches to decision making, Kahneman and Tversky described a strong tendency for people's expectations to be dominated by their most recent experiences.

Commodity price forecasts from investment banks are among some of the most common examples of the phenomenon.

In December 2014, for example, Deutsche Bank was advocating a long-term oil price of US$90/bbl. The same institution had put forward $80 per tonne as the long-term iron ore price in January 2013.

Others' forecasts ranged as high as $150/t, at the same time. In December 2013, a consensus of 16 investment firms was pointing to a $175/t coking coal price for the longer term.

Investment firms have historically shown strong and systematic upward biases in their forecasting despite well-documented tendencies in commodity markets for prices to revert to costs of production.

The psychological biases within investment banks, and the business pressures requiring the cultivation of company relationships, have consistently overwhelmed the quality of their thinking.

Last week, Seville depicted lithium prices hovering around $10,000/t indefinitely, roughly where they have been trading recently and up to five times higher than his costs of production. Seville used forecasts from investment banks, including Deutsche Bank, to support his conclusion.

Seville was perversely using the output of groups with demonstrably persistent biases in their forecasts to establish the credibility of his investment case.

Saying that lithium will not follow the paths of oil, coal and iron ore is just another sign of the debilitating effects lithium is having on the mental state of the mining industry.

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