Why Glencore is uninvestable

Perspectives: March 20th, 2020

Glencore is a large listed company. It is investable in a narrow sense that, if I wanted to, I could spend money on it by buying the shares.

I consider it uninvestable for the following four key reasons pulled together.

Starting with its leadership, the regulatory investigations into its business practices and a director of a subsidiary being barred from serving as a director in a leading developed economy raises a serious question mark.

Secondly, it derives approximately 60% of its profits from the production of thermal coal, copper and zinc. All these commodity prices are falling rapidly, for understandable reasons given the global economy right now.

Thirdly, it derives approximately 30% of its profits from something called 'marketing'. This is a rather opaque source of profits and I have never been able to make much sense of this division nor met anyone able to, or figure out how these profits are derived, how much risk is taken on and how sustainable they are. To me it appears the result of trading activities with the company's capital. With commodity prices falling so unexpectedly and rapidly, this source of profits can quickly become a source of losses, as the evidence shows has happened to them in previous downturns.

Lastly, like many other global companies, Glencore has been spending lots of capital on buying back its own (overvalued) shares in the past few years, in the process ratcheting up its balance sheet net debt levels. Despite operating profits declining by 80% and being loss-making in the 2019 financial year they also persisted with paying dividends at the same level as in 2018, essentially paying those dividends by increasing debt.

Taken together, the combination of a geared balance sheet with falling profits, a question mark on leadership and a lack of transparency leads me to a conclusion Glencore is currently uninvestable.

Our work continues...

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