



Insigneo Weekly Dispatch

# Lithium: A Hot Topic

- What are the current supply and demand dynamics of lithium?
- How could an investor get exposure to this industry?

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## Lithium: A Hot Topic

The topic of Lithium is a hot one. Not only from an industry perspective, but also in terms of investor interest. There are several vehicles through which an investor could get exposure to this theme. However, it is important to spend some time on the dynamics of the lithium industry before we delve into any potential investments ideas.

As we can imagine, the demand for lithium has increased over the past decade, as demand for Electric Vehicles has meaningfully grown around the world. Demand has increased significantly in North America and Asia, particularly in the United States and China. As would be expected, this has driven prices of lithium through the roof. In fact, according to Bloomberg, prices for some of the key chemical components needed to produce lithium are currently 4-6 times more expensive than they were over the past 5 years.

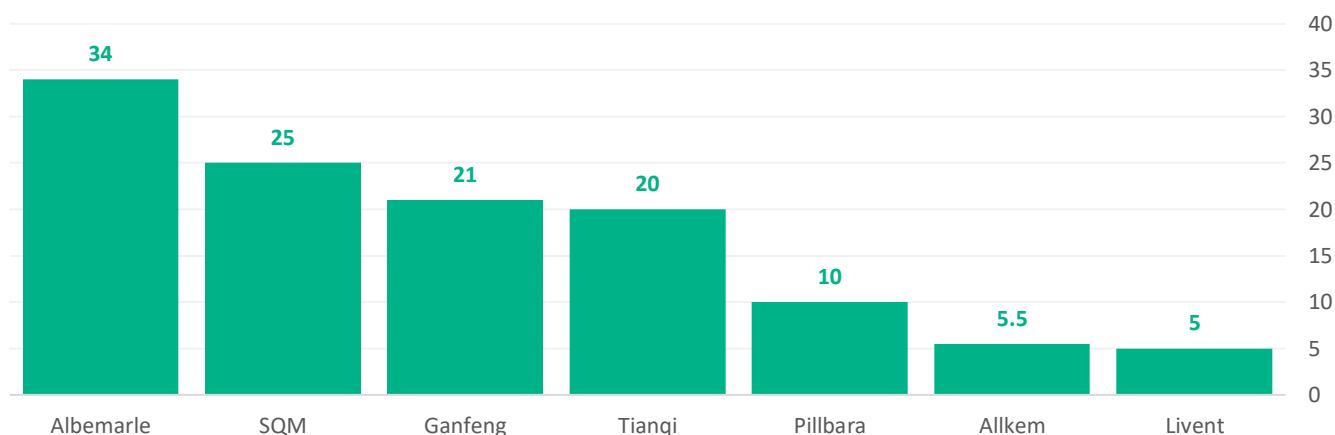
The basic raw materials needed for the creation of lithium generally come from two sources: a mineral rock called Spodumene and a salt-based brine. As of 2020, 65% of lithium production stemmed from Spodumene, 33% from Brine, and 2% from other sources. Most of the production of Spodumene is in Australia, while brine production is mostly found in the salt flats of Chile and Argentina. These raw materials must then be processed into lithium carbonate and lithium hydroxide, the chemicals that are used to create batteries. Approximately, 65% of this processing takes place in China.

As we can see, the production of battery-grade lithium is rather complicated, involving different players across different countries. Consequently, increasing the supply of lithium production capacity is something that takes time, which also helps keep prices elevated.

In response to high lithium prices, producers have started increasing production capacity in anticipation of higher demand for the product over time. However, this dynamic has divided Wall Street, as some analysts believe that higher supply will inevitably derail high prices, while others think that rising demand will be able to absorb increasing supply. In our view, prices could remain volatile, affected by events such as the recent end of subsidies for electric vehicles in China. **However, the supply/demand dynamics for lithium are still favorable, and although prices could come down temporarily from elevated levels, their trend is most likely to continue to point upward over the long-term.**

Given the favorable long-term outlook for the industry, investors looking to gain exposure to lithium could do so through ETFs or through individual equities. Within the ETF space, investors can choose to get exposure solely through producers of lithium, or through both producers and consumers of the product. On the producer side, the Sprott Lithium Miners ETF (LITP) tracks the NASDAQ Sprott Lithium market index. However, as it is concentrated solely on lithium producing companies, this ETF can experience a high degree of volatility. A more diversified way to get exposure could be through ETFs like the Global X Lithium and Battery Technology ETF (LIT), its UCITS counterpart (LITU), or the Amplify Lithium & Battery Technology ETF (BATT). These ETFs have a nearly 50/50 split between producers and consumers, having exposure not only to miners, but also to companies in industries like automobile, electronics and telecommunications that are end markets for lithium.

**Largest Global Lithium Producers by Market Cap (in Billions \$)**



Source: Bloomberg Intelligence, Insigneo (As of 2/16/23)

Investors with higher risk tolerances that would rather get exposure to this industry through individual equities could consider companies such as Albemarle Corp. (ALB) and Sociedad Química y Minera de Chile (SQM). There are many producers of lithium around the globe, but as we can see on the chart below, only a few that are large enough (on a market cap basis) to be meaningful players in the industry. ALB and SQM are both diversified specialty chemical companies that are, in essence, taking the strong profits and cash flows generated by their legacy business lines and using these to invest in and expand their lithium operations. With operations around the world, they are dominant players in the lithium production industry. Allkem Ltd. (OROCF) and Livent Corp. (LTHM) could also be potential considerations. Both companies are “pure play”, vertically integrated lithium producers. However, unlike ALB and SQM above, they do not have other business lines that can provide a certain degree of diversification for their operations. As a result, their earnings, and stock prices, can exhibit even higher degrees of volatility in response to changes in lithium prices.

It is important to keep in mind that the ETFs and individual equities mentioned here can exhibit high degrees of volatility and are not suitable for every investor. These investments are best considered on a case-by-case basis, based on a particular investor’s willingness and ability to tolerate risk. If you need more information or would like to discuss these potential ideas in more detail, please do not hesitate to contact the Insigneo Research Team.



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