



## Did Cameco Just Prove Miracles Exist?

### Description

Do you believe in miracles? No, I am not referring to the Toronto Maple Leafs hot start to this year's NHL season. I'm talking about the third quarter earnings recently released by **Cameco Corporation** (TSX: CCO, NYSE: CCJ).

Cameco reported third quarter adjusted earnings of \$208 million representing a 324% increase over the same period last year. Adjusted earnings per share were up 342% to \$0.53 per share, easily blowing past consensus analyst estimates of \$0.17 per share which were actually lowered from \$0.19 per share in the week leading up to the release. Revenues were up 102% to \$597 million which topped consensus estimates by \$34 million.

Like many analysts, I did not see this positive quarter coming. A few days before the announcement, I previewed Cameco earnings. As was obvious by my title, [Don't Expect any Miracles when Cameco Reports Third Quarter Earnings this Week](#), I did not expect this to be the break out quarter turned in by the company. Crow anyone?

### The making of the miracle

So how did they do it? According to management, the improvement was primarily a result of lower exploration costs due to a restructuring program initiated earlier in the year combined with increased sales from the uranium unit as a result of increased volumes and higher realized prices. The company saw a 63% jump in the sales volume of uranium to 8.5 million pounds while production increased 9% to 5.8 million pounds.

Cameco also saw a 15% increase in the average realized price supported in large part by the company's contracting strategy which continued to deliver average prices above the current uranium spot price. On the cost side of the ledger, the company saw a 9% drop in the average cost of sales of uranium thanks to lower cost opportunities for purchased material and lower exploration costs for produced material.

When you put together substantially increased sales volume combined with increased realized prices and lower costs, you have the making of a great quarter.

### **From miracle to sustainable**

The question now on the minds of the investment community: Is this sustainable? Management was asked this question head on and without being overly specific the company's CFO stated, "if you just want to focus on the produced material, we see good contribution from costs, performance, as well as from higher production." This should bode well for upcoming quarters unless there is a material change that would impact the cost structure.

In addition to apparent internal factors putting this quarter and potentially future quarters in the headlines, there are also some external factors that could brighten the outlook for Cameco. According to company CEO, Timothy Gitzel, Japan currently has approximately five utilities comprising of fourteen reactors that are being reviewed for a potential restart. Mr. Gitzel went on to point out that there are 69 reactors under construction today of which 30 are located in China. China is not alone; India, South Korea and Russia also have aggressive build programs. Management expects over 90 net new reactors to be added by the year 2022.

### **Some good things never last**

One program that paid dividends this quarter was the contracting strategy. This allowed the company to sell material at prices above spot. However, the contracts are a mix of both fixed and market-related contracts with a target ratio of 40:60, respectively. According to management, a large number of market-related contracts were delivered during the first three quarters of the year making future deliveries less sensitive to market prices for the remainder of 2013. This should support solid earnings in the fourth quarter. However, based on comments and illustrations by management, continued weakness in uranium prices will start to have a negative impact on expected realized prices in 2014 and beyond.

Another item that struck me was the reduction in cost at the company's 31.6% owned partnership producing electricity from four reactors at the Bruce Power site in Ontario. Operating costs dropped \$50 million or 21% due primarily to an adjustment to supplemental lease charges during the quarter that were originally occurred in the second quarter of 2012. Also adding to the reduction were deferred maintenance costs. Based on historical data, operating costs at this level are most likely not sustainable.

### **Final thoughts**

My hat is off to management for staying on top of their game in a difficult environment for the uranium industry. The company initiated a restructuring program to cut production costs that is now bearing fruit and had the foresight to lock in a contract strategy producing sales well above the current spot price for uranium.

This type of quarter will certainly instill investor confidence in management. That alone should put some short-term support under the stock. However, in today's world of "what have you done for me lately?" management will need to stay on their game. Any continued weakness in the uranium market

will certainly make that task more difficult.

However, it does appear the outlook for the industry is starting to look brighter as the disaster in Japan begins to fade into the history books and idled reactors are brought back online. In addition, the United Kingdom recently surprised many when the government approved the construction of the country's first new nuclear power station in 20 years.

For the most part, it appears management did a very good job preparing the company for a difficult market. In light of this performance, investors may be well served digging deeper into Cameco as a way to play a uranium market that should recover down the road. In the meantime, I will be chewing on my crow.

For much more on Cameco and the entire Uranium space, [click here now](#) and we'll send you our special **FREE** report "**Fuel Your Portfolio With This Energetic Commodity**".

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*Fool contributor Alex Gray does not own shares of any companies mentioned. The Motley Fool has no positions in the stocks mentioned above at this time.*

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1. Investing

## TICKERS GLOBAL

1. NYSE:CCJ (Cameco Corporation)
2. TSX:CCO (Cameco Corporation)

## Category

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agray

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