Cameco Corporation: Should Contrarian Investors Buy This Stock?

Description

Cameco Corporation (TSX:CCO)(NYSE:CCJ) remains stuck in a slump, but contrarian investors with a long-term outlook are wondering if the bottom is finally in sight.

Let's take a look at the current situation to see if Cameco should be in your portfolio.

Japan restarts

Five years ago a tsunami hit Japan and caused the planet's worst nuclear disaster since Chernobyl.

As a result, the country shuttered its entire nuclear energy fleet. The move sent uranium into a long tailspin, falling from US$70 per pound in early 2011 to below US$30 in 2014. The uranium market has recovered slightly, but still remains well below the $40 mark.

Japan recently began the process of restarting its nuclear energy facilities. Two reactors went back online in the fall of last year and another plant began operation at the end of January.

Four more locations are expected to get clearance in the coming months, and a total of 23 reactors are currently under evaluation to be restarted.

Market reactions

The positive news out of Japan was supposed to provide a lift to uranium prices and the shares of the producers, but that hasn't happened yet.

Cameco's shares traded at $40 before the Fukushima accident. Today the stock remains stuck below $16 per share, not far off its multi-year lows.

What's the hold up?

The uranium market remains oversupplied as secondary sources continue to offset lower primary output. As such, the spot price remains under pressure, and energy producers are simply fillingdemand gaps with purchases in the open market.

Most uranium is delivered on long-term contracts, but power plants are not in a rush to sign new agreements while prices remain so low.

At some point, the secondary supplies will dry up and the market will begin to tighten. When that happens, energy producers are expected to scramble to secure long-term supply at fixed rates, and that should be a catalyst for higher prices.

Market outlook

Japan’s fleet is slowly coming back online, and other countries are adding more facilities.

In total, Cameco has indicated that it expects as many as 80 net new reactors to be in service by 2024, which would result in annual uranium demand of about 230 million pounds. Current demand is about 155 million pounds.

The long rout in the market has forced global producers to shelve expansion projects, and that could result in a supply squeeze at some point in the coming years.

Cameco’s position

The company has done a good job of reducing costs through the downturn and is still profitable despite the weak market conditions. Adjusted Q4 2015 earnings actually came in at a respectable $151 million, or $0.38 per share.

Cameco is sitting on some of the highest-grade deposits on the planet and is a low-cost producer, so the miner is positioned well to benefit from a recovery in uranium prices.

CRA issues

One item to keep an eye on is the company’s ongoing battle with the Canada Revenue Agency (CRA) over revenue generated through a foreign subsidiary.

A decision isn’t expected before late 2017, but the potential hit to Cameco is about $2.1 billion, according to the company’s latest update.

Should you buy?

The near-term outlook for the uranium market is more of the same, and the CRA issue will likely cap any rally in the stock until it gets resolved. Contrarian investors might want to start nibbling at the current level, but there probably isn’t a rush to buy the stock.

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1. Investing
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