Cameco Corporation: Risks vs. Rewards

Description

Cameco Corporation (TSX:CCO)(NYSE:CCJ) remains stuck in a rut, and investors are wondering when the company will finally break out of its five-year funk.

Let's take a look at the ongoing challenges as well as the potential opportunities for Cameco's investors.

Long road down

Back in early 2011 Cameco traded for more than $40 per share and uranium spot prices hovered around US$70 per pound. Most pundits thought the trend would be higher based on strong global support for nuclear energy, but the situation changed completely when the tsunami hit Japan.

The Fukushima disaster totally altered the nuclear energy landscape. Japan shut down its entire fleet of more than 40 reactors, and countries around the world put new projects on hold or even started the process of abandoning nuclear energy altogether.

The result has been a nasty five-year slide for both uranium prices and the values of the world's producers. Cameco currently trades at $16 per share and uranium is below US$30 per pound.

CRA risk

To matter matters worse, Cameco is embroiled in a nasty battle with the Canada Revenue Agency (CRA) over taxes owed on revenue generated through a foreign subsidiary.

If Cameco loses the case, which won't see a decision until at least late 2017, the company could be hit for an additional $2 billion.

Upside opportunities

The near-term outlook isn't overly positive, but investors with a broader perspective are seeing some strong potential for gains.

Producers have cut production and shelved development plans to the point where global uranium demand currently outstrips primary production. Secondary supplies have filled the gap in recent years, but that resource pool is drying up and demand is expected to increase.

Japan is slowly restarting its nuclear fleet. Two reactors are back in service, and the country could eventually reboot a majority of the 43 existing operable sites. At the same time, the world is warming up to nuclear energy once again and more than 60 new reactors are now currently under construction.

Cameco is actually forecasting 113 new facilities by 2025. About 55 existing reactors will be decommissioned, but the net effect should drive annual uranium demand from the current level of 160 million pounds to 220 million pounds over the next decade.

Uranium mines take seven to 10 years to go from the planning stage to production, so there is a chance the market could switch to a shortage situation in the coming years. If that happens, the price of both uranium and Cameco's shares should surge.

Should you buy now?

Cameco is a low-cost producer and is sitting on some of the richest resources on the planet. At some point, things will turn around and the shares could move quickly on good news out of Japan or a deal with the CRA.

There isn't a rush to buy the stock today, but contrarian types might want to consider a small position on further weakness.

CATEGORY

1. Investing
2. Metals and Mining Stocks

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