Uranium Prices Set to Double: Time to Buy Cameco Corporation

Description

Cameco Corporation (TSX:CCO)(NYSE:CCJ) is one of the largest publicly traded uranium producers, and in recent years it has been a casualty of the low-price-commodity environment which is currently hampering producers in a range of industries. We will be taking a look at where we see uranium prices going over the medium to long term and determine if Cameco could be a decent long-term hold.

Uranium prices set to double by 2020

High-profile uranium analysts, such as David Talbot of Dundee Capital Markets, have proposed that a 6% annual growth rate of the current uranium price to 2020 is not only feasible but likely. Talbot notes that "the period from 2017-2020 to be a landmark period for the nuclear sector and uranium stocks, as the global operating nuclear fleet expands."

Other analysts have pointed more specifically to a doubling in the average market price for uranium. Taking the expert analysis into consideration, we move to taking a look at how Cameco is doing right now relative to competitors in the industry.

Third-quarter profit higher than industry average

Cameco president and CEO Tim Gitzel has repeatedly declared to the media that a uranium price turnaround cannot be expected. One of his key functions as CEO is to try to manage production revenues via contracts and hedge as much exposure as possible when it comes to uranium–a commodity that has lost value every year since 2011.

So far, it appears Mr. Gitzel has done a decent job, given the operating environment presented to him. Under his reign, Cameco has posted a Q3 2016 profit of $142 million compared with a $4 million loss in 2015.

New contracts may hamper profits

These previously mentioned production contracts are currently what is keeping the company's average realized price above the current weak market prices. This is currently working in the company's favour, as many of its smaller competitors are finding it harder and harder to stay in business with the existing downward price pressure.

As part of the company’s long-term hedging strategy, one of the downfalls of a potential uranium price rebound would be the fact that new contracts will continue to be locked in at lower rates until such a rebound occurs. With the expectation that uranium prices will continue to rise, we will need to build into the expected future increased cash flows from operations some allowance for downward pressure from existing production contracts.

What is interesting about the uranium industry is that uranium prices are generally negotiated between buyers and sellers, and sellers such as Cameco may have enough market power to renegotiate contracts or simply adjust future contracts higher as needed to mitigate some of this “fixed-price production” risk.

We will continue to monitor the uranium price over the short term, but we’ll view the current market price of uranium as an attractive entrance point. We also view Cameco as an attractive company for a long-term investor looking for exposure to the uranium and commodity sectors.

CATEGORY

1. Energy Stocks
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