Why Did Cameco Corp. Shares Drop 7% on Monday?

Description

Cameco Corp. (TSX:CCO)(NYSE:CCJ) shares lost about 7.19% of their market valuation during Monday's trading hours to close at $11.74 in a choppy trading environment characterized by a general stock price decline in all uranium names.

This development has come after the uranium mining giant took off on a bumpy rally on November 9 after making the big announcement of a production suspension at the world's biggest uranium mine, McArthur River, putting the Key Lake mill under care and maintenance, while at the same time cutting the once 3.8%-yielding quarterly dividend down to a $0.08 annual payout which yields a paltry 0.7%.

This bullish trend was, however, premised on a broader market sentiment that Cameco's announcement could be the biggest catalyst for a rebound in global uranium market prices that have been heavily depressed since the wake of the Fukushima nuclear disaster in Japan and subsequent nuclear plant shutdowns wiped away vital uranium demand and rendered the market severely oversupplied.

It is on this background that Cameco stock shed 7.19% in a single trading day, putting a significant dent to investors' hopes of a sustained bullish trend in Cameco's market valuation, as traders look forward to a significant recovery in uranium spot prices.

A plummeting uranium futures market

Following the production cut news by Cameco, which the analysts believed could be the biggest catalyst since Fukushima, the uranium futures market has been on a rally.

Uranium futures contracts on the CME and NYMEX exchanges for March 2018 delivery rose from US$20.55 on November 8 to trade at US$26.40 by November 21 in a solid 28.5% price appreciation in just two trading weeks.

However, the same contacts took a price downturn to trade at US$24.85 on November 22, and the price plummeted to US$21.95 on November 27, as the contracts took in a 16.9% knock in just four trading days, losing nearly 8% on Monday alone.

The speculative bullish sentiment on uranium may be waning, as market traders start to lose confidence and wait for confirmation from the long-term contracts market as to whether uranium prices are actually going to trend up after Cameco removed significant production from the oversupplied market.

Technical indicators in the uranium futures market are, however, still depicting a bullish long-term trend, but most threatening is the short-term outlook, where simple moving averages and the moving average convergence and divergence is showing a bearish signal, suggesting that the short-term downward trend in the contracts may continue and, at worst, result in a reversal in the long-term trend.

That said, the uranium market is purely being driven by speculation at the moment, as the anticipated pick in market demand for this cleaner, reliable, but dangerous energy fuel is still long into the future, yet there is a massive oversupply from primary mining production, as other suppliers are reluctant to cut back production, as Cameco and Kazakhstan have already done.

Profit taking

It is also possible the one-day plunge in uranium stocks on Monday may be a result of some profit taking by traders who rushed to initiate trading positions after the recent Cameco production-cut news.

The stock had gained about 10.4%, as investors priced in a potential uranium price recovery in spot and long-term contract prices for uranium going forward. The waning bullish trend could have triggered profit taking by short-term uranium futures and stock traders who rely mostly on technical charts, which are currently printing bearish short-term trading signals.

Foolish bottom line

There will always be a lot of deafening market noise in the short term, but bullish long-term investors need to stick to their guns and avoid the selling pressure from short-term trends.

However, Cameco is still an intriguing contrarian play with significant investment risks and growing market volatility after the dividend cut. The uranium market recovery remains very cloudy, and market demand will take a long time to usurp the current product oversupply.

Considering the pending tax dispute with the Canada Revenue Agency, Cameco remains a risky contrarian buy. Investors may be better off considering smaller uranium names for a uranium recovery play.

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