Cameco Corp.: Should This Stock Be on Your Contrarian Buy List?

Description

Cameco Corp. (TSX:CCO)(NYSE:CCJ) has been on an upward trend since early February, and investors are wondering if the beleaguered stock might finally be on the verge of a long-term recovery.

Let's take a look at Canada's largest uranium producer to see if it deserves to be on your contrarian buy list today.

Rough run

Cameco was a $40 stock back in early 2011 when uranium prices were close to US$70 per pound. Then the tsunami hit Japan, and everything changed.

The Fukushima disaster forced Japan to shut down its entire fleet of nuclear reactors, and countries around the globe took a step back to evaluate the future of their nuclear energy programs. This sent uranium prices into a multi-year tailspin, bottoming out just below US$20 per pound.

Producer stocks followed suit, including Cameco, which has traded below $10 per share in the past 12 months.

At the time of writing, uranium spot prices remain near the lows, barely trading above US$20 per pound. Cameco is at $13.40 per share.

Bull case

Fans of the sector point to the long-term outlook for the industry and Japan's determination to get its reactors back in service. As of mid-February, Japan only had five of its 42 operable reactors back in commercial operation. The country has struggled with legal battles and technical challenges in its efforts to get the fleet in service, and those headwinds are expected to continue.

Eventually, the country will make more progress, but investors shouldn't expect a wave of restarts.

Regarding growth, annual uranium demand could rise as much as 50% through 2030, as countries around the world ramp up their nuclear energy programs. China and India, among others, face growing electricity demand and plan to expand their nuclear energy capacity. Today, more than 50 new reactors are under construction around the world.

Producers have cut output and shelved development plans to the point where the industry could eventually see a supply squeeze. If that scenario materializes, uranium prices could rocket higher.

Bear case

Secondary supplies continue to put pressure on the market, and utilities are comfortable filling demand gaps with purchases in the spot market. Cameco sells most of its uranium on long-term contracts that were signed at much higher prices. As those agreements expire, the average realized sale price is at risk of falling, unless buyers get nervous about supply and begin to sign new multi-year agreements.

Cameco is also caught up in a battle with the Canada Revenue Agency (CRA) over taxes owed on earnings generated through a foreign subsidiary. The first round of the legal proceedings wrapped up last September and a decision is expected six to 18 months from that time.

If Cameco loses the case, it could be on the hook for more than $2 billion in taxes and penalties.

Should you buy?

The stock is up 25% since early February, despite ongoing weakness in uranium prices. A shift of funds back into commodity plays might be part of the reason for the mini-rally, but I’m not convinced this is the time to step in and buy the stock.

If you have a contrarian style and think the long-term opportunity is attractive, I would at least wait for a decision on the CRA case before adding Cameco to the portfolio.

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