



## 2 Strong Signs That Cameco Corp's (TSX:CCO) Best Days Lie Ahead

### Description

Low cost uranium mining giant **Cameco Corp** ([TSX:CCO](#))([NYSE:CCJ](#)) is battling to survive the prolonged dip in the oversupplied uranium market, but there is new hope among contrarian investors on the stock as recent supplier collaborative efforts are beginning to yield some fruit.

Two important factors favour the prospect of a sustained recovery on Cameco stock, one being the latest favourable tax court ruling that eliminates risk discounts, while the ongoing recovery in uranium spot and contract prices since last quarter could be the most bullish development that investors have been waiting to see for several years.

Should investors start smiling now? A closer look at recent developments could provide some model answer to this question.

### Rising spot prices

Uranium spot and long-term contract prices rose significantly during the last quarter.

As market leader Kazatomprom slowed down production growth this year, Cameco decided to indefinitely extend its shut-down of valuable producing assets, the McArthur River mine and related Key Lake milling plant in July, further constraining industry supply.

In response, the uranium spot market rebounded sharply during the quarter to trade around US\$27.50 per pound by September, up more than 21% from the June average price. Long-term contract prices rose nearly 9.5% during the quarter to US\$31.75 per pound.

*Uranium Average Monthly Price Per Pound (June 2016-Sep 2018). Source: Cameco Corporation*

While the increase in long-term prices hasn't been as encouraging as the rebound in the spot market, the increase could be an important sign that the market is warming up to increasing equilibrium prices as mining production recedes.

That said, this short-term recovery isn't 100% favourable to Cameco.

### **Unfavourable spot prices?**

Management could have been more pleased if contract prices had mimicked the surge in spot prices to allow the company to contract at better terms. Cameco supplies into the long-term contracted market, and is currently a significant buyer in the spot market to augment cover the gap from reduced mining output.

As spot prices rise faster than contract prices, gross margins suffer in the short term, yet the company cannot enter new supply contracts at low long term price points.

That said, the company's supply contracts include a fixed price leg and a spot price leg at delivery. The respective weighting of the two legs in realized prices remains confidential information, but the company could realize better average prices going forward.

### **Long-term price recovery lagging**

The uranium market has suffered from surplus supplies from both fresh mine production and from secondary material for years. Customers may still be convinced that supply surpluses are still existent, hence the resistance to contract at higher prices even as spot prices increase.

Further, Cameco's spot market presence today somehow increases demand in the short term, which may contribute to rising spot prices. However, this new demand will evaporate once the company restarts production at its currently idle key assets.

Could the price trajectory then reverse after Cameco exits the spot market and restarts production?

The above remains a puzzling question, but the key question could be: *At what contract price range will Cameco restart its suspended production?* Production economics kick in at this point, but I would bet that management could start contracting at prices nearly double today's spot, which is a long way up.

### **Investor takeaway**

A long-term collapse in capital investment and low development in the uranium market due to a low price environment have paved the way for market recovery as new supply capacity dries up. The obtaining recovery could therefore be sustained in the long term, and that's a bullish factor for Cameco stock price.

Further, the company has scored big in the high value tax case against the Canada Revenue Agency (CRA), but it could still contest the ruling.

Even if the CRA could decide to appeal against the tax court judgement, there is evidently strong legal merit in Cameco's plea for innocence in the case; the CRA could simply respect the court decision, reimburse claimed taxes and penalties as well as apply the ruling to other tax years.

There's reason enough to be bullish on Cameco today as the CRA's case gets shrugged off and uranium market prices tick higher.

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brianparadza

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