

Action Note

Equity Research

May 4, 2020

Metals & Minerals

Cameco Corp.

(CCO-T, CCJ-N) C\$14.42 | US\$10.29

Utility Term Demand the Next Domino to Fall; Upgrading to BUY

Greg Barnes

Derick Ma, CFA, CPA, CA

Event

Cameco management discussed the uranium market outlook during its Q1/20 conference call.

Impact: POSITIVE

- In our view, Cameco management is demonstrating increasing confidence that the uranium market is transitioning away from oversupply and a short-term focus to a market that is in deficit and security of LT supply will play an increasing role in utility purchasing decisions.**
- Over the past week, both Cameco and Kazatomprom managements have voiced their views that the mid-term uranium market is facing a lack of available material to drive the carry trade that has dominated the utility contracting activity for the past several years at the expense of the term contract market. Kazatomprom management has indicated that it will not supply material to the spot market this year, which is a significant shift in strategy. We believe that a decline in mid-term market activity will drive utilities into the term market. Last week's US\$2/lb increase in the term price (to US\$33/lb, the highest in 3.5 years) and UxC's comment that further upward pressure on term pricing is expected suggest that this may be happening.**
- Utilities have been inwardly focused during the COVID-19 crisis. While spot market activity has hit record levels over the past two months, activity in the term market has remained muted. Cameco believes that nuclear utilities have been focused on maintaining safe work environments and ensuring their supply chains are in good order. They have not yet moved towards assessing their LT supply requirements - although this is expected and should drive the long-awaited contracting cycle.**

TD Investment Conclusion

We are increasing our recommendation to BUY (from Hold); our target price has increased to \$18.00 (from \$14.00). With both of the world's largest primary uranium producers cutting production and committing to further supply discipline, we believe that after almost a decade of weak prices (and several false starts) uranium pricing power is moving into the hands of the producers. We also believe that a more constrained mid-term market should allow producers to rebuild LT contract portfolios at commercially acceptable prices.



Company Profile

Cameco is one of the world's largest uranium producers. The company's flagship McArthur River and Cigar Lake mines are located in the Athabasca Basin in Saskatchewan, Canada.

Recommendation:

BUY↑

Prior: HOLD

Risk:

HIGH

12-Month Target Price:

C\$18.00↑

Prior: C\$14.00

12-Month Dividend (Est.):

C\$0.08

12-Month Total Return:

25.4%

Market Data (C\$)

Current Price	C\$14.42
52-Week Range	\$7.69 - \$14.92
Mkt Cap (f.d.) (\$mm)	\$5,707.4
EV (\$mm)	\$5,641.6
Current Dividend	\$0.08
Dividend Yield	0.6%
Avg. Daily Trading Vol.	2,520,644

Financial Data (C\$)

Fiscal Y-E	December
Shares O/S (f.d)(mm)	395.8
Float Shares (mm)	395.8
Net Debt/Total Cap	3.5%
NAVPS	\$11.68
Working Cap (\$mm)	\$1,529.6

Estimates (C\$)

Year	2018A	2019A	2020E	2021E
EBITDA (\$mm)	460.0	372.8	286.1	102.9
EBITDA (\$mm) (old)	-	-	182.5	81.2
EPS (f.d.)	0.38	0.10	0.19	(0.13)
EPS (f.d.) (old)	-	-	(0.17)	(0.21)
CFPS (f.d)	1.21	1.04	0.34	0.28
CFPS (f.d) (old)	-	-	0.01	0.20

EPS (f.d.) Quarterly Estimates (C\$)

Year	2018A	2019A	2020E	2021E
Q1	0.06	(0.08)	0.07	-
Q2	(0.07)	(0.04)	(0.06)	-
Q3	(0.12)	(0.01)	0.02	-
Q4	0.52	0.23	0.15	-

Valuations

Year	2018A	2019A	2020E	2021E
EV/EBITDA	12.3x	15.1x	19.7x	54.8x
P/E (f.d.)	37.9x	nmf	75.9x	nmf
P/CFPS (f.d)	11.9x	13.9x	42.4x	51.5x

Supplemental Data

Year	2018A	2019A	2020E	2021E
U3O8 (US\$/lb)	25	26	29	31
U3O8 Prod. Mlb	9	9	8	9

All figures in C\$, unless otherwise specified

Action Note

Equity Research

May 4, 2020

Details

Cameco reported adjusted Q1/20 EPS of \$0.07, above TD at \$(0.09) and consensus at \$(0.02). Estimated adjusted EBITDA was \$51mm vs. TD at \$15mm. Q1/20 results were ahead of our expectations based on higher earnings in the fuel services division relative to our expectations. Uranium deliveries were also higher than we forecast at 6.0mm lbs (TD forecast 5.2mm lbs); the company's realized uranium price was in line with our forecasts (see Exhibit 1).

Exhibit 1. Q1/20 Summary

	Q1/20			Q/Q			Y/Y		
	Actual	TD Est.	% Diff	Q1/20	Q4/19	% ch.	Q1/20	Q1/19	% ch.
Realized Uranium Price (US\$/lb)	31.39	32.00	-2%	31.39	35.92	-13%	31.39	32.05	-2%
Realized Uranium Price (C\$/lb)	41.44	42.67	-3%	41.44	47.50	-13%	41.44	42.80	-3%
Total Cost (C\$/lb Sold)	32.53	44.95	-28%	32.53	33.62	-3%	32.53	35.35	-8%
Uranium production									
Rabbit Lake	-	-	na	-	-	na	-	-	na
McArthur River	-	-	na	-	-	na	-	-	na
Cigar Lake	2,100	2,300	-9%	2,100	2,700	-22%	2,100	2,400	-13%
Highland-Smith	-	-	na	-	-	na	-	-	na
Crow Butte	-	-	na	-	-	na	-	-	na
Total uranium production (klbs)	2,100	2,300	-9%	2,100	2,700	-22%	2,100	2,400	-13%
Total uranium sales (klbs)	6,000	5,185	16%	6,000	14,000	-57%	6,000	4,746	26%
Gross profit (C\$M)									
Uranium	5	-9	nm	5	136	-96%	5	-3	-258%
Fuel services	30	8	260%	30	46	-36%	30	20	46%
Financial highlights									
Adj. EPS (C\$)	0.07	-0.09	nm	0.07	0.23	-70%	0.07	-0.08	nm
CFPS (C\$)	0.11	-0.06	nm	0.11	0.62	-82%	0.11	0.03	247%
EBITDA (C\$M)	51	15	252%	51.28	252	-80%	51	16	224%

Source: TD Securities Inc. estimates

Exhibit 2. Uranium Spot and Term Prices



Source: UxC; TD Securities Inc. estimates

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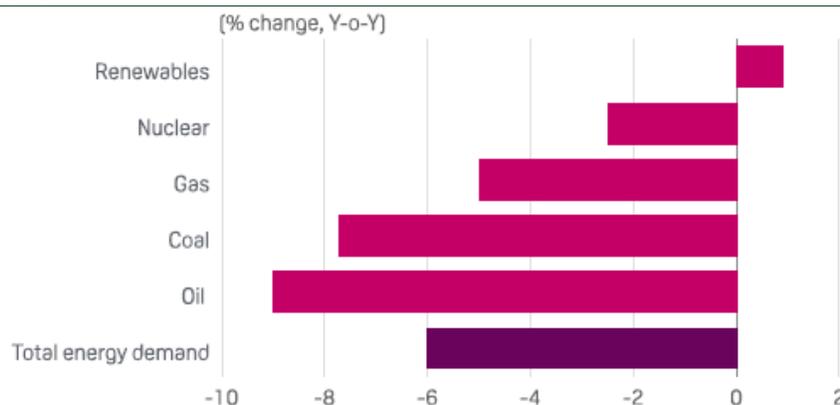
May 4, 2020

Spot market seeing record activity. UxC reported April spot market volume at 15.1mmlbs U3O8e under 84 transactions. Total demand year-to-date is now at 34.2mmlbs U3O8e and total transactions are at 207. Spot volume year-to-date is well above the five-year average and tracking above the record volumes that were achieved in 2018. We understand that producers have been the most active in the spot market this year (purchasing to meet contractual volumes); to this point, utilities have seen limited players in the spot market.

Mid-term market under pressure. We are hearing from various sources that the mid-term uranium market (deliveries in the one- to three-year time frame that is dominated by traders) is under pressure as the supply of available spot material tightens due to production curtailments. As well, Kazatomprom has indicated publicly several times year-to-date that it will not make material available to the spot market in 2020 given that its production is fully committed. Utilities have been using the spot market on a rolling basis to supplement their inventory/purchasing requirements at the expense of the term market. With the availability of material to the mid-term market contracting, utilities should be forced into the term market and the long-awaited contracting cycle should resume.

Nuclear electricity demand holding up relatively well. According to the International Energy Agency (IEA). The worldwide response to the coronavirus pandemic is set to push global electricity demand down by ~6% y/y in 2020. Coal and oil are expected to see the biggest declines in terms of electricity generation, down ~7.5% and ~9%, respectively. Nuclear electricity generation is holding up relatively well, down slightly more than 2% y/y. Cameco noted that it does not expect a material impact on its committed sales volumes for 2020.

Exhibit 3. Projected Change in Primary Energy Demand by Fuel-Type in 2020 vs. 2019



Source: IEA, Platts

Outlook

We have updated estimates to reflect Q1/20 results.

Valuation

CCO is currently trading at a P/NAV multiple of 1.2x, compared with its large-cap producer group average of 0.81x. Over the past five years, CCO has traded at an average P/NAV multiple of 1.1x, which compares to 0.99x for First Quantum, 0.95x for Teck Resources, 0.93x for Lundin Mining and 0.72x for Hudbay Minerals.

Action Note

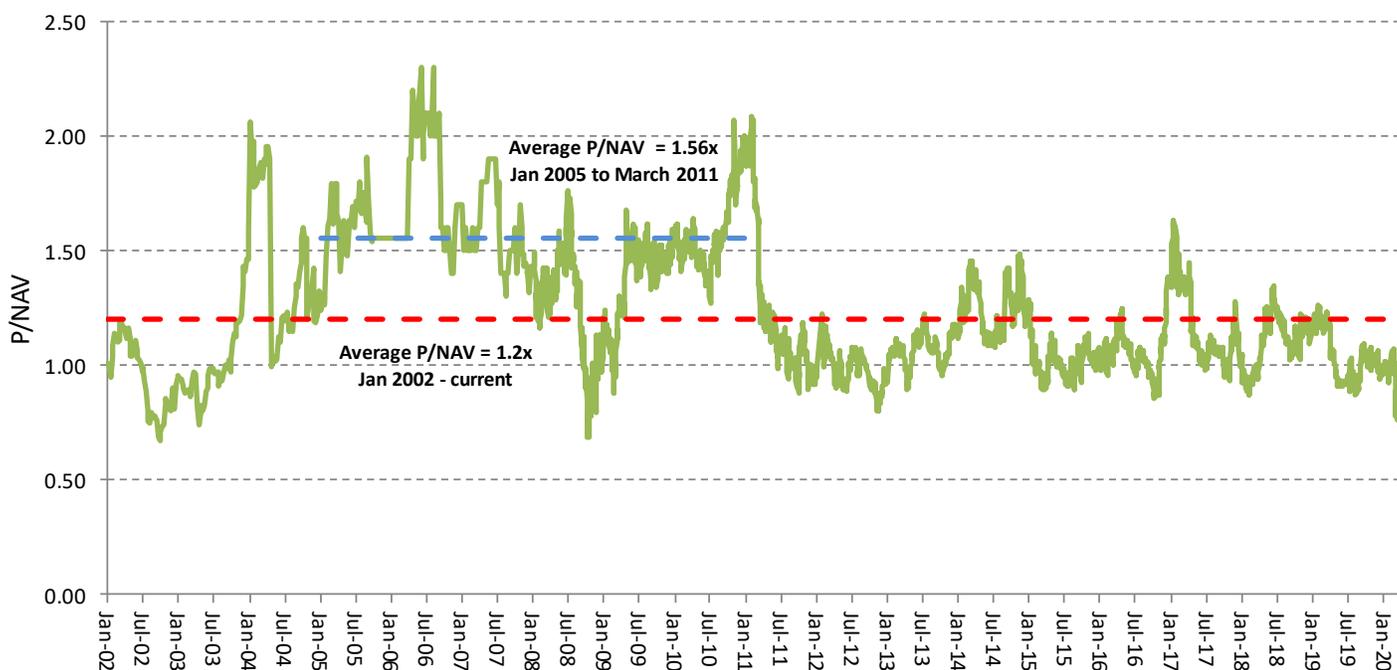
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May 4, 2020

Justification of Target Price

Our revised \$18.00 target price is based on a NAV-10% multiple of 1.55x (100% weighted, previously 1.2x). Our increased NAV target multiple reflects improving market conditions and the potentially positive impacts the recent supply tightening could have on the term market, in our view. We note that Cameco's P/NAV multiple can trade at a significant premium during periods of rising and elevated uranium prices. Over the period January 2005 through March 2011 (the Fukushima disaster occurred on March 11, 2011) Cameco's P/NAV multiple averaged 1.56x (within a range of ~1.2x (excluding the Financial Crisis) and >2.2x). Over that same time frame, the spot uranium price averaged US\$56/lb.

Exhibit 4. Historical Cameco P/NAV multiple



Source: TD Securities Inc. estimates

Key Risks to Target Price

The main risks facing the company include forecast, financial, technical, and political risks. Among other things, these include risks related to uranium prices, input costs, and fuel prices; the governing fiscal and legislative regimes; the timing of key developments; market conditions; capital and operating costs; foreign exchange rates; resources and reserves; operating parameters; permitting; environment; and staffing and key personnel retention. As Cameco is primarily a uranium mining company, it faces heightened environmental risks relative to other mining companies. The tax dispute with the CRA, which is now undergoing an appeals process, and COVID-19-driven operational closures are additional risk factors.

Action Note

Equity Research

May 4, 2020

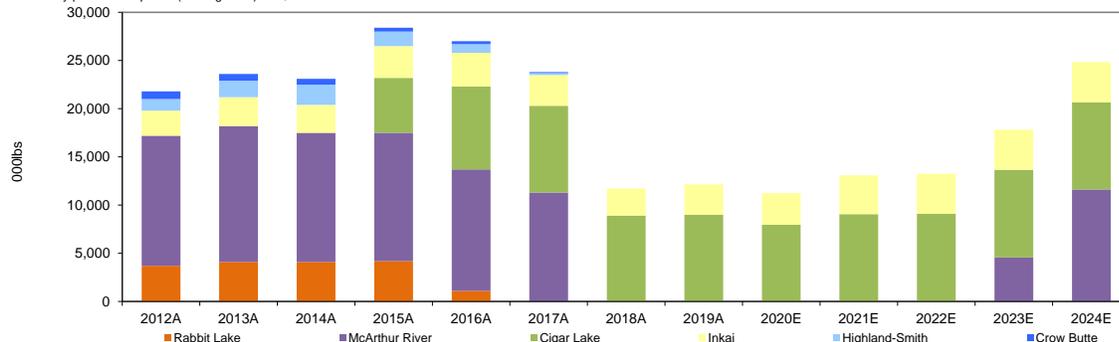
Exhibit 5. Cameco Snapshot

Risk Profile:	HIGH												
Stock Rating:	BUY												
Target Price:	18.00												
NAV Estimate													
McArthur River								1,906.8	4.82	1,480.2	3.74		
Cigar Lake								1,041.5	2.63	960.6	2.43		
Rabbit Lake								59.3	0.15	36.6	0.09		
Inkai								1,286.0	3.25	1,017.0	2.57		
Highland-Smith								190.2	0.48	190.2	0.48		
Crow Butte								108.6	0.27	108.6	0.27		
Conversion								385.8	0.97	337.2	0.85		
Total Operations								4,978.2	12.58	4,130.4	10.44		
Resources - Existing Mines*								515.2	1.30	515.2	1.30		
Resources - Pipeline projects*								628.2	1.59	628.2	1.59		
Nukem								0.0	0.00	0.0	0.00		
Mining/Project NAV								6,121.6	15.47	5,273.8	13.32		
Working Capital								1,529.6	3.86	1,529.6	3.86		
Corporate G&A								-448.3	-1.13	-409.3	-1.03		
CRA Cash Remittances								207.0	0.52	207.0	0.52		
Debt								-996.7	-2.52	-996.7	-2.52		
Other								-979.8	-2.48	-979.8	-2.48		
Total balance sheet adj.								-688.4	-1.74	-649.3	-1.64		
Total Net Asset Value								5,433.3	13.73	4,624.5	11.68		

* Existing mines and pipeline projects are based on 50% inferred resources @ C\$8/lb and 50% of total resources @ C\$4/lb, respectively.

Fiscal Yr-End: Dec	2017A	2018A	2019A	Q1/20A	Q2/20E	Q3/20E	Q4/20E	2020E	2021E	2022E	2023E	2024E
Metal Price Assumptions												
Spot Uranium (US\$/lb)	22.12	24.82	25.90	24.77	31.00	30.00	30.00	28.94	31.00	33.00	35.00	40.00
Realized Uranium Price (US\$/lb)	35.70	37.13	33.00	31.39	32.00	32.00	34.00	32.35	34.15	35.10	37.00	41.00
Realized Uranium Price (C\$/lb)	46.06	47.95	44.84	41.44	45.07	45.71	47.89	45.46	46.78	45.58	45.12	50.00
Production Assumptions												
Uranium (mmlb), attributable	23.8	8.9	9.0	2.1	1.4	2.3	2.3	8.0	9.1	9.1	13.7	20.7
Per Share Estimates (US\$/sh)												
EPS (f.d.) (C\$/sh)	0.15	0.38	0.10	0.07	(0.06)	0.02	0.15	0.19	(0.13)	0.05	(0.05)	0.57
CFPS bf WC (C\$/sh)	1.31	1.21	1.04	0.11	0.01	0.03	0.19	0.34	0.28	0.37	0.21	0.95
EBITDA	1.43	1.16	0.97	0.13	0.10	0.16	0.34	0.72	0.26	0.38	0.16	0.99
Financial Estimates (\$mm)												
Total Revenue	2,156.9	2,091.7	1,862.9	345.6	357.2	388.0	581.3	1,672.0	1,265.4	1,017.2	966.4	1,519.0
Operating Cost	1,390.2	1,467.9	1,345.6	255.5	286.1	294.4	417.4	1,253.4	1,035.5	733.8	754.4	948.3
Gross Margin	766.6	623.7	517.4	90.0	71.1	93.6	163.9	418.6	229.9	283.3	212.0	570.7
Gross Margin %	36%	30%	28%	26%	20%	24%	28%	25%	18%	28%	22%	38%
EBITDA	567.9	460.0	372.8	51.3	39.8	62.3	132.6	286.1	102.9	148.5	64.3	392.1
EBITDA Margin %	26%	22%	20%	15%	11%	16%	23%	17%	8%	15%	7%	26%
Operating CF bf. ch. in WC	519.9	478.4	413.8	44.2	2.9	11.6	75.0	133.8	109.4	147.6	84.6	374.5
Changes in Working Capital	76.1	189.0	113.2	137.9	0.0	0.0	0.0	137.9	0.0	0.0	0.0	0.0
CF from operating activities	596.1	667.4	527.0	182.1	2.9	11.6	75.0	271.7	109.4	147.6	84.6	374.5
CF from financing activities	(227.8)	(144.2)	(606.9)	(0.7)	0.0	0.0	(31.7)	(32.3)	(31.7)	(431.7)	(31.7)	(531.7)
CAPEX	(114.0)	(55.4)	(75.2)	(18.8)	(30.0)	(30.0)	(30.0)	(108.8)	(95.0)	(97.3)	(73.1)	(68.4)
Other	21	(356)	513	(169)	(4)	(4)	(4)	(182)	(18)	(18)	(18)	0
CF from investing activities	(93.1)	(411.6)	437.4	(187.4)	(34.4)	(34.4)	(34.4)	(290.5)	(112.5)	(114.8)	(90.6)	(68.4)
Cash	591.6	711.5	1,062.4	1,066.0	1,034.6	1,011.8	1,020.8	1,020.8	986.0	587.1	549.4	323.9
Current portion of LTD	0.0	499.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Long-term debt	1,494.5	996.1	996.7	996.9	996.9	996.9	996.9	996.9	996.9	596.9	596.9	96.9
Net Debt	902.9	393.1	(65.7)	(69.1)	(37.7)	(184.2)	(193.2)	(193.2)	(158.4)	(159.6)	(121.9)	(396.4)
Net Debt/EBITDA	1.59x	0.62x	-0.18x	nm	nm	nm	nm	-0.08x	0.11x	0.07x	0.74x	-0.58x
Net Debt/Net Debt + Equity	15.7%	5.4%	-1.3%	-1.4%	-0.8%	-0.3%	-0.5%	-0.5%	0.2%	0.2%	1.0%	-4.9%
FCF	405.9	423.1	338.6	25.4	(27.1)	(18.4)	45.0	25.0	14.4	50.3	11.5	306.1
S/O basic (mm)	395.8	395.8	385.8	395.8	395.8	395.8	395.8	395.8	395.8	395.8	395.8	395.8

* LT commodity price assumptions (starting 2025): US\$45.00/lb U3O8



Source: TD Securities Inc. estimates



Action Note

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May 4, 2020

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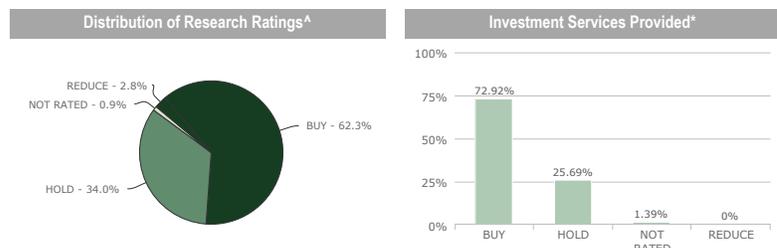
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Action Note

Equity Research

May 4, 2020

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May 4, 2020

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