

## Micro to Macro Monthly **BETA**

26 April 2011

### **The Sky is (Still) Falling!**

If you watch the news, read the paper, or talk to your neighbors, you hear that the world is in chaos. American unemployment remains high. The Middle East and North Africa boil, threatening global stability: war rages in Libya, Egypt has only a transition government; Mideast governments shoot citizens to suppress protesting. In the Far East, the largest earthquake in Japanese recorded history and a massive tsunami wreaked unimaginable devastation. With thousands already dead, the threat of nuclear disaster now looms in the world's third most important economy. Times of crisis, though, are also times of opportunity.

These tragedies have put the spotlight on our energy supply lines, and how fragile they really are. Partial meltdowns at the Fukushima reactors in Japan have released dangerous levels of radiation. Investors have panicked, and rushed to eliminate exposure to the nuclear sector. They've liquidated positions in companies that produce electricity from nuclear power, those that build nuclear reactors, and most relevant to this letter, those that mine and process the uranium into fuel for power plants.

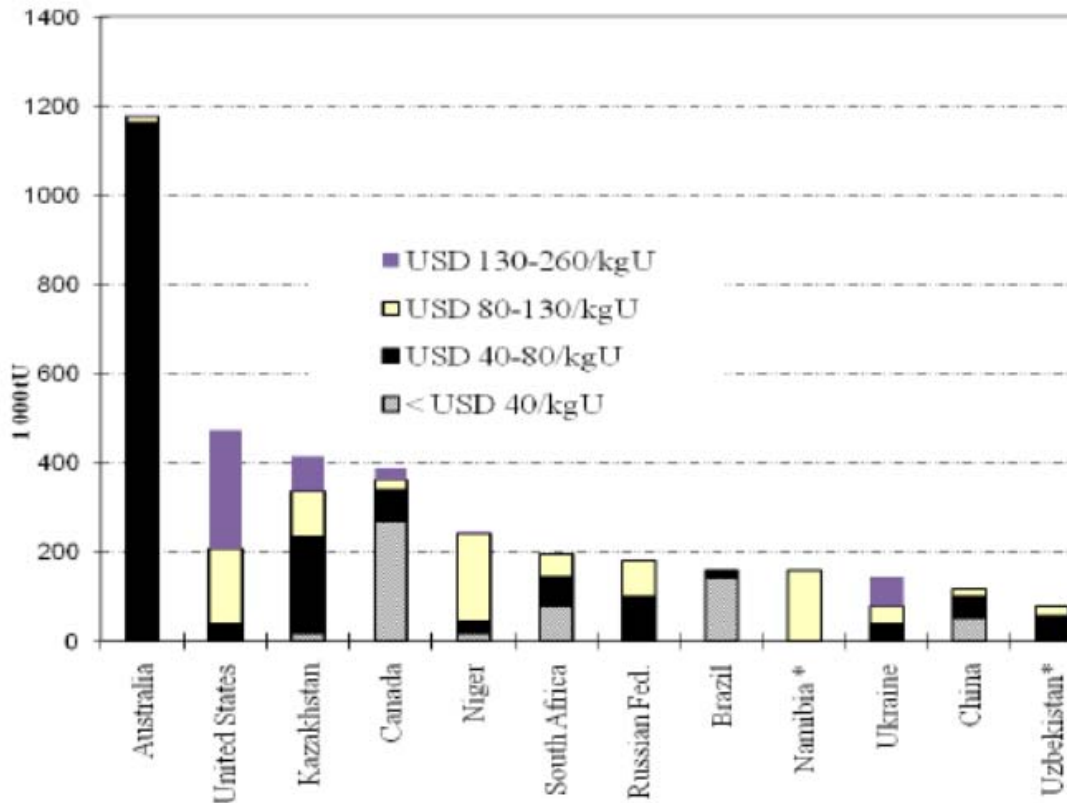
Anticipating a drop in long term demand, Uranium spot prices plummeted from \$73 to less than \$60 per pound. One producer, Cameco Corporation (NYSE:CCJ), has seen a 25% drop in share price – but this crisis actually *helps* Cameco's business.

Here's why...

### **Low Uranium Prices benefit Cameco**

CCJ is the only large uranium producer that can still make a profit at virtually any price. The ore from their mines in Saskatchewan is over 100 times richer than average deposits, which translates into low extraction and refining costs. During the past quarter century, uranium supplies have been sustained by commercial stockpiles (now used up)

and reprocessed HEU (highly enriched uranium) from decommissioned warheads. This glut of Uranium drove prices down and discouraged mining activity for much of the past three decades. As a result we can no longer mine enough to supply what we use - even in existing reactors! The longer low prices persist, though, the more important Cameco becomes. Look for gray bars on this global production chart from the International Atomic Energy Agency (IAEA):



Those gray bars represent the lowest cost producers – the ones that are profitable below \$40/kg. See how Canada makes up more than half of the gray space? That’s Cameco. And they’re planning to double production by 2015, easily maintaining the best margins in the industry on anything like that scale.

### Nuclear Power is not Dead

The so-called “Nuclear Renaissance” - a global resurgence of power generation from Uranium – will continue. Governments are reviewing safety guidelines for reactors to

address safety concerns, but we need the electricity. Nothing substantial has changed in global energy policy, and we're not about to shut down existing capacity. Far from it –China *by itself* accounts for half of projected growth in global uranium consumption, and has no plans to abandon its ambitious nuclear program. The only real option for reasonably priced, low-carbon electricity is still the nuclear option.

### **How to Play It**

Cameco is a secure company. I don't expect the headlines to go away any time soon, and as long as people are scared, its price may stay low. Some reactors may even be shut down temporarily for safety reviews, increasing reserves and lowering prices.

Good – it means fewer competitors when the reactors come back online. I believe any risks to the company are priced in at current levels, and that downside is minimal, but I don't want to just sit on shares while they stay cheap. So here's what I'm doing: I've bought the stock (below \$31) and sold May covered calls at \$33/share. You can get about \$1 a share for those – about 3% in 45 days – for a simple ARR over 25%. I sold them a few dollars out of the money because I want to keep my stock and do it again in May – but I wouldn't be shocked if, 45 days from now, someone exercises that option and I'm left with a 10% return. Either way, Cameco just became my printing press.

And here's a way to put some of that profit to good use – Go to [redcross.org](https://www.redcross.org) or text REDCROSS to 90999 to donate \$10.

### **A Note on Telestone:**

If you sold the TSTC puts at the last newsletter, they expired worthless so you kept that premium – happy days! Wall Street is more scared than ever by Chinese reverse mergers, though. If you bought the stock, you're sitting on a loss. I did both, and my analysis there hasn't changed. I'm staying long, down about 10% on the stock, but compensated by the premium from my puts.