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Is This Uranium Bull Market For Real?

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Summary:
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In light of Toshiba's recent proposed acquisition of Westinghouse Electric from the government-owned British Nuclear Fuels (BNFL), historians may be reminded of former Westinghouse Chairman Robert Kirby's litigious international outcry and prolonged battle over secretive and illegal price manipulation by a global uranium cartel. In the 1970s, Westinghouse, determined to capture the world market of building nuclear reactors, offered dirt-cheap nuclear fuel as part of its incentive to get sales from utility companies. The company's 27 utility customers had locked in agreements with Westinghouse to provide them with 65 million pounds of U3O8 over the next twenty years, well into the 1990s. Those contracts set off one of the most curious legal battles of the 1970's, ultimately reducing Westinghouse to a shell of the powerhouse it once was.

In recent weeks, Toshiba (London Stock Exchange: TOS; Tokyo Stock Exchange Ticker Code: 6502) has been strongly criticized for the Westinghouse acquisition, and may sell as much as 49 percent of the deal to two other Japanese firms and a smaller stake to an American firm. Toshiba's CFO, Sadazumi Ryu said the company would pay for some of its acquisition costs within three years out of current cash flow plus float debt to about 115 percent of equity. Will Toshiba repeat the mistakes made by Westinghouse in the mid 1970s during the last uranium bull market?

Today, Toshiba aims its sights on the lucrative Chinese nuclear energy market, which on the surface appears more ambitious than the U.S. civilian nuclear program of the 1970's. Toshiba wants to be a major beneficiary of China's aggressive plans to expand the country's nuclear energy program. And why not? Uranium prices have soared the past few years. Spot uranium rocketed in 2005 at an even faster degree than in 1975. That was the year when Westinghouse's Robert Kirby was told by his doctor to not even bother giving up his chain-smoking habit. Things at Westinghouse had gotten that bad.

The head of the Pittsburgh-based conglomerate failed to grasp what was behind the escalating uranium price during the 1970s. His Westinghouse incentive plan sounded great when spot uranium sold for $6/pound. However, at $40/pound, Westinghouse got stuck with potential liabilities of more than $2 billion (1970s dollars) because of his offer to provide the utilities with cheap fuel. By July 1975, Kirby began blaming the world's uranium cartel, which he believed manipulated the spot price higher to piggyback his company's development plans. Across from Kirby's offices in Pittsburgh's Golden Triangle were the offices of Gulf Oil, a uranium supplier, whom he believed to be a member of the uranium cartel. By September 1975, Westinghouse announced a shortfall of 25,000 metric tons of uranium, and claimed "commercial impracticability" in honoring its nuclear fuel commitments to the 27 utilities. And the lawsuits began.

According to a special report in the Pittsburgh Post-Gazette, Kirby's "suspicions heightened when, in late 1976, he received copies of documents suggesting Gulf and 28 other suppliers had conspired to form a cartel to keep Westinghouse out of the uranium business." The documents were the minutes of a private meeting of uranium suppliers held in Australia. In a bizarre twist of fate, the whistleblower came in the form of Friends of the Earth, which offered Westinghouse additional documents if the nuclear power plant manufacturer would help the environmental group release jailed members in the Philippines. Kirby ran with what he had, ignoring their request, and began a course of intense litigation. The lawsuits were eventually consolidated and heard in a federal district court in Virginia. During the course of the litigation, Westinghouse took its grievances to London's House of Lords, setting international case law about the discovery process in litigations.

What really happened in the 1970's?

Kirby and Westinghouse were caught up in an international trade dispute, during a world revival of the uranium market. Uranium prices had collapsed in December 1959 when the U.S. government placed an embargo on the purchase of foreign uranium for domestic purposes. The embargo came after the nuclear weapons build-up of the 1950s had peaked. In 1959 alone, the U.S. bought 20,000 metric tonnes of uranium for the country's weapon procurement program, about 61 percent from

Canada. Within a week after the embargo, global uranium prices fell by 75 percent. Twenty-four out of the 28 Canadian uranium producers and processors left the business.

Two Canadian crown corporations remained with viable uranium assets to mine and sell. Eldorado Mining and Refining Ltd had stakes in mines at Port Radium, Key Lake and Rabbit Lake. The provincially owned Saskatchewan Mining Development Corporation owned had stakes in Key Lake, Cluff Lake and Down Lake. Before 1942, Eldorado Mining (later re-named El Dorado Nuclear Ltd) had been a privately owned radium company, which in that year was taken over by the Canadian government and made into a crown corporation. During World War II and for the next decade, the company’s raison d’etre was to produce uranium for the U.S. and U.K. nuclear weapons programs.

By 1956, both countries looked elsewhere for their uranium. By 1965, Canada’s production plummeted to 3,000 tonnes from a peak of 12, 000 tonnes annum in 1959. Canada’s uranium exploration came to a standstill, and only three mines remained operational. Boom town Elliot Lake became a ghost town. Lacking buyers, a self-serving Canadian Prime Minister Lester Pearson announced in 1965 that Canada’s exported uranium would only “be used for peaceful purposes only.” Nearly a year earlier, the U.S. government had banned the enrichment of foreign uranium for domestic use, pre-empting any newsworthy value to Pearson’s announcement.

Between 1964 and 1967, more than sixty nuclear reactors were ordered for the U.S. civilian nuclear energy program. Westinghouse’s newly designed light-water reactor created excitement within the industry. During that time, Canadian uranium exploration was taken out of mothballs and production resumed. Hardball shenanigans in Washington kept the uranium ban intact, and global uranium prices reached an all-time nadir of $4/pound. Canada was shut out of the U.S. nuclear fuel cycle market, and Ottawa was forced to stockpile a reported $100 million of uranium during the Nixon presidential administration. By late 1971, Prime Minister Trudeau’s cabinet had reached the end of their rope failing at every step to remove the ban by diplomatic means.

News reports suggest a number of uranium-heavy countries held an initial meeting in Paris in February 1972 to establish a uranium-producer’s alliance, in essence a de facto uranium cartel. Others suggest it was formed in April 1972, after the Canadian government reportedly gave its blessing. Canadian author Gordon Edwards (Canada’s Nuclear History) bluntly wrote, “The purpose of the cartel was to secretly manipulate world uranium prices using a phony bidding system. Hidden quotas were established by representatives from Canada, France, Australia, South Africa and Rio Tinto Zinc (London Stock Exchange: RIO).” Namibia and Niger were also included in the alliance, as was Gulf Oil, at least according to Robert Kirby of Westinghouse.

When the U.S. government re-affirmed its trade embargo in March of that year, a subsequent uranium cartel meeting took place in Johannesburg, South Africa in May 1972. At an Ottawa conference on May 28, 1972, it was reported that Jack Austin, then deputy minister of energy, voiced his concern the cartel could be considered illegal under Canadian law. Nonetheless, the politicians gave the uranium cartel a green light.

The alleged price manipulation was paying off. In 1973, the spot uranium price doubled. By 1976, it doubled again and stayed above $40/pound for nearly four years. It was around that time the alleged cartel disbanded to avoid international anti-trust laws, which Westinghouse was arguing after unleashing a tsunami of litigation. Westinghouse was desperate to escape its liability over the promise of cheap uranium to utilities. In March 1976, the U.S. Department of Justice began investigating possible infringements of U.S. anti-trust laws by the alliance of uranium producers. By mid 1977, a federal grand jury had been formed to pursue the investigations and possibly initiate criminal proceedings.

In a letter dated July 12, 1977, the U.S. Attorney-General wrote to the U.S. District Attorney for the Eastern District of Virginia, explaining the quandary this international episode had caused and discussed invoking immunity to obtain witnesses who would talk about the alleged conspiracy:

“These persons are not likely to come within the personal jurisdiction of the United States courts so long as the Department of Justice continues a sitting grand jury investigation of the international uranium industry; (3) These persons are British subjects and we have determined that it is highly unlikely that their testimony could be obtained through existing arrangements for law enforcement co-operation between the United States and the United Kingdom; (4) The Department of Justice has been largely unable to obtain information from these foreign persons about the subject matter of this investigation…”

By mid 1978, Westinghouse Electric’s complaint against Rio Tinto Zinc in the United Kingdom floundered in that country’s court system. Obtaining evidence in England was markedly different from the U.S. style of depositions.

Conclusion

During this litigious period, Westinghouse settled with several utilities, but continued to pursue the lawsuits. By 1979, Judge Merhige in the U.S. District Court for the Eastern District of Virginia, Richmond Division, ordered

Westinghouse and the utilities to equitably resolve their differences. Westinghouse agreed to concessions that ultimately cost the company nearly $1 billion, but locked up the utilities as long-term customers by providing parts and engineering services for up to 25 years. In quiet out-of-court settlements, the uranium suppliers paid Westinghouse nearly $100 million and supplied the company with uranium.

Besides, there was another cartel in the 1970’s, which posed a far greater risk to the developed nations. From the oil embargo, which began 1973 and throughout the decade, the OPEC oil cartel overshadowed the tiny uranium cartel. Saudi King Faisal’s “oil sword” had a far greater impact on the energy climate, Gross Domestic Product, inflation and quality of lifestyles, than an anxious alliance of uranium producers trying to meet production costs and peddle stockpiled inventory at higher prices. Not only was the oil crisis a more serious affair, but another un-related episode tanked the price of uranium.

Just as the decade was coming to a close, on March 28, 1979, a water pump broke down at the Three Mile Island nuclear plant, about ten miles southeast of the Pennsylvania state capital. It was an unexpected event, heightened Hollywood-style, as the accident coincided with the opening of a new movie called The China Syndrome, starring Jane Fonda, Michael Douglas and Jack Lemmon. In short order, many Americans were persuaded that events within the movie were somehow related to the Three Mile Island event. This was a Hollywood PR man’s dream. Fanning the media flames to capture a larger box office gross, a basically nothing episode (in terms of loss of human life, since no one died from the reactor accident) was transformed into an earth-shattering campaign against the entire nuclear energy industry. Ironically, more died in the movie (one, Jack Lemmon’s character) than as a direct result of the Three Mile Island accident (0 reportedly died).

Hysterical commentary from that era bespoke of a nuclear accident, which would melt down to the earth’s core, as one character in the movie suggested. Unable to distinguish what was movie fiction from scientific reality, the movie’s message left a horrifying memory in the collective minds of the general populace. A general panic followed, and nuclear energy was badly tainted by the accident. As the momentum for building U.S. nuclear power plants came to a grinding halt, overflowing inventories for the raw material to fuel those power plants had once again nullified the uranium exploration and mining sector. It took more than two decades to draw down those built-up uranium inventories, about as long as it has taken for the public to once again accept nuclear energy as a safer, cleaner alternative to fossil-fuel powered electricity.

Why is today’s uranium bull market different? Is the current and spectacular rise in spot uranium prices different today than it was in the early to mid 1970’s, when an alleged uranium cartel reportedly bid up prices to an artificial level? Is that same factor occurring during the current steep rise in the spot price of uranium? Will Toshiba sink into the same quicksand, during the balance of this decade, as Westinghouse Electric once did?

(To Be Continued)