Paid To Wait For PNG Activity to Pick Up

Description

Last week, small cap energy service company **High Arctic Energy Service** (TSX:HWO) announced that it is increasing the monthly dividend from $0.01 to $0.0125, a 25% increase.

The increase takes the annual payment to $0.15 from $0.12 and brings the yield on the stock to 6.2%. With net cash of $13.6 million and 2012 free cash flow of $15 million, the annual cash requirement of $7.5 million to fund the dividend appears more than affordable.

Expect a pause

High Arctic was profiled here in early February and continues to offer solid long-term prospects, particularly for the bargain basement valuation affixed to the shares (P/E ratio of 4).

However, in the recently released quarterly results, management indicated that growth will be a struggle in 2013.

Low natural gas prices and crude oil transport bottlenecks are having a negative impact on the Western Canadian Sedimentary Basin (WCSB) and causing a slowdown for the company's Canadian operations.

In addition, we can expect a temporary plateau in the company's Papua New Guinea operations, which continue to offer compelling upside over the long-term. The company's primary client, Oil Search Limited, is temporarily diverting financial resources towards completing an LNG facility in PNG and away from drilling. This dynamic should reverse once the LNG facility is complete. The project is on track for completion at the end of 2014.

No need to panic

Though subdued near-term drilling in PNG is expected, the company continues to expect growth from its equipment rental platform that it has established in the country. And, the eventual completion of the LNG export facility bodes well for activity levels in this highly undeveloped resource base.

Another consideration that was mentioned in the quarterly release was that the company is negotiating with Oil Search to extend the current service contract that expires at the end of 2013. A new contract will relieve one of the more significant risks involved with this story.

Solid prognosis

Given the stock's current valuation, a slowdown in Canadian activity and a pause in PNG is priced in. If the company can keep printing results like the ones achieved in 2012, the multiple on this name will expand. Earnings growth is not required for a stock price to go up when it trades at a multiple of 4. Assuming nothing breaks in either the Canadian or PNG operations, a worst case scenario for this name is an affordable 6.2% yield as you wait for multiple expansion and earnings growth to take hold.

Follow us on Twitter and Facebook for the latest in Foolish investing.

Fool contributor Iain Butler does not own shares in any of the companies mentioned in this report at this time. The Motley Fool has no positions in the stocks mentioned above.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:HWO (High Arctic Energy Services Inc)

Category

1. Investing

Date
2025/06/30
Date Created
2013/03/25
Author
tmfohcanada