4 Reasons to Buy Whitecap Resources

Description

Strong crude prices continue to spur on further mergers and acquisitions activity in Canada's oil patch.

Intermediate light oil producer **Whitecap Resources** (TSX:WCP) recently entered into an agreement with oil patch heavy weight **Imperial Oil** (TSX:IMO)(NYSE:IMO) to purchase a range of light oil assets located in Western Canada. These assets are focused primarily in Whitecap's Pembina Cardium core area, as well as at Boundary Lake in northeast British Columbia, located just northwest of Whitecap's core Valhalla assets.

The total transaction is valued at around $885 million and net consideration will be $693 million after the disposition of some of Whitecap's Nisku natural gas assets and a $49 million price adjustment. This acquisition reaffirms why Whitecap is fast becoming a significant player in Canada's light oil industry, making it an interesting choice for investors.

1. Latest acquisition significantly boosts oil production
This is Whitecap's second major acquisition in as many months and will significantly boost both its oil reserves and production. It is highly accretive to Whitecap adding additional average daily production of 6,500 barrels of oil. The majority of this production is composed of higher margin oil and non-gas liquids NGLs, which make up 83% and has a low average decline rate, giving it a long production life.

As a result of the acquisition, Whitecap estimates 2014 average daily production will grow a whopping 69% in comparison to 2013 to 33,500 barrels of oil. Clearly this will boost Whitecap's financial performance particularly when coupled with higher oil prices, the price of Canadian light oil (Edmonton Par) has firmed 5% since the start of 2014.

But the differential between Edmonton Par and West Texas Intermediate has widened over the same period by 4%. This is because of waning U.S. demand for Canadian light oil on the back of an explosion in U.S. light oil production on the back of the shale oil boom.

2. Balance sheet remains strong
The acquisition will be funded with a concurrent $500 million bought deal equity financing and debt. Whitecap anticipates its credit facilities will increase to $1 billion as result of the acquisition, with

approximately 70% or $700 million having been drawn-down.

But even after this increase in debt it is expected that post acquisition, Whitecap will have a modest debt-to-cash flow ratio (a key measure of a company's financial strength and ability to manage its debt) of 1.2 times. With this ratio expected to fall to under 1 times by the end of 2015, Whitecap is not overly leveraged and the increased cash flow provided by the significant boost in production will add to its financial strength.

3. Dividend set to continue growing
With Whitecap expecting free cash flow to grow significantly post acquisition, to around $20 million in 2014 and $76 million in 2015, the company has slated another dividend increase. It has committed to boosting the monthly dividend by 10% to $0.0625 per share or $0.75 annualized, giving it a particularly tasty dividend yield of 6%.

When coupled with an expected payout ratio of 96% in 2014, falling to 84% in 2015, the dividend appears sustainable making it compelling reason for income-hungry fools to invest.

4. Remains attractively priced
Whitecap, while not the cheapest of its peers on the basis of its enterprise value of eight times EBITDA and 17 times reserves, certainly offers value for investors when its solid balance sheet and high dividend yield are taken into account.

Fellow Canadian intermediate oil producer **Lightstream Resources** (TSX:LTS), while having an enterprise value of a mere five times EBITDA and 16 times its oil reserves, has a significantly weaker balance sheet. Even after slashing capital expenditure and its dividend by half in late 2013 it still has worrying debt-load of more than three times cash flow.

Large-cap light oil producer **Crescent Point Energy** (TSX:CPG)(NYSE:CPG) continues to trade at a premium, with an enterprise-value of nine times EBITDA and 28 times its oil reserves, making it appear expensive in comparison to Whitecap.

Foolish bottom line
Whitecap's latest acquisition not only highlights the renewed M&A activity in the patch being driven by strong oil prices, but why it is fast becoming a desirable opportunity for income-hungry investors — particularly when it's solid balance sheet, strong cash flow generation and attractive dividend yield are taken into account.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:VRN (Veren)
2. NYSEMKT:IMO (Imperial Oil Limited)
3. TSX:IMO (Imperial Oil Limited)
4. TSX:VRN (Veren Inc.)
5. TSX:WCP (Whitecap Resources Inc.)

Category

1. Investing

Date
2025/08/23
Date Created
2014/03/18
Author
mattdsmith