The Stock Picker's Guide to Husky Energy for 2014

Description

Integrated energy heavyweight **Husky Energy** (TSX: HSE) continues to unlock and deliver solid returns for shareholders from its turnaround strategy. It was back in 2010 that Husky's management realized it needed to alter the strategic direction of the company and implement a plan allowing it to unlock the considerable value held in its diverse range of assets.

Oil reserves continue to grow
Not only did Husky deliver solid results for 2013 but it recently reported that its oil and gas reserves had grown significantly during the year. For 2013 Husky's oil reserves grew at a faster pace than its oil production.

This was the result of the addition of considerable oil and gas reserves in its oil sands business, the development of the Ansell liquids-rich gas resource play, and increased heavy oil recovery from thermal projects in Western Canada. This saw Husky's total oil reserves grow by 7% to an impressive 3.1 billion barrels gross before royalties.

However, even more impressive is Husky's 2013 reserves replacement ratio of 164%. Essentially, this ratio measures the pace at which an oil producer is able to replace oil reserves as they are depleted by production. It's an important metric for measuring the sustainability of an oil company's production.

Husky's reserves replacement ratio compares favorably to a number of Canadian and international oil heavyweights. It is superior to **Exxon Mobil's** (NYSE: XOM) 106%, **Chevron's** (NYSE: CVX) 112%, **Suncor's** (TSX: SU)(NYSE: SU) 64% and **Canadian Natural Resources** (TSX: CNQ)(NYSE: CNQ) 143%. But is lower than the whopping 214% reported by **Cenovus** (TSX: CVE)(NYSE: CVE) for 2013.

Positive future outlook
After delivering a solid operational and financial performance in 2013, Husky is well positioned to continue this success in 2014 and beyond. Husky's management has provided guidance that 2014 production will grow by between 6% and 14% in comparison to 2013. Coupled with crude prices ofover $90 per barrel and a narrowing price differential between Canadian heavy crude and West Texas Intermediate, Husky's revenue, cash flow, and ultimately bottom line will grow.

The company also firmly has its eyes on the future and continues to focus on developing its core assets. Husky has allocated $4.8 billion in capital expenditure for 2014, to be allocated to a range of exploration and development projects. This will see a total of 865 wells drilled in 2014 with a focus on higher margin oil and natural liquids, which should see Husky grow its margins and boost its netback per barrel.

In the short term, a range of projects are set for completion, including the Sandall heavy oil thermal project, expected to commence production in the first half of 2014 with 3,500 barrels of crude daily. But more importantly the landmark Liwan Gas Project is in the final stages of commissioning and production is expected to come on stream in early 2014.

Initial production is expected to be 61,000 barrels of crude and 257 million cubic feet of natural gas daily. This project is the largest investment in Husky's history. It owns a 49% stake, with the other 51% held by CNOOC, and gives Husky access to lucrative Asian energy markets.

More importantly, prices for natural gas produced from the project will be fixed at between $11 and $13 per thousand cubic feet, which is around double the current spot price for natural gas. This removes a significant amount of uncertainty around natural gas prices and will boost Husky's margins and bottom line.

Continues to reward investors with a tasty dividend yield
An appealing aspect of Husky is the company's solid dividend yield of 3.7%, which compares favorably with its peers. The yield is higher than the risk-free rate as well as superior to Exxon's 2.7%, Chevron's 3.5%, Suncor's 2.5%, Canadian Natural Resources 2.2%, and Cenvous' 3.5% dividend yields.

When the dividend payout ratio of 65% is considered as a quick and dirty measure of dividend sustainability, the dividend and its yield appear sustainable. Even more appealing is the dividend has continued to grow since inception in 2001, with a compound annual growth rate of 11% since then. Patient, income-hungry investors will continue to be rewarded with steadily growing dividend.

Foolish bottom line
Husky's varied portfolio of quality oil and gas assets, growing oil reserves and production coupled with a steadily growing dividend with an attractive yield make it a particularly compelling investment.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:XOM (Exxon Mobil Corporation)

2. TSX:CNQ (Canadian Natural Resources Limited)
3. TSX:CVE (Cenovus Energy Inc.)
4. TSX:SU (Suncor Energy Inc.)

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