



Can Encana Rally Past its Recent Highs?

Description

With ongoing uncertainty surrounding the direction of natural gas prices, **Encana Corporation** (TSX: ECA)(NYSE: ECA) continues to divest itself of non-core assets as it moves to focus on higher margin oil and natural gas liquids production. This has seen the company target increased investment in the Duvernay and Montney shales while divesting itself of dry natural gas assets.

Already the success of Encana's restructure has seen its share price rally, recently hitting a 52-week high. Is there sufficient momentum for the rally to continue?

Turnaround strategy continues to gain traction

A key plank of Encana's turnaround strategy has been its focus on the divestment of noncore assets, the latest being the sale of its natural gas properties in the Jonah field in Wyoming to Stabilis Energy, for approximately U.S. \$1.8 billion. Another important plank is the increasing focus on higher margin liquids production, with an increase of 30% targeted for 2014.

This is a key reason for Encana's increased focus on the Montney, with the shale formation being extremely rich in higher margin natural gas liquids including butane, propane, and condensate. Encana has committed to investing between \$800 million and \$900 million, or a roughly third of its total capital budget for 2014, in its assets in that formation alone. Another compelling reason for Encana's focus on the Montney is that the formation has some of the lowest development costs of any of the natural gas plays in Canada, according to the National Energy Board.

Such a strong growth in natural gas liquids will boost Encana's profitability with it estimating 2014 netbacks – a key measure of profitability – will increase by 10% in comparison to 2013. This will also boost cash flow – a key requirement for oil and gas companies because of the capital-intensive nature of the industry – which for 2014 is estimated to grow by 5% in comparison to 2013 to \$2.4 billion.

Another positive development for investors is Encana's plans to unlock the value held in its Clearwater Royalty business through an initial public offering in 2014. It has been estimated by industry analysts the IPO of this business could net Encana anywhere between \$1.5 billion and \$2.5 billion. These proceeds will give Encana considerable flexibility with the continued implementation of its turnaround

strategy, providing a range of opportunities to strengthen its balance sheet and grow the business.

Foolish bottom line

Under the leadership of Chief Executive Doug Suttles, Encana continues to go from strength to strength as the turnaround program gains traction and value is unlocked through the sale of non-core assets. Despite the company having recently hit a 52-week high, it is clear over the long term there is further room for its share price to rally as Encana's financial results start to reflect the gains made through this program in 2014.

CATEGORY

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