What to Watch When Cenovus Energy Reports Next Week

Description

Cenovus Energy (TSX: CVE)(NYSE: CVE) is set to publish its latest earnings report on Wednesday. Thanks to improving conditions in the Alberta oil sands, the Street is generally optimistic. However, production problems at the firm's mammoth Foster Creek project remain a dark cloud over the stock. Let's take an early look at what we're likely to see in this report.

Stats on Cenovus

Analyst EPS Estimate	$0.48
Year-Ago EPS	$0.52
Revenue Estimate	$4.67B
Change from Year Ago Revenue	8.00%
Earnings Beats in Past 4 Quarters	1

Source: Yahoo! Finance

Will Cenovus impress the Street this quarter?

Just about everything is going right in Alberta's oil patch. U.S. President Barack Obama's deliberations on **TransCanada's** Keystone XL pipeline are becoming less pressing as trains begin carrying oil sands bitumen. Cold weather over North America and a falling Canadian dollar are also helping to lift energy prices.

This has put a bid underneath the stock, with Cenovus shares rallying over 14% off their February lows. Bay Street is also more optimistic about the company's earnings prospects, adding $0.06 to the consensus earnings per share estimate for the fourth quarter.

However, investors are concerned that the company's Foster Creek oil sands project, one of the first commercial facilities to use steam to extract bitumen, is showing signs of age. Last quarter, the company reported the project produced an average of about 53,000 barrels per day, or bpd, of bitumen in 2013, down 8% compared to the year before. Meanwhile, operating costs have increased 13% year-over-year to $13.77 per barrel.

The upset in production comes as the field, which has been in production for over a decade, enters uncharted territory. After injecting steam underground to extract bitumen for years, Cenovus is struggling to figure out how to optimize production from its wells. It's work that Chief Executive Brian Ferguson likens to going to the moon.

Heading into the next phase of development, Cenovus plans to inject steam for an extra month. Analysts, however, are worried about the new plan. Injecting more steam is expensive and is expected to add $0.40 per barrel in operating expenses. More steam also increases water use and carbon emissions, which could draw the ire of environmentalists.

Cenovus is also looking for ways to improve the economics of shipping bitumen by rail in order to avoid pipeline jams. Oil sands producers are increasingly eager to cut costs as rail moves from a stop-over to a permanent feature of the industry.

One problem operators face is that bitumen is too thick to flow freely on its own through pipelines. It must be diluted with an ultra-light hydrocarbon called condensate. However, condensate is expensive, trading for as much as a 10% premium to West Texas Intermediate per barrel.

To get around this expense Cenovus is experimenting with methods to recover this condensate before shipping it in railcars. If the company can pull this off, Cenovus significantly reduce the per-barrel cost of transporting crude by rail. Perhaps in time, rail costs could even achieving parity with pipelines.

Foolish bottom line

In Cenovus' upcoming earnings report, watch to see if management can soothe fears regarding its Foster Creek megaproject. After the stock's recent run, investors are counting on the company to find a way to boost production while controlling expenses. It's a tall order if the company is to maintain its current valuation.

CATEGORY

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