3 Key Signs Lightstream Resources' Turnaround Is Working

Description

Troubled intermediate oil producer **Lightstream Resources** (TSX: LTS) continues to report solid operational and financial results, indicating that its strategic turnaround program is working. This is despite the volatile outlook for the price of crude and the flood of Canadian oil and gas assets on the market as a range of players in Canada's oil patch seek to reinvent themselves and dispose of non-core assets.

It was only in late 2013 when investors lost patience with Lightstream and its management, who had continued to overpromise and underdeliver. The company's share price plunged precipitously to new lows, reaching $5.43 per share, before bouncing back by 32%. But what signs show that Lightstream is making progress?

1. This key profit metric continues to grow strongly

One of the most pleasing aspects of Lightstream's performance in the first quarter of 2014 was the significant growth in its operating netback per barrel of crude produced. It shot up to $56.11, a massive increase of 24% compared to the previous quarter and 13% over the equivalent period in the previous year, making it one of the best operating netbacks in the oil patch.

In fact, the only Canadian oil companies delivering higher netbacks are those with access to Brent crude pricing -– which trades at a premium to West Texas Intermediate –- operating in lower cost environments like Latin America.

Lightstream's netback is well above the industry average of $42 per barrel for oil companies operating in North America. It's superior to some of the most efficient operators in the patch, including **Crescent Point Energy's** (TSX: CPG)(NYSE: CPG) netback of $52.65 and **Whitecap Resources'** (TSX: WCP) of $45.80. It is also superior to several other troubled Canadian oil producers that are also engaged in their own turnaround programs. This includes **Pengrowth Energy** (TSX: PGF)(NYSE: PGH) and **Penn West Petroleum** (TSX: PWT)(NYSE: PWE), which reported netbacks of $29.71 and $36.67 respectively for the same period.

Lightstream's higher operating netback can be primarily attributed to higher realized prices for both crude liquids and natural gas, which exceeded Lightstream's assumed pricing in its 2014 guidance.

2. Capital expenditures have fallen drastically

One of the key reasons why investors lost confidence in Lightstream was the company's addiction to debt. Not only was it using debt to fund the majority of its capital investment, but it was leaking capital through paying a dividend it couldn't afford.

But in late November 2013, the company slashed the dividend by 50%. It also cut the budget for capital expenditure in 2014 by 25% while still planning to produce amounts of oil and gas comparable to those of 2013. To date, the company's management has met this promise, with capital expenditures in the first quarter of 2014 down a healthy 34% compared to the equivalent quarter in 2013, while production output has fallen by only 10% for the same period.

Even more promising is that despite the significant drop in capital expenditure, Lightstream drilled only three fewer wells compared to the same period in 2013 yet still had a higher success rate — 100% compared to 98%.

Lightstream's success in reducing capital outflows while also improving drilling results shows that the smarter targeted use of capital in proven oil and gas plays is paying dividends.

3. Liquidity continues to grow

An important part of Lightstream's turnaround strategy is rebuilding the shattered balance sheet; the 2014 Q1 results show this is clearly underway. The sale of non-core assets is an important element of this strategy. In the first quarter alone, Lightstream has achieved asset sales of $253 million, or 85% of the $300 million targeted for 2014.

During that quarter, Lightstream was also able to increase its liquidity by reducing its credit facility from $1.4 billion to $1.3 billion and extending the maturity date by one year from June 2016 to June 2017.

As a result, the company's total debt fell by 11% compared to the previous quarter, though it increased marginally year-over-year by 2%. This reduction in debt saw Lightstream's net debt fall to just under three times funds flow from operations.

Despite funds flow from operations declining marginally during the first quarter, the debt reduction indicates that Lightstream's 2015 target of net debt being less than 2.5 times its funds flow from operations is achievable.

Even with Lightstream's share price having bounced back by 19% for the year-to-date it still appears very attractively priced. Its enterprise value is a mere six times EBITDA and 20 times its oil reserves. This is considerably lower than Crescent Point's EV of nine times EBITDA and 32 times reserves or Whitecap's EV of 10 times EBITDA and 21 times its oil reserves.

Clearly, there is some way to go before Lightstream completes its turnaround plan, but as the 2014 Q1 results indicate, the company's performance is improving. All of its goals appear achievable within the targeted time frame, and the earmarked non-core asset sales of $45 million during 2014 will go a long way towards mending the company's balance sheet.

These indicators show that Lightstream stands a strong chance of successfully completing its turnaround program and unlocking value for shareholders.

CATEGORY

1. Investing

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1. TSX:VRN (Veren Inc.)
2. TSX:WCP (Whitecap Resources Inc.)

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