4 Things Canadian Natural Resources Limited's Management Wants You to Know

Description

Canadian Natural Resources Limited (TSX: CNQ) (NYSE: CNQ) is transitioning its portfolio towards long-life, low decline assets like Horizon and Pelican Lake. As it does, the company will generate a significant amount of sustainable cash flow. However, having additional free cash flow is a challenge as the management team needs to prudently allocate this capital. On the second-quarter conference call the company's President Steve Laut outlined its four priorities for this extra cash.

"Our first priority is resource development, and in 2014, we're close to optimal capital allocation."

Canadian Natural Resources is putting a priority on organic growth that drives value. The company is investing in heavy oil production, for example, because it delivers the highest returns on capital in its Canadian portfolio along with strong free cash flow. In addition to that, it's investing in offshore wells in Africa because these could provide huge upside.

Earlier this year the company announced the discovery of oil offshore Cote d'Ivoire, and it's very excited about deepwater explorations in South Africa. These projects will be what fuel future returns and cash flow, which is why the company is making these investments its top priority.

"Our second priority is returning cash to shareholders via dividends and share buybacks."

Mr. Laut noted that the company's dividends have increased for the last 14 years, however, since completion of the first phase of Horizon has come online the company has increased its dividend by a 35% compound annual growth rate. Further, he noted that the company spent $372 million to buy back 8.165 million shares so far this year. At this level the company's share buyback ranked Canadian Natural Resources in the top tier of its peer group. Clearly, the company is giving a priority to returning cash to investors.

"… Thirdly, through opportunistic acquisitions. The recent asset acquisitions we have made in 2014 are opportunistic and clearly demonstrate our ability to be nimble."

Canadian Natural Resources demonstrated this earlier this year when it spent $3.125 billion to buy **Devon Energy Corp.'s** (NYSE: DVN) conventional assets in Canada. The assets it picked up were in areas that were either adjacent to or in close proximity to its own assets in Western Canada. That provides the company with cost synergies so it can make more money on the assets than it otherwise could. Further, it was also opportunistic in this deal as it noted in the deal announcement that it can package the royalty revenue stream it acquired along with its own royalty stream in a move to monetize both and maximize shareholder value.

"… Fourthly, debt repayment. Our balance sheet is very strong and is the last priority for free cash flow allocation. Canadian Natural's strategy works, and we continue to balance the allocation of free cash flow effectively."

While debt repayment is last on its list, Canadian Natural Resources will pay down its debt if it makes sense to do so. While investors shouldn't expect the company to pare down debt too much, however, having the flexibility to opportunistically reduce its higher interest debt could create additional value for investors.

Investor takeaway

Canadian Natural Resources' priorities couldn't be better for shareholders. The company is putting organic growth ahead of acquisitions and it's giving a priority to dividends. The company will also buy back shares or pay down debt if either makes the most sense for investors. By sticking to these priorities the company should be able to maximize long-term returns from the additional cash flow heading its way from Pelican Lake and Horizon.

CATEGORY

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