Parex Resources Inc. Offers Better Upside Compared to Its Oil Patch Peers

Description

When hunting for value among Canadian energy companies, investors usually stick to the well-known names in the patch that have solid growth prospects like **Crescent Point Energy Corp** (TSX: CPG)(NYSE: CPG) or appear undervalued like **Penn West Petroleum Ltd** (TSX: PWT)(NYSE: PWE).

However, many investors don't know that Canada's energy patch is home to adventurous oil producers that have identified considerable opportunities in regions once thought of as off-limits by mainstream energy companies. One of those companies that stands out is intermediate oil producer **Parex Resources Inc.** (TSX: PXT), which operates predominantly in Colombia.

I believe Parex offers considerable potential for investors superior to many of the operators in the patch solely focused on Canada and North America. Here are three reasons why.

1. Its outlook continues to be upgraded by industry analysts

It was only in April this year that I explained how Parex could easily hit $15 per share; since then its share price has spiked a massive 40% and is now trading at $14 per share. This is only 7% shy of my $15 per share target, and there are a range of tailwinds that are set to push the price still higher.

The company's strengths have been recognized by a range of institutions, and a number of analysts have recently upgraded their outlooks. In July this year, the consensus target price increased to $16 per share, or 78% higher than at the start of 2014. The highest target price has been set by analysts at the **Royal Bank of Canada** at $18.50 per share.

2. Its oil production continues to rocket skyward

A key aspect of the company's continuing success has been the strong growth of its oil production. In the second quarter of 2014 it continued to grow strongly, up a healthy 8% compared to the previous quarter and a massive 29% compared to the equivalent quarter in the previous year.

An important driver of this boost in crude production was the closing of its acquisition of Verano Energy Limited, which increased production by 4,000 barrels of crude per day.

3. It continues to generate healthy margins

This oil production is heavily weighted to oil and other petroleum liquids, making up well over 95% of Parex's total production for the quarter. This production mix is superior to those of many players in the patch solely focused on Canada and North America. For the same period, Crescent Point's production weighting was 91% oil and other liquids, while for the previous quarter troubled oil producer Penn West's weighting was 65%.

This is an important aspect of Parex's operations, as it reduces the company's exposure to volatile and softer natural gas prices, which is affecting the profitability of a number of operators in the patch including Penn West.

Another important aspect of the company's oil production is that its crude prices are benchmarked to Brent, which for the last four years has traded at a premium to West Texas Intermediate, the benchmark oil price for North American refining markets.

At this time the premium is 9% and is expected to widen as the U.S. shale oil boom floods North American refining markets with light sweet crude, applying further downward pressure to WTI prices. As a result, Parex is able to consistently sell its crude at an average realized price well above the price for WTI, unlike Crescent Point Energy and Penn West, further boosting its profitability. These factors also bode poorly for the profitability of players in the patch like Crescent Point and Penn West that are unable to access refining markets outside of North America and have their oil sales benchmarked to WTI.

This benchmarking, coupled with Parex's portfolio of high-quality oil assets located in Colombia's Llanos and Putumayo basins, sees it continue to report some of the best netbacks in the industry. For the second quarter, Parex reported a monster netback of $61.65 per barrel of crude produced, superior to the majority of its peers operating in North America. This netback is 13% higher than Crescent Point's own healthy netback of $54.75 and 68% higher than Penn West's $36.67 per barrel.

Clearly, Parex is an exceptional company and currently offers investors further upside despite appreciating a massive 109% for the year to date. It continues to generate solid margins from its consistently growing production, which is superior to oil producers operating exclusively in North America, and the ability to benchmark its oil sales to Brent offers it a handy financial advantage, with Brent trading at an ever-widening premium to WTI.

CATEGORY

1. Investing

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1. NYSE:VRN (Veren)
2. TSX:PXT (PAREX RESOURCES INC)
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