2 Reasons to Avoid Penn West Petroleum Ltd, and 1 Stock to Buy Instead

Description

Life hasn't been fun recently for shareholders of **Penn West Petroleum** (TSX: PWT)(NYSE: PWE). First came an overambitious expansion plan, then a stretched balance sheet, then asset sales into a buyer's market, and most recently an accounting scandal. Since early 2011, the shares have fallen by roughly 70%.

At this point, no one wants to touch Penn West with a 50-foot pole. So if the company is able to turn itself around, the share price gains could be substantial. Is it worth the risk?

Well, you should be very careful before buying Penn West shares. On that note, below we take a look at two reasons to avoid this energy producer, then we take a look at a stock to buy instead.

Reasons to avoid Penn West

1. A poor track record

Saying that Penn West has a poor track record might be the understatement of the year. But it's worth taking a closer look, just to make sure we understand the company's problems.

On the operational side, everything has been a mess. Penn West grew quickly through acquisitions in the income trust era, but has seen its production fall every year since 2008, after its $3.6 billion acquisition of Canetic Resources Trust. The integration was done very poorly, corporate cultures clashed, and costs skyrocketed. The aftermath has been messy too, with asset sales done for far less than what analysts were expecting.

And these problems have appeared to spread to the financial side. In fact just last year Penn West was accused of manipulating the price of stock options, and also faced questions about its refusal to write down goodwill (i.e., accept defeat on its acquisitions).

So when the most recent accounting scandal broke, it wasn't much of a shock. But are these the kind of people you want to entrust your savings to?

2. An unsustainable dividend

Penn West does have one thing that investors seem to like very much: a big fat dividend. In fact, even after cutting the payout by nearly half in 2013, the company still has one of the top five yields in the **S&P/TSX 60**.

But this is not a company that should be paying a dividend at all. Its balance sheet is stretched, free cash flow is hard to come by, and after the latest accounting scandal, it seems it may be violating debt covenants.

Unless Penn West turns itself around, and quickly, its dividend has more room to fall.

1 stock to buy instead: Cenovus

On that note, it's time for a more cheery subject. And **Cenovus Energy** (TSX: CVE)(NYSE: CVE) is able to play that role.

Cenovus has some of the best assets in the entire energy patch at Christina Lake and Foster Creek. This brings numerous benefits. First, there is no need for expensive acquisitions to grow production. Second, the company will remain profitable even if oil prices fall.

Cenovus also has a much better corporate culture, and pays a modest dividend that it can actually afford. The only similarity it has with Penn West is a lagging share price – over the past 12 months, its shares are up 12%, which trails the Canadian energy index by 18 percentage points. So this is your chance to pick up a quality company without overpaying.

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