Billionaire Investor Prem Watsa Is Buying Penn West Petroleum Ltd. Shares; Should You?

Description

Try as I might, I'm never going to be able to take a slap shot like Sidney Crosby. I won't ever be able to throw a knuckleball like R.A. Dickey. And I'll never be able to jump high enough to dunk. Heck, I have problems consistently making baskets playing horse. Unfortunately, I'll never be able to play sports like the pros.

Good thing this type of disparity doesn't exist in investing. It turns out it's really easy to invest just like the best in the world do.

Take Prem Watsa, CEO and Chairman of **Fairfax Financial Holdings Ltd.** (TSX: FFH). He took control of Fairfax in 1985, modeling it just like a mini **Berkshire Hathaway**. Like Warren Buffett, Watsa used the proceeds from insurance premiums — called the float — to invest in a myriad of undervalued and unloved stocks.

The results have been remarkable. Since Watsa took over, Fairfax Financial has increased its book value by more than 20% a year, and that's even after not doing so well in 2012-13. Those are the kind of results that put Watsa in a pretty select group.

Naturally, I think you should be paying attention to what he's doing. Which is why I'm going to tell you about his newest position, **Penn West Petroleum Ltd.** (TSX: PWT)(NYSE: PWE).

How you can get a leg up on one of the best investors of all time

Each quarter, the Securities and Exchange Commission requires the largest investors to disclose their portfolios. Because large investors have so much clout, they're required to keep the general public aware of what they're doing.

There are two steps to this process. If an investor acquires more than 5% of a publicly traded company's shares, regulators require it get disclosed. Once the stake hits 10%, another disclosure is required. If an large investor hasn't yet reached the 5% threshold, it just gets reported after the quarter is completed, on a filing called a 13F.

Watsa is one of the investors required to file a 13F form, meaning once a quarter we get to take a peak at his portfolio. While it was mostly the same as last quarter, he did disclose the beginning of a small position in Penn West.

Watsa's stake in the company was worth a little over $2 million at the end of the quarter. Back then, Penn West's shares traded at $7.59 each. Today, thanks to the decline in the price of oil, you can back up shares for $4.72. That's a discount of at least 38% less than Watsa paid.

Thus, if you buy shares in Penn West today, you'll not only be piggybacking on a legend, but you'll be getting in at a much cheaper price.

Why Penn West?

Although I can't be sure, I wouldn't be surprised if Watsa is buying more Penn West. If he liked it above $7 per share, he must really like it now. Not much has changed.

On a price-to-book value basis, Penn West is ridiculously cheap. The company's tangible book value is more than $11 per share, which implies an upside of more than 230% from these levels, assuming shares can ever get back to book value. Most oil companies trade at between 1.5 and 2.5 times book, as a comparison.

The company is aggressively selling off non-core assets to pay down debt. It is on pace to pay down more than $1 billion since it started its debt reduction program in 2013. It has also cut costs by 23% over the last 12 months, and has shifted most of its capital expenditures to three main oilfields, each of which have good long-term prospects.

Production is scheduled to come in at approximately 105,000 boe/d in 2015, and grow 13% annually until 2019. Most of that production is going to come from oil as well, as the company continues to move away from natural gas. This could end up looking pretty smart when oil prices recover.

Penn West is not without risks. Its 12% dividend will probably end up being cut or eliminated. It still has a decent amount of debt. But if Watsa likes the name, you should consider it too.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. TSX:FFH (Fairfax Financial Holdings Limited)

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