The Case for Penn West Petroleum Ltd.

Description

Numerous commentators, including yours truly, have written about the risks of an investment in **Penn West Petroleum Ltd.** (TSX: PWT)(NYSE: PWE) in recent months.

That being said, now may be the perfect opportunity to bet on the company. Below we take a closer look.

Penn West: The background story

Penn West is essentially the poster child for everything that's gone wrong with the Canadian energy sector. Its problems started back in 2008, when it acquired Canetic Resources Trust for $3.6 billion. Unfortunately, output from this acquisition did not meet expectations, and production has shrunk every year since 2008.

More recently, the company got bogged down by its mountainous debt load, and has been selling assets to relieve the burden. But that comes with a problem too – Penn West has been selling assets into a buyer's market, and some sales have fetched prices well below expectations. Making matters worse, an accounting scandal emerged this year, which required $400 million worth of restatements. Plunging oil prices have only added to the misery.

The company's stock is down by nearly 70% over the last three years.

A potential turnaround?

At this point, Penn West seems like a very risky play. But with the stock price so depressed, is there any upside?

Well, the company is currently valued at about $4.7 billion, including debt. And production is expected to total somewhere around 100,000 barrels of oil equivalent per day next year. So at less than $50,000 per flowing barrel, Penn West is trading at an attractive price.

Providing further upside, the company also has various other assets that are not yet producing. Penn

West plans to sell much of these assets, in an effort to further pay down debt. While this will be challenging in the current oil price environment, it's good to see the company continuing with this strategy.

Other reasons to bet on Penn West

Of course Penn West's future depends largely on energy prices – higher energy prices not only increase cash flow, but also make the company's non-core assets easier to sell. And energy prices could get a boost soon, with OPEC nations meeting Thursday in Vienna.

Secondly, Penn West still has a big dividend, currently yielding more than 10%. This has two benefits. Not only do shareholders get paid while they wait for a turnaround, but the dividend forces the company to spend money very frugally. After all, if Penn West returns to its old "drill, baby, drill" strategy, then it won't be able to afford the payout.

So even though Penn West is very risky, you might want to add a small stake to your portfolio.

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bensinclair