Should You Buy Cenovus Energy Inc After its Latest Update?

Description

On Wednesday, **Cenovus Energy Inc.** (TSX:CVE)(NYSE:CVE) became the latest Canadian energy company to cut its capital spending plans.

It's the second time Cenovus has done so in the last couple of months. Back in December, the company announced a 2015 budget of $2.5 billion to $2.7 billion, a reduction of 15% relative to 2014. And now, that budget has been reduced by a further 27%, and is set at $1.8 billion to $2.0 billion.

Cenovus has made it very clear why the budget has been altered — oil prices have continued to deteriorate, which the company did not expect back in December. At the time, it expected oil prices to average US$77 per barrel in 2015. Now it expects a US$50.50 average price this year, a much more realistic number.

So what does this mean for shareholders of Cenovus? And what does it mean for the industry as a whole? Below we take a look.

Some important details about the budget cut

Crucially, Cenovus is not expecting production to suffer from this budget cut. The company is still forecasting 2015 production of 195,000 to 212,000 barrels per day of output, down only 1% from December's guidance. How exactly is this possible?

Well, Cenovus is deferring most of its conventional drilling program in southern Alberta and Saskatchewan. Other longer-term projects are also being suspended. Meanwhile, expansion plans remain unchanged at the company's two big core operations, Christina Lake and Foster Creek.

A strong company

If you're looking to bet on an oil rebound, Cenovus is a great way to do so. The company is very financially strong, with a debt-to-capitalization ratio of only 33%. Furthermore, only about half of 2015 production is projected to be unhedged crude oil — the rest is hedged oil, refined oil, or natural gas. In other words, the company can survive a prolonged oil slump, significantly reducing the risk of an investment.

Best of all, the expansion plans at Christina Lake and Foster Creek are already two-thirds complete. As a result, they only need oil prices of US$40 to US$45 to earn a 9% return on investment from this point forward.

Why investors should be worried

We've seen this before. An oil company cuts its capital budget, but is not willing to cut production. Meanwhile, its growth projects are mostly complete, and are not worth cancelling at this point. Cenovus is also pursuing up to $500 million in cost savings over the next few years.

Unfortunately for investors, lots of companies are doing the exact same things. And for that reason, don't expect supply to take a hit anytime soon. Instead, you should expect low oil prices to persist for a while.

Fortunately, there's one energy company in particular that doesn't need high prices to thrive. It's also The Motley Fool's top stock pick for 2015. You can read all about it in the free report below.

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