Crude Oil Slide Forces Cenovus Energy Inc. to Take Another Slice Out of Growth

Description

Cenovus Energy Inc. (TSX:CVE)(NYSE:CVE) announced this week that it would take another slice out of its 2015 capex plan again in response to the continued weakness in the oil market.

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This time Canada's second largest independent oil producer is slicing $700 million from its spending plan, which is on top of the 15% slice the company took out of its spending plan late last year. In doing so it joins a growing number of oil companies moving ahead with a second revision to capex spending for 2015 as the oil market continues to show no signs that it will turnaround any time soon.

What's getting cut

Because crude oil prices continue to slide, the company is taking action to keep its balance sheet from weakening. Originally, the company expected its cash flow to be $2.6-2.9 billion in 2015, however, the unrelenting sell-off in oil prices is forcing the company to revise its guidance. It now sees cash flow of just $1.3-1.5 billion in 2015, which is 49% lower than it previously expected. Because of this it's slicing $700 million, or 27% more off of its 2015 capex plan.

Cenovus Energy is taking a pretty bold step in its revised plan. The company is suspending nearly all of its conventional drilling programs in Southern Alberta and Saskatchewan. In addition, it's deferring spending on other long-dated oil sands expansions and other greenfield projects. Most of these projects would have resulted in longer term growth, which is why the company's actual production guidance is just changing by 1% as it still expects low single-digit production growth in 2015.

Surviving the ax

Cenovus Energy is keeping the bulk of its core spending plan intact. For example, it's not altering its construction plans for Christian Lake's phase F or the phase G expansion of Foster Creek, both of which are part of a joint venture with **ConocoPhillips** (NYSE: COP). The fact that its partner is funding half of these projects is one reason why Cenovus isn't cutting these programs. However, it also helps that these expansions have strong economics as Cenovus can earn a 9% return on investment with oil prices in the range of US$40-$45 per barrel. That low cost oil will come in handy in today's low oil price environment.

What this means for investors

Cenovus Energy is taking prudent actions now in order to ensure it doesn't come out of the downturn in a weakened state. Instead, it's deferring longer-term projects such as its emerging oil sands assets as well as lower return conventional oil drilling. Instead, it's funneling all of its cash flow into projects that can still earn a decent return at current oil prices. This will put it in a much better position to thrive once oil prices turn around, which is something Cenovus Energy expects to see at some point in the future.

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Date
2025/07/03
Date Created
2015/01/29
Author
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