



Why Pengrowth Energy Corp. Is One of the Best-Levered Plays on a Rebound in Crude

Description

Despite having its outlook downgraded earlier this month, oil producer **Pengrowth Energy Corp.** (TSX:PGF)(NYSE:PGH) is fast shaping up as one of the best contrarian plays on a rebound in oil.

Now what?

Pengrowth's full year results were somewhat disappointing, with the company reporting a net loss of \$579 million. The key driver of this was a series of non-cash impairment charges. These charges were recorded against a range of assets because of declining values triggered by significantly softer oil prices. It also missed its forecast 2014 EBITDA by 3%, though impressively, it did meet guidance for oil production, cash flow, and expenses for the year.

Despite this disappointing result, there are a number of factors that indicate Pengrowth has the potential to deliver outsized gains for investors willing to take a risk and bet on a rebound in oil.

A key factor is Pengrowth's Lindbergh thermal project, which is set to achieve meaningful production during the first half of 2015. Commercial production of 12,500 barrels daily commenced in December 2014, and after the completion of additional phases, is expected to deliver 40,000-50,000 barrels of crude daily.

The value of Pengrowth's oil reserves highlights just how undervalued the company is. Not only did the company boost those reserves during 2014 by 17% compared to 2013, but they have an independently assessed after-tax value of \$4.6 billion or \$8.60 per share. This is almost 1.5 times greater than Pengrowth's current share price, illustrating just how much the market has undervalued the company at this time.

Nonetheless, this does not take into account the costs or risks associated with developing those reserves to the point where they are commercially recoverable.

The final reason why I find Pengrowth an attractive contrarian play on a rebound in crude is its approach to managing commodity risk.

For 2015, the company has hedged 75% of its forecast oil production at \$94 per barrel and 56% of its 2016 production at \$90 per barrel. This, coupled with a 78% cut in capital expenditures compared to 2014, along with 2015 oil production expected to grow by up to 2%, will help to maintain cash flow so as to protect the ongoing funding of projects under development.

So what?

Pengrowth is well positioned to weather the current storm in oil prices because of its hedging position.

However, it is the value of its underlying oil assets, which are worth almost 1.5 times its current share price, along with the successful development of the Lindbergh project, which highlights the potential upside available to investors. I believe this makes Pengrowth an attractive levered play on a rebound in crude for investors who can stomach the risks associated with oil exploration and production in the current operating environment.

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