Why Canadian Western Bank Is a Better Bet Than Canadian Natural Resources Ltd.

Description

As oil prices remain below US$50, many investors are convinced this cannot last. After all, producers in the United States are not drilling like they used to. Demand should eventually see a boost too, thanks to low gasoline prices. These investors have been pouring their money into oil producers. I think this is a mistake.

You should bet on oil by investing in **Canadian Western Bank** (TSX:CWB). We take a look at why CWB is a better bet than **Canadian Natural Resources Ltd.** (TSX:CNQ)(NYSE:CNQ).

CWB—an introduction

Canadian Western Bank is one of Canada's most respected financial institutions, and for good reason. Its stock price has easily outperformed the big six banks over the past decade, and this has come without taking outsized risk.

In fact, over the last 10 years, its loan losses have averaged just 0.11% of loans outstanding, well below those of the bigger banks. Even during the financial crisis, the bank didn't see any spike in its net charge-offs. More recently, in the first quarter of this year, low oil prices had little impact on loan losses—the annual provision totaled just 0.16% of loans.

That said, there is one big concern about CWB: its focus on western Canada. Alberta accounts for 41% of total loans, and another 35% are in British Columbia. Even though few of these loans are directed at energy producers, the bank's numbers could suffer if Alberta's economy languishes.

Why CWB is better than CNRL

Without doubt, today's oil industry can be described as a war of attrition, and there's one big reason why Canada's producers can win this war: exchange rates. With the Canadian dollar getting cheaper, efficient producers can easily have better economics than their American counterparts. So, even if oil doesn't bounce back right away, Canada's energy patch isn't doomed.

Does that mean you should buy an oil producer? Not at all. Some of these companies have rock-bottom share prices, but that's because they have an awful balance sheet. If oil prices don't bounce back, these companies will likely go bankrupt.

Responsible companies like CNRL are much better positioned. The problem here is a strong share price. To illustrate, the company's stock price is up by about 5% in 2015, even though oil prices have continued to fall. Meanwhile, CWB shares have continued to slide down 15% this year. So, why have CWB shares done so much worse?

To put it simply, CNRL shares are more popular. The company is one of the strongest players in its industry, and many institutional investors have to hold at least some energy companies. It's easy to imagine these investors selling weaker oil producers and buying CNRL shares with the proceeds.

Meanwhile, CWB has become a true victim of investors' fear. Its stock price has slid by 25% over the last year, and now trades at just 10 times earnings. There's definitely more upside from this point. The stock remains a risky pick, but I would argue it's still a better bet than any energy company.

CATEGORY

1. Investing

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1. NYSE:CNQ (Canadian Natural Resources)
2. TSX:CNQ (Canadian Natural Resources Limited)
3. TSX:CWB (Canadian Western Bank)

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