2 Beaten Up Energy Stock I'd Buy With an Extra $5,000

Description

The energy patch is full of battered and bruised former dividend favourites, and most of these companies should still be given a wide berth.

However, some of the names in the sector are starting to look attractive. Here are the reasons why I think investors might want to put **Pembina Pipelines Corp.** (TSX:PPL)(NYSE:PBA) and **Cenovus Energy Inc.** (TSX:CVE)(NYSE:CVE) on their watch lists.

Pembina Pipelines

When it comes to pipeline companies, most investors automatically go to the giants when looking for exposure to oil and gas distributors. Pembina is not a pipeline goliath, but it plays a much larger part in the transportation of Canadian oil and gas liquids than most people realize.

In fact, Pembina carries almost all of the conventional oil and condensate produced in British Columbia, 30% of western Canada's natural gas liquids output, and half of Alberta's conventional crude oil production.

As with other pipeline operators, Pembina has very little direct exposure to movements in commodity prices because the majority of its revenue is earned on a fee-for-service basis. Before Pembina decides to build a new pipeline, it gets long-term commitments from its customers to guarantee the viability of the project.

Pembina currently has nearly $6 billion in secured and committed projects underway. About $1.7 billion should be completed and put into service in 2015, $520 million in 2016, and about $3.7 billion is expected to go into operation in 2017.

This is great news for investors because free cash flow should increase significantly as each project gets completed and goes into service.

Pembina pays an annualized dividend of $1.74 that yields about 4.2%. The shares have dropped more than 20% since the beginning of September and the current price-to-book ratio of 2.5 is attractive compared to its five-year average.

Cenovus Energy Inc.

Cenovus has really taken it on the chin in recent months. The company slashed capital spending a number of times and just raised $1.5 billion in a bought-deal stock issue to shore up its balance sheet.

Throughout the process, Cenovus has maintained its generous dividend, but pundits worry the distribution will have to be sacrificed to preserve capital. If oil prices stay below $50 through 2015, the payout will probably be at risk, but a couple of things should keep it safe in the near term.

Cenovus recently set up a 3% discount for investors who decide to use their dividends to purchase new shares. A strong uptake on the DRIP would lower the amount of cash that actually gets paid out, thus reducing the stress on the balance sheet. Cenovus paid out about $800 million in dividends in 2014, so a 30% DRIP participation could save $240 million.

Another potential gain could come from the refining operations. Recent changes in the “crack spread” could make the company earn much better margins. The crack spread is the price differential between the crude oil that enters the refinery and the products the company creates through the refining process.

In its 2015 corporate guidance report released on January 28, Cenovus said it expects the Chicago 3-2-1 crack spread for 2015 to average US$11.75 per barrel. The company also says a US$1 increase in the crack spread would add $90 million in cash flow.

TD Securities analyst Menno Hulshof recently pointed out that current crack spreads are much higher than the guidance rate and cash flow from the refining operations could come in better than expected in 2015 if the differential remains elevated.

Should you buy?

Volatility is likely to continue in the oil market and these stocks could easily retest recent lows. However, if you believe oil prices are headed higher by the end of the year, Pembina and Cenovus offer attractive dividends and a shot at some big capital gains.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:CVE (Cenovus Energy Inc.)
2. NYSE:PBA (Pembina Pipeline Corporation)
3. TSX:CVE (Cenovus Energy Inc.)
4. TSX:PPL (Pembina Pipeline Corporation)

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