



3 Reasons Investors Should Be Nervous About Crescent Point Energy Corp.

Description

In the past few weeks I have been diving deep into dividend stocks, trying to find ones that I think are a worthy investment for you to purchase. Along the way, I found a company that makes my greed kick in, but my rational side run away. When companies have high yields, it can easy to fall into the greed trap, but it's important to dig a little deeper.

Crescent Point Energy Corp. (TSX:CPG)(NYSE:CPG) is one of the top producers of oil and natural gas in North America. And it is one of the top paying stocks in Canada, which has many investors biting at the bit. But there are underlying problems that should make long-term investors very nervous.

The payout is too high

If we look at last quarter's results, the company reported a \$46 million loss. To top it off, its free cash flow was negative \$170 million. Between these two numbers, one would expect that the company might have to cut its dividend.

But it hasn't, and that has me very nervous because the company is paying out over 200% its earnings in dividends. With a yield of 9.29%, it's earning investors a significant amount of money, but it's not sustainable. The company lost money because of low oil prices and as time goes on, that could get worse.

Hedging shields the real problem

What's amazing is that Crescent Point was able to do as well as it did last quarter—which wasn't good at all—because of a strategy called hedging. In essence, you sign contracts well in advance for a predetermined number. If the price goes above that the company misses out on revenue. If the price goes below that contractual number, the company ensures it keeps making as much money as it can.

It has a significant percentage of its oil hedged for over \$80 a barrel for 2015. That means that it is making over \$20 more per barrel than other suppliers. But when 2016 hits and oil prices remain this low, buyers aren't going to be willing to pay more money for oil if they don't have to. That could have a significant impact on the business. If it has to suddenly start generating revenue at the \$60 a barrel

price rather than \$80, it may not be able to succeed.

Its debt is unsustainable

Part of how the company is able to pay its dividend is by taking out debt. In the last quarter, net debt increased by 53.1% to \$3.54 billion. The company took on \$500 million in debt last quarter and then took an additional \$300 million in April.

These numbers are unsustainable. While interest rates are low now, the company could experience the perfect storm in which oil prices don't go up, but interest rates do go up, and then the company is in trouble.

Dividends could get cut

I'm not going to predict if/when the dividend gets cut, but if the perfect storm happens, the company has no choice: it can't borrow its way out of its problems forever.

There is only one way that the dividends don't get cut, and that's if the price of oil jumps up again and stays consistently at high levels. That will allow the company to generate significant returns on investment, which should allow it to keep paying the dividend. But if that doesn't happen, Crescent Point makes me very nervous for investors.

CATEGORY

1. Energy Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:VRN (Veren)
2. TSX:VRN (Veren Inc.)

Category

1. Energy Stocks
2. Investing

Date

2025/09/09

Date Created

2015/05/14

Author

jaycodon

default watermark