# Canadian Natural Resources Ltd. vs. Encana Corporation: Which Is a Better Investment?

## Description

The recent reversal in oil prices is sending energy stocks back toward their 12-month lows, and contrarian investors are wondering which names offer the best shot at some long-term gains.



**Canadian Natural Resources Ltd.** (TSX:CNQ)(NYSE:CNQ) and **Encana Corporation** (TSX:ECA)(NYSE:ECA) are big players in both oil and natural gas, and the two companies often come up as top picks for a recovery in the energy space.

**Canadian Natural Resources**

Canadian Natural Resources is regularly cited as the company with the best asset portfolio in Canada's energy patch. The majority of the properties are located in western Canada, including vast land holdings in the liquids-rich region of northeastern British Columbia. The company is one of the region's largest natural gas producers and also holds substantial light oil, heavy oil, and oil sands resources.

Management prefers to control 100% of the assets instead of working with a partner. This strategy comes with higher operational risks, but it also gives the company greater flexibility to move capital around when market conditions change.

Over the past year, Canadian Natural Resources has done a good job of managing expenses. In Q1 2015 the company reported a 22% drop in year-over-year operating costs on its liquids production and a 10% drop in expenses on the gas side.

Despite heavy capital cuts, the company still expects to deliver 11% production growth in 2015.

Canadian Natural Resources actually increased its dividend in the first part of this year. The current distribution yields about 2.8% and should be very safe.

**Encana Corporation**

Encana is in the middle of a large transition from being primarily a natural gas company to a big player in the oil space.

The oil rout arrived at exactly the wrong moment for Encana. Management dumped natural gas properties at low prices and made a couple of expensive oil acquisitions before the collapse in crude prices.

Despite the unfortunate timing of some of its deals, Encana has amassed an impressive asset portfolio in four of the sector’s top regions: Montney, Duvernay, Eagle Ford, and Permian.

The leadership team is doing a good job of staying focused on the task at hand and the results have been encouraging in a difficult market. Year-over-year liquids production rose 13% in Q1 2015, resulting in a 31% jump in cash flow.

While progress is being made, the continued weakness in oil and gas prices is cause for concern. Encana’s cash flow guidance of $1.6 billion for 2015 is based on the company receiving an average WTI price of $50 per barrel and average NYMEX natural gas prices of $3 per million British thermal units (MMBtu).

Oil traded well above the guidance number through Q2 and is still slightly above $50. Natural gas hasn’t fared as well, trading mostly lower than the target price.



The company plans to spend $2 billion this year on capital projects, so there is likely to be a cash shortfall, and that still doesn’t cover the dividend.

Encana raised $1.44 billion in March to give it some breathing room and to pay down near-term obligations, but the company still finished Q1 with $5.9 billion in long-term debt. Most of the remaining debt isn’t due for quite a while, but it’s a heavy burden to carry if the market doesn’t rebound as fast as some pundits expect.

**Which stock is a better bet?**

A recovery in oil and gas markets will send both stocks significantly higher and Encana’s upside potential is probably greater given the fact that it has taken a far greater beating than Canadian Natural Resources.

However, Canadian Natural Resources has a better balance sheet, and management expects to have enough operating cash flow to cover its capital outlays and dividend through 2015.

If oil and gas prices continue to remain weak and stay depressed for an extended time, Encana’s cash flow situation is going to be an issue. The dividend would be at risk and the company could actually find itself in the sights of a bigger player like Canadian Natural Resources.

At this point, Canadian Natural Resources is probably a safer bet.

**CATEGORY**

1. Energy Stocks
2. Investing

**POST TAG**

1. Editor's Choice

**TICKERS GLOBAL**

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2. TSX:CNQ (Canadian Natural Resources Limited)

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