Is Canadian Natural Resources Limited Still a Safe Dividend Pick?

Description

The rebound in oil prices is bringing money back into the energy sector, and investors are wondering where the best opportunities lie. One name that often comes up is **Canadian Natural Resources Limited** (TSX:CNQ)(NYSE:CNQ).

Let’s take a look at the current situation to see if the company deserves to be in your portfolio.

Dividend safety

Canadian Natural Resources surprised the market earlier this year when it raised its payout. At the time, most of the company’s peers were slashing their distributions.

Investors saw the move as a vote of confidence in the cost-cutting program as well as the company’s ability to quickly reduce its capital program while maintaining strong production.

As oil prices rallied during the second quarter, the stock got a nice lift, and investors expected Canadian Natural Resources to deliver reasonable Q2 results, but that didn’t happen.

The company reported a Q2 loss of $579 million. Management blamed the ugly number on Alberta’s 20% tax hike and said earnings would have been $174 million without the rate increase. The higher tax bill isn’t the main issue.

Canadian Natural Resources delivered Q2 cash flow from operations of $1.5 billion and spent $1.3 billion on capital projects, so the company adequately covered the investments needed to keep the company operational.

The concerning number for investors is the $503 million the company paid out in dividends because the $300 million gap had to be paid with borrowed money.

Oil prices have dropped significantly over the past two months, so cash flow is likely to be a lot lower in the current quarter than it was in Q2. At this point, investors should start to brace themselves for the possibility of a dividend cut.

The quarterly distribution of $0.23 per share currently yields 3.3%.

Asset portfolio

Canadian Natural Resources owns an impressive portfolio of assets. The company is one of western Canada's largest natural gas producers and controls a diverse collection of heavy oil, light oil, oil sands, and gas liquids properties located in several provinces as well as the North Sea and offshore Africa.

Because Canadian Natural Resources owns 100% of most of its properties, it has the flexibility to move capital to the best performing projects. This is important for investors because it means all the eggs are not in one basket. For example, Canadian Natural Resources could decide to move capital out of Alberta and focus more on its properties in British Columbia.

Cost reductions

The company is doing a good job of reducing expenses. During the second quarter Canadian Natural Resources reduced oil sands costs by 20% and its offshore Africa production costs fell 25% compared with Q2 2014.

Should you buy?

Due to its size and strong balance sheet, Canadian Natural Resources should survive the oil rout and investors could see management go on a buying binge in the next 12 months as troubled competitors start to sell off assets.

If you believe in the oil story and are looking for a long-term bet in the energy sector, Canadian Natural Resources is probably one of the safer choices, but near-term risks remain and the dividend could be cut before the end of the year. At this point, it might be best to wait for the Q3 numbers to come out before starting a position in the stock.

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Date
2025/09/09
Date Created
2015/09/08
Author
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