Is Encana Corporation or Cenovus Energy Inc. a Better Oil Bet?

Description

Encana Corporation (TSX:ECA)(NYSE:ECA) and **Cenovus Energy Inc.** (TSX:CVE)(NYSE:CVE) used to be one big company. Today, investors are wondering which half of the former energy giant is best positioned to survive the oil rout.

Let's take a look at the two companies to see if one deserves to be in your portfolio.

Encana

Back in 2009, Encana spun off its oil business into what is now known as Cenovus. At the time, Encana's management team wanted to focus on being a natural gas company and the decision looked reasonable. Natural gas prices were still strong and oil prices lingered at low levels.

Over the next couple of years, gas supplies surged on the back of shale production, driving natural gas prices to near-record lows. At the same time, oil prices soared.

The board brought in a new management team in 2013 that decided to reverse course and make Encana an oil company once again. This decision has also proven to be ill-timed. Crude prices plummeted through the back half of 2014 just after Encana paid premium prices to get into the oil game.

The overall result has been a disaster for shareholders. In early 2010, just after the split, Encana traded for about $36 per share. The stock has pretty much been on a downward trend ever since and now sells for $9 per share.

Management remains committed to its strategy and is doing a good job of keeping the company solvent as it battles through the oil rout and executes the rest of its transition.

Unfortunately, things still look a bit scary.

Encana finished Q2 2015 with US$500 million in cash and cash equivalents and US$6.1 billion in long-term debt. That's not great considering the company has a market value of about US$5.8 billion.

The company just announced a US$1.3 billion sale of its natural gas assets in Louisiana, so that should help take some pressure off the balance sheet, but there is a bigger concern—cash flow.

The company says it is on track to bring in cash flow of US$1.4-1.6 billion in 2015. The first half of the year delivered US$676 million, just short of the halfway mark for the lower end of guidance. Oil prices have weakened significantly since the end of June, and gas isn't doing that great either. It's possible that the company won't hit the low end of its guidance.

At the same time, capital expenditures are expected to be US$2-2.2 billion this year. The company spent just under US$1.5 billion in the first six months, so Encana will really have to tighten its belt to keep capex under the target.

Cenovus

Cenovus is primarily known as an oil sands producer, but it also has a large refining operation. The midstream assets give the company a nice alternative revenue source to help offset weakness in the production segment.

Cenovus is also having a bad year, but it is in better shape than its former parent. The company recently sold its royalty land holdings for $3.3 billion, giving Cenovus ample cash to weather the slump.

Management is doing a good job of bringing down costs while boosting production, and even managed to generate $120 million of free cash flow in the second quarter.

Cenovus recently bought a crude-by-rail loading facility. This will help the company bypass the pipeline bottlenecks and move its oil to the refineries in the United States. Cenovus also just received a licence to export oil from the U.S.

Which should you buy?

Both stocks are still risky bets, but Cenovus looks like the safer play right now. If you are an oil bull and willing to take a chance on a big gain, Encana might have more upside potential, but things could get really ugly if crude prices are headed to new lows.

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