



Should Investors Bet on Husky Energy Inc.'s 5.4% Yield?

Description

Husky Energy Inc. (TSX:HSE) is reporting its third-quarter earnings results on Thursday. The fallen oil prices have been unkind to the energy company. Its shares have fallen over 38% from a 2014 high of \$36 to \$22. Should investors consider its shares today? First, let's take a look at Husky Energy's business.

The business

Husky Energy is one of the bigger integrated energy companies. It has upstream and downstream operations around the world. Specifically, it operates in Canada, the United States, and the Asia Pacific Region.

With major projects behind it, Husky Energy is shifting capital spending towards short payback opportunities.

Assets

Its thermal portfolio continues to expand. Annual heavy oil production made up 21% of total production in 2010 and grew to 45% of production in 2014, or roughly 121,000 barrels per day (bbls/d). Its thermal portfolio requires low sustaining capital of \$5-7 per barrel, and it has a project life of 14 years.

In 2014, its downstream business contributed close to half of its net earnings. Its growth areas include the Asian Pacific Region, which has some gas projects coming online between 2017 and 2019.

As well, its Sunrise Energy Project in the oil sands is producing 11,000 bbls/d, but is ramping up to 60,000 bbls/d near the end of 2016. The Sunrise project life is roughly 170 years with production of 60,000 bbls/d. Operational efficiency in the Sunrise project has improved by reducing drill time by 40%, reducing its footprint by about 40%, and reducing its capital costs by a third for each pad.

Husky Energy's third growth area is the Atlantic Region, where a new basin was discovered in Flemish Pass. The 18-month delineation program is expected to be completed by April 2016.

Balance sheet strength, valuation, profitability, and dividend

Husky Energy maintains a solid balance sheet. It has been awarded an S&P credit rating of BBB+, which is investment grade. Further, it can access \$3.4 billion unused credit facilities if needed.

At about \$22 per share, Husky Energy is trading at a price-to-book ratio of 1.1. Although, it's not quite at its book value of \$20.3 yet, the shares are the cheapest in a decade based on that metric. Probably for good reason.

Its operating margin has declined dramatically from 2013's 11% level to its trailing 12-month (TTM) 2% level. In the same time frame, revenue declined by over 12%.

Husky Energy has maintained a quarterly dividend of 30 cents per share since cutting it from 50 cents per share in 2009. It yields 5.4% today. The company only managed to scrape 28 cents of TTM earnings per share, which is not enough to sustain the annual payout of \$1.20 per share. If commodity prices stay low, Husky Energy may have trouble paying its dividend.

In conclusion

I'm not encouraging the timing of the market, but around earnings report time, the market can get especially emotional about a company. Husky Energy could go up or down 5% in one day.

Since commodity prices have stayed low, Husky's revenue and earnings will likely to stay down, even with its higher production. So, there's no rush for investors to buy the shares today.

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kayng

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