Crescent Point Energy Corp. Would Be Better Off Without its 8% Dividend

Description

Crescent Point Energy Corp. (TSX:CPG)(NYSE:CPG) has always been popular among dividend investors, and it's easy to see why. The company been one of the highest-yielding stocks on the **S&P/TSX 60** for a long time, and its dividend still yields roughly 8%, even after being slashed by over 50% in August.

Yet for a long time this dividend has been more of a curse than a blessing. We explain why below.

Before the crash: a drag on returns

Even when oil prices were elevated, Crescent Point's $0.23 monthly dividend was higher than the company's free cash flow. So how exactly did Crescent Point afford the dividend?

Well, the company employed a so-called dividend reinvestment plan, under which shareholders received a small incentive for taking their dividends in shares instead of cash. At the same time, Crescent Point made numerous acquisitions, funding them mainly with equity.

As a result, the share count grew like a weed from 125 million at the end of 2008 to 446 million by the end of 2014.

Crescent Point was performing well operationally, and its stock price was outpacing the company's peers. If the company didn't pay out such a big dividend, then more cash could have been spent on growing production, and the company's success would have been spread out over fewer shareholders.

During the crash: wrecking the balance sheet

Because Crescent Point had used equity to finance its acquisitions, its balance sheet was still in strong shape entering 2015. But as the year progressed, dividend payments once again outpaced cash flow, forcing the company to issue new debt.

Then in May, Crescent Point issued another 20 million shares to help pay for its Legacy Oil + Gas acquisition. Of course these new shares came with dividend requirements as well. All of a sudden, Crescent Point's debt load had ballooned from $3.2 billion to $4.0 billion in just six months. The dividend was much to blame.

Looking ahead: the wrong use of cash

As oil prices continue to slump, we are quickly seeing a divergence between the haves and the have-nots. The haves are taking full advantage of the downturn by developing projects at lower cost and pouncing on weaker competitors. Meanwhile, the have-nots (those with poor balance sheets) are struggling for survival and are trying to sell assets into a market with few buyers.

Crescent Point could have been one of these strong companies. It could have used its balance sheet to prey on weaker rivals or grow production very cheaply. But instead its money has gone towards the dividend, and when looking ahead, that is unlikely to change.

Oddly enough, Crescent Point would be doing its shareholders a favour by scrapping the dividend altogether. However, if history is any guide, this will not be done for as long as possible.

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