Will These 3 Energy Companies Survive 2016?

Description

Many investors in the energy sector find themselves in an interesting conundrum.

On the one hand, it seems obvious the true value for crude oil is more than $30 per barrel. Just take a look at each oil producer's cost of production if you don't believe me. There aren't many who are breaking even with prices so depressed.

So there's value in the sector. The main issue is finding it. Every energy company needs the price of crude to recover. Some just need it to recover more than others.

Unless crude recovers substantially at some point in 2016, there will be casualties. We might think that $40 or $50 for oil is cheap, but those numbers represent a 27.3% or 59.1% increase from today's price. Oil is volatile, so a recovery into the $50 range by the end of the year is possible. I'm just not sure it's something investors should count on.

There are risky ways to play the recovery in energy and safer ways. Betting on a company that needs oil to recover in a hurry might result in some very nice upside. But it also could mean losing your whole investment. That's not the risk/reward ratio I like to see.

Here are three energy companies that are hoping and praying for higher crude prices in 2016. Their very survival could hinge on it.

Penn West

I sold my **Penn West Petroleum Ltd.** (TSX:PWT)(NYSE:PWE) shares a few weeks ago. The thought process was simple.

If crude stays in the low $30 range, it's going to be very difficult for Penn West going forward. The company is dependent on asset sales to help shore up its balance sheet, and the longer prices stay low, the worse it'll be in terms of getting top dollar for these assets. That's assuming there's even a market for them.

Two recent sales helped to get Penn West's debt down from $2.4 billion to $2.0 billion, which is a nice start. But with production falling and capital expenditures cut to the bone, it's easy to envision a scenario where Penn West can't even generate enough in funds flow to pay the interest on its debt.

The company is forecasting barely positive funds from operations with crude at $40 per barrel. At $31 per barrel, things aren't good.

Precision Drilling

Precision Drilling Corporation (TSX:PD)(NYSE:PDS) picked the wrong time to lever up its balance sheet. At the end of 2013 it had $1.3 billion in debt. At the end of September, that number has ballooned to more than $2.1 billion.

Precision Drilling does have a few advantages. It has some $400 million in the bank. It's on pace to be approximately free cash flow neutral in 2015 (fourth-quarter results aren't out yet), and it still has a relatively healthy backlog of contracts for 2016.

But as we saw with the offshore drillers in 2015, customers will find a way to wiggle out of these contracts if the numbers don't work. If this happens on a large scale, it's very bad news for Precision Drilling.

Lightstream

Oh, how **Lightstream Resources Ltd.** (TSX:LTS) has fallen. Just 18 months ago the stock was flirting with $9 and paid a $0.04 per share monthly dividend. These days shares trade at just $0.34 each.

Lightstream's biggest problem, like so many others in the sector, is debt. It owes more than $1.5 billion while on pace to post only about $200 million in funds flow in 2015. And that amount will likely go down in 2016, barring a big recovery in the price of crude.

Lightstream is also looking to sell assets, officially putting its Bakken assets up for sale in 2015. Even though the area is highly regarded in the industry, there has been little interest thus far. There's a glut of property for sale, and suitors might be waiting for Lightstream to officially declare bankruptcy, taking their chances to buy the assets then.

Without a major sale, Lightstream might not survive 2016. It's that simple.

CATEGORY

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TICKERS GLOBAL

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