These Oil Companies Almost Drilled Their Own Graves in 2015

Description

Despite the fact that the oil industry was vastly oversupplied heading into 2015, most oil producers chose to invest to grow production last year. That made a bad problem grow worse, which is why oil has continued to crater. Here's a look at a couple of oil companies that nearly drilled their own graves.

Keeping the foot on the accelerator

Even though the oil market remained chronically oversupplied all year, **Enerplus Corp.** (TSX:ERF)(NYSE:ERF) didn't do much more than tap the brakes on production growth in 2015. Sure, the company slashed its capital spending by 39% over what it spent in 2014, but its production was still 3% higher year over year to 106,524 barrels of oil equivalent per day (BOE/d) and above its own guidance.

Further, that number would have been even higher if it wasn't for the fact that it sold a number of assets during the year, which actually reduced its annual average by roughly 1,300 BOE/d. Not only that, but the company grew its oil production by a much faster rate with overall oil production up 6% year over year, fueled by 28% higher oil production in the Bakken Shale, despite the fact that the world had more oil than it knew what to do with last year.

The big problem with Enerplus's production push last year was the fact that it spent every dollar it brought in with capex of $493 million exactly matching funds flow of $493 million. Because it used every dollar it had to drive growth, it has less cash to work with this year.

That's why the company is cutting deeply into capex spending this year, slashing it by 60% to just $200 million. As a result of that steep drop in spending, its production is expected to fall to a range of 90,000-94,000 BOE/d, which is down 7% at the mid-point and adjusting for 8,000 BOE/d in asset sales.

Suffice it to say, growing in 2015 not only didn't pay off, but was a complete waste, seeing how production is now projected to decline back to what it was before the year started.

Continuing to grow the core

Encana Corporation (TSX:ECA)(NYSE:ECA) was another company that kept its foot on the production accelerator last year, growing production from its core plays by 35%, exceeding its own production guidance. Though, due to asset sales and declining natural gas production, overall production fell 15% to 405,900 BOE/d.

That core growth didn't pay off, and now Encana is paying the price. The company recently announced a major cost reset. The company is cutting its workforce by 20%, reducing its dividend from $0.07 per share to a paltry $0.015 per share, and it's making another reduction to capex.

In fact, the new capex plan is to spend between $900 million and $1 billion, which is 55% less than it spent last year. That along with more asset sales will cause its overall production to fall to a range of 340,000-360,000 BOE/d this year.

Encana's focus on growing in 2015 not only forced it to make steep spending cuts in 2016, but it hurt the company's credit rating, which was recently downgraded to below investment grade by its credit rating agency. That downgrade was made because its rating agency is concerned is that if conditions worsen, Encana might not be able to meet its financial obligations in the future.

Clearly, growing in 2015 wasn't the best plan.

Investor takeaway

Growth for the sake of growth hasn't done either of these two companies any favours during the downturn. Not only is the oil glut worse, but these companies drilled a big hole into their financial position. In fact, if conditions continue to worsen, the growth that both companies pushed for in 2015 could be what causes their demise.

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