Revealed: These 3 Cheap Oil Stocks Have Massive Potential Upside

Description

Many investors want to participate in what they view as oil's inevitable recovery. They just don't know the best way to do it.

Many are choosing to be cautious, putting their capital to work in the largest names. Because of this, shares of the behemoths of the sector–companies like **Suncor Energy**, **Imperial Oil**, or **Canadian Natural Resources**–haven't really declined as much as their weaker peers. Investors value the safety of these big players' balance sheets, their rock-solid dividends, and their diverse operations.

For investors looking for safety, I can see the logic in buying these big names. But for folks looking for the kind of upside that can really make a difference in a portfolio, perhaps a different strategy would be best.

There are dozens of oil producers who have massive potential upside. These stocks are risky–that much is obvious. They desperately need the price of crude to improve in a hurry. The recent move up from $26 per barrel to $38 per barrel sure does help, but we need to get back to the $45-50 range for many producers to really be out of the woods.

Here are three energy producers that could double … triple … or even more if crude continues its march upwards.

Pengrowth

Pengrowth Energy Corp. (TSX:PGF)(NYSE:PGH) is suffering from the same problem that's plaguing many of the other medium-sized producers–debt. At the end of 2015 the company owed $1.86 billion compared to total equity of $1.76 billion.

But it is taking steps to get the balance sheet under control. It cut the dividend to just $0.04 per share annually before suspending it completely in January. It started getting aggressive with hedging. Capital spending was cut to the bone. And the company sold some non-core assets.

Like many other producers, Pengrowth will see production slip in 2016. The company was able to pump out in excess of 70,000 barrels per day of crude in 2015, which will slip to approximately 60,000 barrels per day this year. But even at that lower production, the company thinks it can put almost $600 million towards the debt in 2016. Half will come from cash flow and the other half will come from asset sales.

Pengrowth is risky if crude doesn't recover. Internal forecasts made by management say that if crude stays at $30 per barrel for all of 2016, the company will be very close to breaching debt covenants by the end of the year.

Athabasca

Athabasca Oil Corp. (TSX:ATH) is in a somewhat unique position. It's actually sitting on a lot of cash–some $560 million at the end of 2015. It also announced a joint venture with **Murphy Oil** that will inject another $250 million into the balance sheet. Once the joint venture closes, Athabasca will be sitting on a small net cash position.

Athabasca is an asset play. It owns significant reserves in both the Montney and Duvernay areas as well as a thermal oil play in northern Alberta, the Hangingstone project. Hangingstone is producing some 8,000 barrels per day with the potential to eventually ramp up the project to 80,000 barrels per day. Between the three major production areas, Athabasca has proved and probable reserves of 290 million barrels of oil.

Athabasca has a current market cap of $445 million, meaning investors are paying less than $2 per barrel of oil in the ground. It seems to me that's a pretty fair price to pay.

Penn West

Penn West Petroleum Ltd. (TSX:PWT)(NYSE:PWE) is probably the riskiest name of the three. Crude needs to recover to at least $45 or $50 a barrel for Penn West to no longer be in danger of bankruptcy.

With great risk comes the potential for great rewards. Shares hit $3 each in April 2015 when crude traded around $60 per barrel. Crude is just under $40 as I type this, meaning Penn West easily has 100% potential upside if crude goes up 50%. That's the kind of reward investors should want for taking on the risks associated with Penn West.

Management is doing everything possible to stave off bankruptcy, too. The dividend has been eliminated. Capital expenditures have been slashed to almost zero. And all sorts of different assets are on the auction block. The company is also negotiating with lenders to make sure it can get some leeway just in case it breaches debt covenants.

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Author
nelsonpsmith