



## Encana Corporation Has a Secret Plan for Growth

### Description

**Encana Corporation** (TSX:ECA)(NYSE:ECA) has been positioning for a prolonged downturn by selling assets, shedding its workforce, reducing its dividend, and lowering spending. Considering it still has \$5.4 billion in debt and posted a \$5.2 billion loss last year, Encana doesn't look like a company with too many opportunities to create shareholder value.

Fortunately, the company's management team has found a fairly unique way to boost long-term returns.

#### An instant 50% return

**Moody's Corporation** cut the company's credit rating below investment grade in February, citing a "material decline in Encana's cash flow" in 2016 and 2017. Rating downgrades often don't predict the future of a business, but they typically raise borrowing costs in the short term. According to *Bloomberg*, "many funds can't hold high-yield notes, so a cut from investment grade to junk could trigger a wave of selling."

To take advantage of its discounted debt, which traded as low as 60 cents on the dollar, Encana bought back as much as \$250 million of its own bonds last month. Not only does the company not have to pay interest on these bonds anymore (they were yielding over 13%), but it no longer needs to pay back the par amount upon maturity. Effectively, Encana experienced an immediate 40-50% return on investment plus the savings in interest.

The company has mainly been buying back bonds due in 2019 and 2021. Because over 75% of long-term debt isn't due until at least 2030, Encana will be in an enviable position if it can continue buying back near-term debt. It also still has access to \$3.5 billion in fully committed, unsecured, revolving credit facilities. Encana would be wise to use up as much capital as possible by repurchasing debt at attractive discounts.

Don't be surprised to see more oil and gas companies take this route. According to *Bloomberg*, "about 20% of \$108 billion of energy company bonds in the country trade below 80 cents on the dollar."

## What's next?

On the business side, executives are positioning the company well for an ultimate turnaround.

Its capital budget is now focused on just four core areas (Eagle Ford, Permian Basin, Montney, and Duvernay), allowing its production profile to slowly shift towards oil rather than natural gas. By 2018, natural gas will likely comprise less than 50% of production, down from 82% in 2014. If the company can unload any of its natural gas assets in the meantime, it could transform itself into an oil producer fairly quickly, resulting in a more profitable business.

In addition to asset sales, Encana is also reducing its workforce by 20% for the second time in six months. The latest job cuts will bring total workforce reduction to more than 50% since 2013.

Encana still needs oil prices to rebound to ensure long-term viability, but it's looking like a great option for patient investors looking to bet on oil markets rebalancing over the coming years.

## CATEGORY

1. Energy Stocks
2. Investing

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