Why I Remain Bullish on Parex Resources Inc. Despite Weak Oil

Description

The recent bounce in oil prices coupled with the fact that a number of notable institutional investors and fund managers are claiming that the bottom is finally in for crude has triggered considerable interest in energy stocks. This makes now the time for investors to start dipping their toes in the water and adding energy stocks to their portfolios.

One company that stands out is Colombian-based intermediate oil producer **Parex Resources Inc.** (TSX:PXT). Not only has it endured the oil slump reasonably well (its share price is up by 32% over the last year), but it has a number of characteristics that will help it emerge from the current harsh operating environment in better shape than when it went in.

Now what?

Key among Parex's growth catalysts is its high-quality asset base with 82 million barrels of oil reserves that are majority weighted to oil and located in Colombia's proven Llanos Basin.

More impressively, the company reported a reserve replacement ratio of 232% for 2015 and boosted its oil reserves by 19% year over year. This follows Parex's continuing investments in exploration and development activities at a time when the majority of energy companies have slashed spending on those activities.

I expect such strong growth to continue. Parex has budgeted US$165 million in capital expenditures for 2016 with US$115 million earmarked for exploration and development activities.

Importantly, given the harsh operating environment, this program will be self-funded, ensuring that Parex's pristine balance sheet remains untouched.

Not only will this investment help to sustain production, but it will ensure that Parex's oil reserves and output continues to grow, leaving it well positioned to take advantage of higher oil prices when they eventually rebound. This is in stark contrast to a number of oil companies, such as **Penn West Petroleum Ltd.** and **Baytex Energy Corp.,** that lack sufficient cash resources to develop their assets in order to offset natural decline rates.

As a result of this investment, Parex expects 2016 oil production to grow by 10% to 30,200 barrels of crude daily, leaving it well positioned to cash in on any recovery in the price of oil.

Parex is also capable of generating solid margins for each barrel of crude it produces. It has forecast a 2016 cash netback per barrel of US$7 if Brent averages US$40 over the year, and this rises to US$15 if Brent averages $50 for that period.

Then there is Parex's balance sheet. With no debt and a high degree of liquidity, it is not only capable of surviving the current operating environment, but it possesses considerable financial flexibility that will allow it to take advantage of low asset prices and expand its operations.

Another positive catalyst is Colombia's improving security situation that should continue to improve. Major guerilla groups, the FARC and ELN, are in peace negotiations with the government. This will mean lower security risk and less costly production outages caused by guerilla attacks on oil pipelines. It should also see Parex's transportation costs fall as it will have to use costly road transportation to transport its crude to the market less frequently.

So what?

Parex offers investors one of the best levered plays on the eventual rebound in crude because, unlike many of its similar-sized peers, it continues to invest in exploration and development. This means that its oil reserves and production will continue to grow, allowing it to take full advantage of any increase in oil prices.

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1. Energy Stocks
2. Investing

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1. Editor's Choice

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