



Here's Why Penn West Petroleum Ltd. Popped 50%

Description

Once on the brink of bankruptcy, **Penn West Petroleum Ltd.** (TSX:PWT)(NYSE:PWE) surged as much as 50% this Monday off some major news. The company has agreed to sell its Viking assets to Teine Energy Ltd. for \$975 million. The deal should help reduce Penn West's onerous debt load by more than \$600 million. The company is now left with its valuable Cardium property as its major asset.

Is Penn West back from the dead?

Wall Street approves

Already, Wall Street analysts are fawning over the deal.

"The sale is a definitive step which will help to change the narrative from constant discussions around its debt toward constructive conversations around Penn West's recent performance its remaining Cardium area," said Jeremy McCrea, an analyst at Raymond James. "The Penn West that ends 2016 will be very different than the Penn West that entered 2016."

While it had been at risk of default by next quarter, Penn West now expects to remain within its financial covenants through 2016.

Encouragingly, it appears as if Penn West's balance sheet isn't that overvalued—an important thing to note given its future bankruptcy risk will hinge on the value of its assets versus its liabilities.

For example, last quarter Penn West valued its Viking reserves at \$899 million, comprising 26% of its total asset base. Over the entire life of the project, it estimated that the cumulative undiscounted cash flows would amount to \$3.4 billion. The recent sale should give the market significantly more confidence that the company isn't overstating the value of its other assets.

How much could shares be worth?

Previously, Penn West was bet on continued solvency, not the ultimate underlying value of its assets. Now that bankruptcy risk has been tabled for a few quarters, how much could shares really be worth?

After the transaction closes, Penn West's Cardium project should comprise about 70% of its asset base. With a listed balance sheet value of \$1.7 billion, the property alone could be worth double Penn West's current market cap, not to mention its \$700 million in additional listed assets. If it can continue to survive, shares could have plenty of upside, especially if oil markets continue to rebalance.

The company's latest deal has a transaction value of \$71,400 a barrel per day. If it can hit its production estimate of 50,000 barrels a day this year, the stock would currently be trading at under \$42,000 a barrel per day, implying plenty of room to grow.

Penn West's management team has done something very rare: it has transformed a near-bankrupt energy producer into a focused, low-cost producer. While there is still a risk that the deal doesn't close, investors can believe that the 50% pop is here to stay.

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