



Why Crescent Point Energy Corp. Is a New Company (and Shares Are Set to Show it)

Description

Back in 2014, an article in *The Global and Mail* summarized the dilemma with **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG). The article interviewed several wealth managers, all of whom had similar complaints about the stock: the company was funding a series of expensive acquisitions with equity (an annual occurrence), had a dividend that was 5.5 times free cash flow in 2014 (a large part of which was funded by its DRIP program), and was not growing production using cash flow.

The result of the equity financing and dividend funding through the DRIP program was that Crescent Point shares outstanding skyrocketed from 388 million in 2013 to an expected 518 million this year and 542 next—a 40% hike in three years.

While Crescent Point recently committed to a new strategic focus of living within its cash flow, focusing on organic growth, and making small acquisitions, a recent move to issue \$650 million of equity to fund organic growth capex has investors punishing Crescent Point once again.

Analyst and shareholder Christine Poole on *BNN* recently stated that the move was disappointing, that she and other shareholders were hoping Crescent Point would hold off on issuing equity, and that this could serve as an overhang on the stock for some time.

The equity issue is not a return to the old strategy

Crescent Point is currently trading at a discount according to several different measures, and this is an opportunity, especially as the market comes to realize that Crescent Point is actually committed to its strategic shift and the recent move is not evidence against this.

What kind of discount is Crescent Point trading at? Currently, Crescent Point is trading at an EV/DACF of 5.75 compared to its most immediate peer group, which is trading at 8.8. Crescent Point is also trading at a large discount to where it was only a few weeks ago before the news of the equity issue came out—it was trading at about 6.75 on September 8.

Crescent Point has 23% upside if it simply returns to the same valuation it was at before the news of

the equity issue came out. The upside is substantially more if it closes the gap with its peer group and moves up to an EV/DACF of 8.8. Analysts at both **TD Bank** and **Bank of Nova Scotia** view this as a reasonable target.

This will likely happen when the market realizes the move to issue equity is not a return to the old strategy. Crescent Point has actually made plenty of progress in changing its approach. Not only has the company repetitively stated it would be focusing on living within its cash flow, but it has made a series of large dividend cuts to make sure its dividend fits well within projected free cash flow.

The new dividend yield is only around 2% compared to 6% or so historically. The company also eliminated its DRIP program, which means less dilution annually to fund its dividend. Crescent Point has also shown progress towards making smaller, internally funded acquisitions. There were no large acquisitions for Crescent Point in 2016; instead, it made two small acquisitions in its core resource plays that were funded entirely from free cash flow and from the sale of a non-core play in Alberta.

It is also important to look at how Crescent Point is using the funds from its equity issue. The company is primarily using it to boost its production guidance (the old 2017 guidance was 165,000 bpd, and the new guidance is 175,000 bpd).

This accomplishes a few things. Since plenty of Crescent Point's inventory is very economic at US\$45 per barrel, it allows the company to start drilling this inventory in advance of what it would be able to do if it simply funded production through cash flow.

Since even conservative analysts see oil above US\$45 by late 2017, Crescent Point is advancing its production early. As the market begins to see the benefits of this and see Crescent Point sticking to its new strategy, its share price should increase.

CATEGORY

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