2 of Canada’s Top Mutual Funds Own This Stock: Should You?

Description

Royal Bank of Canada’s Mid-Cap Class Advantage fund and Phillips Hager & North’s Small Float fund have been two of Canada’s top-performing mutual funds, posting year-to-date returns of 27% and 23%, respectively. The benchmark, smashing performance of these two actively managed funds has been due in no small part to their positions in **Seven Generations Energy Ltd.** (TSX:VII)–a stock that has returned a staggering 136% in 2016.

For those just hearing about this mid-cap, natural gas player, here are a few pointers to get you up to speed.

A pure play natural gas company in the Montney Basin

Seven Generations is a natural gas energy company focused on acquisitions and developments of high-quality, hydraulic, fracturing-based projects along the Kawka River in the Grand Prairie area. The bulk of Seven Generations’s developments are in the gas-rich Montney Basin, which has some of the lowest breakeven prices for condensate rich gas in North America.

The low cost of production has allowed Seven Generations to ramp up production dramatically, even in the face of slumping energy prices. Moreover, Seven Generations’s cash flow generation has been top notch with funds from operations increasing at 100% compounded annual rate since 2011.

Ex 1. Low breakeven costs at Montney means Seven Generations can weather a prolong slump in energy.

montney-break-even
Image not found or type unknown
Source: Company filings

Ex 2. Seven Generations has shown tremendous production and FFO growth.

7g-production-and-ffo
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Source: Company filings

Accretive acquisition spree

Since its debut on the TSX in 2014, Seven Generations has been busy on the M&A front. In July 2016 Seven Generations acquired Paramount Resources Ltd. in a transaction worth $1.9 billion. The counter-cyclical acquisition is expected to be accretive within a year and will boost Seven Generations's high value acreage by 40% and production volume by 30,000 boe/d.

Along with its acquisition of Paramount, Seven Generations acquired a minority stake in Vancouver-based Steelhead LNG in a joint venture to explore overseas LNG markets. The partnership with Steelhead is expected to be conducive towards Seven Generations's long-term value-creation strategy and could provide access to a variety of alternative natural gas markets.

Latest earnings report reinforces bull case

While EPS in its latest reports came below consensus (-.19 vs. .03), Seven Generations announced production volumes of 117,353 boe/d and funds from operations of $.66/share (vs. $.47 for Q2 2015). The production volume reflected a 33% growth from Q1, while cash flow was significantly higher than consensus figures.

More impressively, the production growth and cash flow generation was largely organic, as capex was at $219 million for the reported quarter–in line with management's Q1 forecast of $900-950 million in expenditures for FY 2016.

Final considerations

Although income investors might skip Seven Generations as it doesn't pay any dividends, it's hard to argue with the tremendous growth story.

Currently, Seven Generations has demonstrated that management can execute production targets even in the face of slumping energy prices. Moreover, Seven Generations has shown tremendous capital discipline while growing its asset base with leverage ratios in line with industry norms.

In summation, if you are looking for a well-balanced and well-managed natural gas play that's just beginning to take off, then look no further than Seven Generations.

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1. Energy Stocks
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