Income and Oil Investors: This Is 1 Yield You Can't Afford to Miss Out on

Description

After months of pointless rhetoric, OPEC has actually agreed to set aside their differences and cut oil production by about 1.2 million barrels per day.

Now before we get the confetti, keep in mind that this deal is contingent upon two key factors: first and foremost, the notoriously covetous cartel members must actually abide by their output ceilings; second, non-member nations like Russia must cooperate on their end and also reduce production.

That being said, if (and it's no small "if") these two conditions are met, we could see the oil market finally re-balance in 2017 and Canada's beleaguered energy sector get a much-needed reprieve.

But none of that really matters for **Vermilion Energy Inc** (TSX:VET)(NYSE:VET–one of the top oil and gas production and exploration companies in the game with assets across Canada, the United States, and Europe.

If you're an income investor looking to play an oil rally, then Vermilion should immediately stand out from its peers thanks to the company's 4.6% yield, which has never been reduced once since inception.

Below, you will find a few reasons why this dividend, which has totaled well over $30/share in the past 13 years, will continue to grow well into the future, regardless of OPEC's machinations.

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Vermilion's dividend performance versus peers. (Source: company filings)

Vermilion boasts one of the safest dividends in the industry

First, Vermilion is a cash-generating machine. And although cash flows took a noticeable hit during the cyclical lows of 2015, the company has significantly ramped up production in the last few quarters and is expected to rebound towards pre-glut levels of FFO by 2017.

vermilion-production-and-ffo-profile
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Significant increase in production means more revenues during an oil turn around. (Source: company filings)

Second, Vermilion's cost-cutting measures have resulted in substantial per-unit cost reductions. For example, Vermilion's estimated operating expenses for 2016 will come in at less than $9 per barrel of oil equivalent (boe), versus $11.8/boe for 2015 and $12.5/boe for 2014–a marked reduction of 27% on an annual basis since 2012.

Third, the cost reduction and increased production means Vermilion's margins remain high with after-tax cash netbacks (the income the company receives from sales after royalties and costs necessary to bring the oil to market) for YTD 2016 at a sector-leading $17/boe.

vet-netbacks

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Some of the best netbacks in the biz. (Source: company filings)

Furthermore, if we take this high netback and divide it by the company's three-year average of proved developing and producing costs, we arrive at an industry-leading recycle ratio of 2.5. This means that when it comes to capital efficiency, Vermilion is able to make, on average, 2.5 times what it spends on finding, developing, and extracting oil–the highest in its class.

vet-recycle-ratio

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Best-in-class recycle ratio. (Source: company filings)

Finally, no dividend analysis is complete without an examination of the balance sheet. Yet again, Vermilion does not fail to impress. Currently, the company has total debt of 2.4 times EBITDA, which is well below the covenant limit of four times EBITDA. Furthermore, its 2017 estimated debt-to-cash flow ratio is just 1.8–well below the Canadian and U.S. averages of 2.2 and 4.7, respectively.

The bottom line

Vermilion has grown its dividend steadily, even in the face of cripplingly low oil prices. Moreover, with the looming rally in oil prices, Vermilion's combination of strong cash flow generation, increased production, lowered costs, high margins, and rock-solid balance sheet mean this yield is one you simply can't afford to miss out on.

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