These Oil Stocks Should Thrive Thanks to OPEC

Description

After a battle of more than two years to grow its market share, OPEC reversed course last month and has decided to focus its efforts once again on supporting market pricing. For some producers, that news could be a life saver because they have struggled to operate at lower oil prices. However, for stronger producers, the agreement likely means they will deliver high-end growth in the years ahead.

Here are two such titans that could thrive thanks to OPEC.

The dramatic turn

Penn West Petroleum Ltd. (TSX:PWT)(NYSE:PWE) almost didn't make it through the downturn. That is because the light oil producer got dangerously close to breaching its financial covenants earlier this year. However, the decision to part with two core assets eliminated its financial problems and positioned the company to thrive at lower oil prices. In fact, Penn West Petroleum estimates that it can grow production by a 10% compound annual rate going forward while living within cash flow at just $50 oil.

However, now that OPEC is back to supporting oil prices, it is much more likely that crude will go higher than $50 a barrel in the future. Because of that, Penn West Petroleum has the potential to generate more cash flow, which provides it with additional options. One option is that it could grow production faster in the future.

For example, at $60 oil the company estimates it can increase output by 15% per year and still generate some excess cash flow. Another option is to redirect some of that excess cash flow back to shareholders by re-instituting the dividend. Either way, Penn West's future just got even brighter thanks to OPEC.

A cash flow gusher awaits

Canadian Natural Resources Limited (TSX:CNQ)(NYSE:CNQ), meanwhile, spent the bulk of the oil market downturn investing to expand its Horizon oil sands facility. Because of that, the company is about to experience a significant increase in free cash flow. For example, in a low-oil-price world, the company could generate $600 million in free cash flow next year, which would grow to $1.5 billion in 2018 upon completion of the final Horizon expansion phase. That cash flow would give the company the capacity to improve its balance sheet or fund several high-return growth projects.

However, at $60 oil the company would generate much more cash flow, which puts it in the position to grow at a higher rate. It estimates that cash flow would rise to $1.4 billion next year, $3 billion in 2018, and $3.5 billion in 2019. Those higher cash flows would enable the company to grow production at an 8% compound annual growth rate going forward.

Further, the company would quickly improve its balance sheet with leverage falling from the current 3.9 times debt-to-EBITDA to a range of 1.8-2.2 times. That would also put the company in the position to return more money to investors either through higher dividends or even share buybacks.

Investor takeaway

Thanks to their efforts over the past couple of years, Penn West and Canadian Natural Resources can thrive at just $50 oil going forward. That said, they would do even better at $60 oil, which is now a much more a likely future oil price thanks to OPEC. As a result, both companies should see more cash flowing into their coffers. Those incremental cash flows give them more options, including accelerating growth or returning some of that money to shareholders.

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